THE INVESTMENT COMMITTEE
OF THE
MARYLAND STATE RETIREMENT AND PENSION SYSTEM

MINUTES OF OPEN MEETING

November 21, 2017

The Investment Committee convened on Tuesday, November 21, 2017 at 9:05 a.m. in the 16th Floor Board Room of the State Retirement Agency, SunTrust Building, 120 E. Baltimore Street, Baltimore, MD.

Committee Members Attending: (1) Via telephone	Michael K. Barry Eric Brotman Peter Franchot David Hamilton Linda A. Herman, Vice-Chair (1) F. Patrick Hughes, Chairman Lisa James-Henson	Charles W. Johnson Stephen Kitsoulis Nancy K. Kopp Richard Norman Douglas Prouty Michael J. Stafford, Jr.
Committee Members Not Attending:	David Brinkley James Harkins Sheila Hill	Larry E. Jennings, Jr. Theresa Lochte
Also Attending:	Victor Adekoya Phillip Anthony (MLIS) Jennifer Barb (Indus Capital Partners LLC) Anish Bedi Frank E. Benham (Meketa) Colleen Bower Susanne Brogan Robert Burd, Deputy CIO Elizabeth Burton Rachel Cohen, OAG Eric Farls David Ferguson Anne Gawthrop Michael Golden Dimitri Grechenko Alex Harisiadis, OAG Justin Hayes Levar Hewlett Rebecca Jacobs (UniteHere!) Dana Johns Faina Kashtelyan	Larry Katsafanas Dean Kenderdine John Kenney Rob Kochis (Townsend Group) Thomas Kurowski (Alex Brown) Michael McCord Mary Mustard (Meketa) Stephen Muturi Eileen O'Grady (UniteHere!) Andrew Palmer, CIO Stephen Reilly David Rongione, Chief Internal Auditor, Internal Auditing Div. Michael Rubenstein, (MLIS) Dan Schick Jody Shaw, OAG Ryan Skubic (Townsend Group) Frederick "Beau" Smith Michael Stark (Townsend Group) Toni Voglino Patricia Wild Alex Zlotnikov

Mr. Hughes, Chairman, called the Investment Committee meeting to order at 9:05 a.m.

Item 1: Minutes
On a motion made by Mr. Prouty and seconded by Ms. Lochte, the Investment Committee unanimously approved the October 17, 2017 open meeting minutes.

Item 2: 2018 Investment Committee Meeting Dates
The Committee received potential Investment Committee meeting dates for Calendar Year 2018. The meeting schedule that was presented for the Committee's consideration was as follows: Tuesday, February 20, 2018, Tuesday, May 15, 2018, Tuesday, September 18, 2018 and Tuesday, November 20, 2018.

On a motion made by Mr. Hamilton and seconded by Mr. Hughes, the Investment Committee unanimously approved the 2018 Investment Committee meeting dates as submitted.

Items 3: Meketa Reports
Frank Benham and Mary Mustard from Meketa Investment Group presented the third Quarter of 2017 performance update and current market overview to the Committee. Mr. Benham noted that global stocks had produced very strong returns over the last year. He also highlighted that the MSCI ACWI Index had produced positive returns for 12 consecutive months for the first time in 30 years. He noted that high equity valuations and low volatility were being driven by potential tax reform and accommodative monetary policies by the global central banks.

Item 4: Factor Based Equity Investing
Mr. Benham from Meketa presented a report on factor-based equity investing, which was a continuation from the Trustee education session in August 2017. He indicated that Maryland currently utilizes factor-based strategies in the portfolio. Mr. Benham also pointed out that there was some degree of overlap among the System's managers. He indicated that the System's equity market beta has gradually declined since the global financial crises, and has exhibited a modest bias to the factors of growth, high volatility and lower quality.
Mr. Benham recommended that staff continue to evaluate the use of factor-based investing. He suggested that an increased use of factor-based strategies could improve expected returns, reduce risk and reduce management fees.

Mr. Hughes asked if the System should adopt a more passive style of factor investing within the public equity portfolio. Mr. Palmer replied that staff has been working on this issue with Meketa. Mr. Palmer also noted that staff monitors active managers to determine the source of alpha, with the objective of choosing managers that do not rely on factor exposures to generate excess returns.

Item 5: Report from CIO
Mr. Palmer introduced three new hires in the Investment Division – Anish Bedi, Alex Zlotnikov and Levar Hewlett. He also discussed the restructuring of the Nominal Fixed Income portfolio, as the number of generalist managers was reduced in favor of a more specialized approach in order to enhance returns through improved security selection. He also indicated that assets had been transitioned from developed international equities to emerging market equities to reflect the new asset allocation. In addition, new passive accounts had been established to fund the increased allocation to natural resources and infrastructure.

Mr. Palmer identified the primary drivers of asset movements since the last meeting, including potential tax reform legislation. The system continues to meet its key performance indicators for most periods, achieving returns that largely met the actuarial target, with the exceptions of the three- and ten-year time periods. The System has also continued to achieve excess returns over the policy benchmark, as well as earn a real return greater than three percent. Mr. Palmer also explained that as of October 1, 2017, the System was underweight emerging market and U.S equity, and overweight international developed equity. He noted that assets had been rebalanced during October to bring the weightings more in line with the new asset allocation. At the end of October, the System was roughly 2% overweight developed international stocks and 1% underweight emerging market equities.

Mr. Palmer noted that the recent underperformance in Real Assets was driven largely by benchmark mismatch in natural resources and infrastructure, where public market indices are used to benchmark private market strategies. He expressed confidence that this mismatch would be short-term in nature, and that the differences would be smoothed over time. He also noted that the Absolute Return portfolio has experienced a more persistent shortfall in performance over time. As previously discussed with the Committee, much of this underperformance can also be attributed to differences in composition between the System's portfolio and the benchmark. Mr. Palmer also acknowledged that performance in the Absolute Return program needed to improve, and that he would work with staff to restructure the portfolio by adding a diversified set of strategies to enhance returns while maintaining low correlation to the rest of the portfolio.

Mr. Barry stated that the Absolute Return portfolio will likely be critical over the next few years as the probability of a market correction has increased, and questioned whether staff had an appropriate level of resources. Mr. Palmer explained that additional resources had recently been dedicated to the Absolute Return portfolio. He also noted that not all of the System's hedge funds are included in Absolute Return, as credit hedge funds are now being covered by the Fixed Income group and long/short equity hedge funds are being managed by the Public Equity team.

Comptroller Franchot inquired about the impact on the fund of payouts to beneficiaries during a market downturn. Mr. Palmer replied that net outflows from the plan result in a lower market value only in years when the System earns a return less than 1.5%.

Mr. Reilly then presented an in-depth review of the Real Estate portfolio, including a comprehensive performance and structural analysis.

Item 6: The Townsend Group Report

Rob Kochis, Michael Stark and Ryan Skubic from Townsend Group presented an update of the overall real estate market, as well as a program review of the System's real estate portfolio. The presentation highlighted the impressive real estate returns experienced by institutional investors over the last seven years since the global financial crises. They noted that real estate prices are modestly high relative to historical benchmarks, and that there is less capital flowing into real estate today versus recent years. Mr. Kochis indicated that the System's real estate program is efficient in number of manager relationships and manager fees.

Mr. Hamilton inquired about the damage from recent hurricanes as it related to the System's real estate portfolio. Mr. Reilly confirmed that the System's exposure was minimal.

Comptroller Franchot asked why the allocation to REITs was reduced. Mr. Reilly explained that REITs are publicly-traded on exchanges and susceptible to market volatility similar to stocks. Staff implemented the reduction in order to lower correlation to the rest of the portfolio. Mr. Palmer added that private real estate partnerships have outperformed REITs and have added value to the portfolio.

Comptroller Franchot inquired about the System's exposure to real estate located in Maryland. Mr. Reilly indicated that he would explore the issue and follow-up with a response. Mr. Palmer added that some states do not want their pensions investing in in-state real estate because they believe they already have significant exposure to the local economy in other forms.

Mr. Barry inquired if it is common for pension plans to hold large direct real estate. Mr. Kochis of Townsend replied that other large plans have direct programs, but it can be more challenging from an administrative perspective to manage a direct program. He also noted that the fee savings are usually not substantial. Internal resources and expertise can become an issue. Mr. Palmer added that Tennessee managed real estate internally and used vendors to source opportunities, which became difficult to process. Also, the size of the portfolio can be an obstacle to investing in larger projects.

Mr. Hughes asked about the different incentive compensation structures associated with private funds. Mr. Kochis replied that the fees vary across strategies, with core having the lowest incentive fees and opportunistic funds having the largest.

Item 7: Investment Reports

The Committee received the following investment reports:

- State Street Performance Reports
- Private Markets Performance Reports
- TUCS Report
- Securities Lending Report
- Division's FY18 Travel Plan - Update
- Quarterly ORP Performance Report
- OPEB-PHBT Update
- New Hire Manager Report

On the Directors Desk:

- Broker Commission Reports

On a motion made by Mr. Brotman and seconded by Ms. Lochte, the Investment Committee voted without objection to meet in closed session at 11:35 a.m. for the purposes of: (1) reviewing the closed session Investment Committee meeting minutes, pursuant to General Provisions Art., § 3-103(a)(1)(i) the exercise of an administrative function; and (2) receiving a presentation by staff of a sample manager due diligence report, including the analysis of staff and Pavilion Alternatives Group, the System's private equity consultant, pursuant to General Provisions Art., § 3-305(b)(13), to comply with a specific constitutional, statutory, or judicially imposed requirement that prevents public disclosures about a particular proceeding or matter, namely General Provisions Art., § 4-335 regarding the prohibition on disclosing trade secrets and confidential commercial or financial information, and General Provisions Art., § 3-305(b)(5), to consider the investment of public funds.

CLOSED SESSION

Committee Members Attending:	Michael K. Barry	Charles W. Johnson
	Eric Brotman	Stephen Kitsoulis
	Peter Franchot	Nancy K. Kopp
	David Hamilton	Richard Norman

	Linda A. Herman, Vice-Chair (1) F. Patrick Hughes, Chairman Lisa James-Henson	Douglas Prouty Michael J. Stafford, Jr.
Committee Members Not Attending:	David Brinkley James Harkins Sheila Hill	Larry E. Jennings, Jr. Theresa Lochte
Also Attending:	Victor Adekoya Anish Bedi Frank E. Benham (Meketa) Colleen Bower Susanne Brogan Robert Burd, Deputy CIO Elizabeth Burton Rachel Cohen, OAG Eric Farls David Ferguson Anne Gawthrop Michael Golden Dimitri Grechenko Alex Harisiadis, OAG Justin Hayes Levar Hewlett Dana Johns	Faina Kashtelyan Larry Katsafanas Dean Kenderdine John Kenney Michael McCord Mary Mustard (Meketa) Stephen Muturi Andrew Palmer, CIO Stephen Reilly David Rongione, Chief Internal Auditor, Internal Auditing Div. Dan Schick Jody Shaw, OAG Frederick "Beau" Smith Toni Voglino Patricia Wild Alex Zlotnikov

On a motion made by Ms. Lochte and seconded by Mr. Brotman, the Investment Committee returned to open session at 11:58 a.m.

OPEN SESSION

During closed session, the Investment Committee discussed and took action on the following matters:

The Committee reviewed and approved the October 17, 2017 closed session meeting minutes.

The Committee discussed a presentation by staff regarding a manager due diligence report.

Adjournment — There being no further business before the Investment Committee, on a motion made by Mr. Prouty and seconded by Mr. Brotman, the meeting adjourned at 11:58 a.m.

Respectfully submitted,

Andrew C. Palmer
Chief Investment Officer