

MINUTES

SOUTH DAKOTA INVESTMENT COUNCIL

Conference Call
February 4, 2016

1) Roll Call

The meeting was called to order at 8:30 a.m. on February 4, 2016 by Chair Jim Means. Council members in attendance were Lorin Brass, Ryan Brunner, David Hillard, Steve Kirby, Laura McNally, Jim Means, Rich Sattgast and Rob Wylie.

Others attending all or part of the meeting included Matt Clark, Chris Nelson, Tammy Otten, Sherry Nelson, and Laurie Riss from the Investment Office; Doug Fiddler, Susan Jahraus, and Travis Almond from the South Dakota Retirement System; Cindy Wellard from Legislative Audit; Mike Lauritsen from School and Public Lands; Nathan Vardi from Forbes; and Elliott Mallen from United Here.

AGENDA ITEMS:

- 1) Roll Call
- 2) Minutes
- 3) Investment Update – FY 2016
- 4) Iran Divestiture & Shareholder Activism Reports – Update
- 5) Appropriations Hearing Review
- 6) Legislation Update
- 7) Audit Committee Update
- 8) Compensation Committee Update
- 9) Lone Star Real Estate Fund V
- 10) Higher Education Savings Plan Update
- 11) Blackstone Real Estate Partners Europe V
- 12) New/Old Business
- 13) Future Meeting Dates
- 14) Adjournment

(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.)

2) Minutes

STEVE KIRBY MOVED, SECONDED BY DAVID HILLARD, TO APPROVE THE MINUTES OF THE NOVEMBER 17, 2015 INVESTMENT COUNCIL MEETING. MOTION PASSED UNANIMOUSLY ON A ROLL CALL VOTE.

3) Investment Update – FY 2016

Tammy Otten reviewed the Motions and Actions Notes which included the staff actions taken on the Council motions made at the November 17, 2015 meeting.

Otten indicated that investment update information would be provided to the Council for their review. The trust funds' distribution calculation would be provided to BFM and LRC using the final December 31 valuations per state law. The equity like risk was reviewed.

4) Iran Divestiture & Shareholder Activism Reports – Update

Otten stated that the Iran divestiture annual report was provided to the Executive Board of the Legislature on January 13, 2016 as required by law. The Council was provided the January 20, 2016 memo that included the most recent scrutinized companies lists from Colorado and Florida compared to the South Dakota list. Staff recommended changing the South Dakota list to include the recent additions to the Colorado list.

LORIN BRASS MOVED, SECONDED BY RYAN BRUNNER, TO APPROVE THE CHANGES TO THE IRAN SCRUTINIZED COMPANIES LIST AS PRESENTED. MOTION PASSED UNANIMOUSLY ON A ROLL CALL VOTE.

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, 2016. She noted that no changes to the policy were needed at this time. Staff recommended the continued use of the Colorado scrutinized company list.

5) Appropriations Hearing Review

Jim Means and Matt Clark discussed the FY 2017 budget hearing which took place with the Appropriations Committee on January 21, 2016. They commented on the good questions on compensation philosophy and investment approach regarding market volatility, as well as the positive support of the legislators and executive branch. There were no follow-up issues with the budget expected at this time.

6) Legislation Update

Otten provided an update on various legislative bills which may be of interest to the Investment Council. Rob Wylie provided an update on the retirement bills, and Matt Clark discussed the potential ABLE legislation. 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.

7) Audit Committee Update

Steve Kirby, Chair of the Audit Committee, reported that the Agreed Upon Procedures review for the quarter ended September 2015 was completed by Legislative Audit and came back clean.

8) Compensation Committee Update

David Hillard, Chair of the Compensation Committee, discussed the conference call the Committee held on January 28, 2016 regarding an update to the compensation study completed in the spring of 2013. As opposed to recommending a full study at this time, the Compensation Committee suggested that Matt Clark purchase the McLagan data and make salary comparisons internally. Hillard noted that if compensation levels are significantly different than the updated targets derived from the McLagan data, the Compensation Committee would likely recommend to the Council a full study be completed.

9) Lone Star Real Estate Fund V

Andre Collin and Ben Sarly from Lone Star joined the Council meeting to provide an update on their real estate funds and to present Lone Star Real Estate Fund V.

Collin reviewed Lone Star's organization structure and the key senior people. He discussed the relationship Lone Star has with Hudson Advisors which provides due diligence and analysis, asset management and other support services. He emphasized the benefits derived from this dedicated platform.

Collin discussed actual and projected performance of Lone Star Funds II, III and IV, as well as the current commitment level for Fund IV. He provided information on Fund V including the target fund size and expected capital allocations.

Collin provided an investment overview for the regions of the Americas, Europe and Asia-Pacific, discussing for each the investment opportunities, Lone Star's strategies, focus, and competitive advantages.

In response to Council questions, Collin discussed in more detail Lone Star's key-man risk and succession process, relationship with Hudson, buy and sell strategy, and net returns.

Means thanked Lone Star for their presentation.

Council discussion continued.

Elliot Mallem, representing Unite Here, provided comments about Lonestar during a prearranged period for public comment. Mallem drew attention to Lone Star staff turnover.

Chris Nelson updated the Council on the current and projected exposures to real estate compared to benchmarks. He reminded the Council that Lone Star funds are split 50/50 to real estate and distressed debt for asset allocation purposes. He reviewed the Council's commitment level in the last Lone Star fund.

Clark reviewed staff's recommendation of up to \$300 million in aggregate for Lone Star Fund V. He discussed staff's due diligence on Lone Star, including their dedicated relationship with Hudson, personnel and succession issues. Following Council discussion, Clark indicated he would confirm his understanding of succession issues and inform the Council of any significant adverse finding.

DAVID HILLARD MOVED, SECONDED BY ROB WYLIE, TO AUTHORIZE THE STATE INVESTMENT OFFICER TO INVEST UP TO \$300 MILLION IN AGGREGATE IN ADJUSTED PROPORTIONATE AMOUNTS FOR THE SOUTH DAKOTA RETIREMENT SYSTEM, THE SCHOOL AND PUBLIC LANDS FUND, THE DAKOTA CEMENT TRUST, THE EDUCATION ENHANCEMENT TRUST, AND THE HEALTH CARE TRUST IN LONE STAR REAL ESTATE FUND V. THE MOTION PASSED UNANIMOUSLY ON A ROLL CALL VOTE.

10) Higher Education Savings Plan

Sherry Nelson reviewed the Higher Education Savings Plan summary of accounts and quarterly compliance schedule. She noted that the HESP annual report letter was completed and mailed to the Governor, The Speaker of the House, and the President Pro Tempore of the Senate, and that she would be sending a copy to the Council.

In response to a Council question about the Morningstar rating for the CollegeAccess529 plan, Clark discussed the background behind the rating and the steps Allianz is making to improve.

11) Blackstone Real Estate Partners Europe V

Anthony Myers and Amanda Hudson from The Blackstone Group joined the Council to discuss European real estate and to present their BREP Real Estate Europe V fund.

Anthony Myers gave an overview of Blackstone's real estate operations in Europe and reviewed the organizational structure and historical success. He discussed the real estate environment in Europe and degree of recovery in various countries from the global financial crisis. He discussed the significant opportunities due to continued bank exposure to real estate and limited new supply.

Myers reviewed BREP's size advantage and unique position to capture opportunities. He described their strategy of value creation at the asset level before selling. He discussed their process of establishing platforms across Europe to provide leverage, knowledge and conviction.

Means thanked Blackstone for their presentation. Council discussion continued.

Nelson reviewed the current exposure to Blackstone Real Estate and exposure to Blackstone overall for both the base case and maximum case scenarios. He reviewed Blackstone's projections for return of capital.

Clark reviewed staff's recommendation of up to \$300 million in total for BREP Europe V. He reminded the Council that there was not an investment in BREP Europe IV because the total Blackstone exposure at that time was too close to the maximum limit.

LAURA McNALLY MOVED, SECONDED BY RICH SATTGAST, TO AUTHORIZE THE STATE INVESTMENT OFFICER TO INVEST UP TO \$300 MILLION IN AGGREGATE IN ADJUSTED PROPORTIONATE AMOUNTS FOR THE SOUTH DAKOTA RETIREMENT SYSTEM, THE SCHOOL AND PUBLIC LANDS FUND, THE DAKOTA CEMENT TRUST, THE EDUCATION ENHANCEMENT TRUST, AND THE HEALTH CARE TRUST IN BLACKSTONE REAL ESTATE PARTNERS EUROPE V FUND. MOTION PASSED UNANIMOUSLY ON A ROLL CALL VOTE.

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 Yankton on April 19, 2016.

14) Adjournment

Chair Means declared the meeting adjourned at 11:30 a.m.