

THE INVESTMENT COMMITTEE
OF THE
MARYLAND STATE RETIREMENT AND PENSION SYSTEM
MINUTES OF OPEN MEETING

November 16, 2021

The Investment Committee convened on Tuesday, November 16, 2021 at 9:40 a.m., via hybrid / video-conference call with the host site at the Maryland State Retirement Agency, SunTrust Building, 120 East Baltimore Street, 16th Floor, Board Room, Baltimore, Maryland.

Committee Members	David Brinkley	Richard Norman
Attending:	Eric Brotman, Chairman	Douglas Prouty
	Peter Franchot	Anne L. Shelton
	Sheila Hill	Michael J. Stafford, Jr., Vice Chair
	Nancy K. Kopp	Lamont Tarbox
Also Attending:	Linda Allen (Trustee)	Faina Kashtelyan
	Michael Baker	Larry Katsafanas
	Anish Bedi	Ratna Kota
	Frank Benham (Meketa)	John Lawlor (Hamilton Lane)
	Bernadette Benik (Treasurer's office)	Charles Lee
	Scott Bolander (live stream)	Michael McCord
	Tom Brandt, Jr. (Trustee)	Nitin Mathew
	Robert Burd, Deputy CIO	Kyongdo Min
	Rachel Cohen, OAG	Katie Moore (Hamilton Lane)
	Melody Countess	Mary Mustard (Meketa)
	James Daly, Jr. (Trustee)	Stephen Muturi
	Benjamin Eckroth (Hamilton Lane)	Minh Nguyen
	Mike Fang	Martin Noven, Exec. Director
	Eric Farls	Ashu Pal
	David Ferguson	Andrew Palmer, CIO
	Mimi Forbes	Steven Pytlar
	Anne Gawthrop	Stephen Reilly
	Michael Golden	Greg Ricci
	Dimitri Grechenko	David Rongione, Internal Auditing
	Kenneth Haines (Trustee)	Dan Schick
	Alex Harisiadis, OAG	Jody Shaw, OAG
	John Harris (Meketa)	Janet Sirkis
	Justin Hayes (Comptroller's office)	Kevin Slack
	Angie Jenkins	Frederick "Beau" Smith
	Dana Johns	Toni Voglino
	Danita Johnson	Jack Wheatley

Mr. Noven conducted a roll call to establish a quorum. Chairman Brotman called the meeting to order.

Item 1: Ratification of Open Session Minutes

On a motion made by Mr. Prouty and seconded by Ms. Hill, the Investment Committee ratified the September 21, 2021 open meeting minutes.

Item 2: Next Year's Investment Committee Meeting Dates

The Committee received potential Investment Committee meeting dates for Calendar Year 2022. The meeting schedule that was presented for the Committee's consideration was as follows: Tuesday, February 15, 2022; Tuesday, May 17, 2022; Tuesday, September 20, 2022; and Tuesday, November 15, 2022.

Mr. Stafford made a motion to change the Committee meeting start time from 9:30 a.m. to 8:30 or 9:00 a.m. It was mentioned that the Corporate Governance Committee chair would need to agree to move their meeting start time to 8:30 a.m. for the investment committee meeting to start at 9:00 a.m.

After consulting with the Governance Committee Chair about the time change, on a motion made by Treasurer Kopp and seconded by Mr. Norman, the Investment Committee unanimously approved the 2022 Investment Committee meeting to begin at 9:00 a.m. on the dates as submitted.

Item 3: Report from CIO

Mr. Palmer provided an update on performance. He noted that the portfolio is up in October, but State Street has not provided an estimate in time for the meeting. Markets are up slightly for the month to date. Referring to the September Tearsheet, he noted that for the quarter, the System produced a 1.56 percent return against the benchmark return of 1.74 percent. The primary driver of the difference is the timing mismatch of return reporting for Real Estate. The Real Estate benchmark was up 6.5%, while the Real Estate portfolio was up only 45 bps. The difference is the result of reporting timing differences. Mr. Palmer noted that the real estate portfolio is performing well as demonstrated by the report provided by Townsend that adjusts for the timing differences in reporting. The benchmark for Private Equity was updated, and the asset class was up 50 percent for the year. He also indicated that the Absolute Return benchmark was also updated.

Ms. Shelton asked which benchmark for Absolute Return is currently being reported. Mr. Palmer responded that the benchmark is the same one that has been used over the last several years, which is the HFRI Fund of Funds Conservative plus 100 basis points. The new benchmark would be effective on December 1, 2021.

Mr. Palmer then reviewed the Executive Summary section of the report, noting that total plan performance continues to be strong, up 21.46% over past 12 months with 106 basis points of excess return. All three of the main performance metrics are positive, signaling outperformance of the measurement benchmarks. Looking at the cash flow exhibit, two billion dollars was committed to managers over the quarter across all asset classes. He also mentioned that rebalancing activities into bonds from stocks and Absolute Return were performed due to asset classes moving away from targets.

Mr. Palmer noted that the division was active on the manager hire front and activity was largely evenly distributed, with credit being the most active for the quarter. He also indicated that the System was rebalancing, and capital calls were largely being funded by distributions with positive cash flow in Private Equity.

Mr. Brotman asked if the System was at risk of violating the approved allocation ranges for private equity.

Mr. Palmer noted that there are no explicit ranges around private equity, but rather indirectly through the overall allocation to growth equity (private and public equity combined). Mr. Palmer added that there is a pacing plan in place to reach long-term target allocations.

Mr. Palmer then informed the Committee of two recent hires at the Associate position – John Blichar and Michael Klos. He added that the division is recruiting for a few additional positions, including an open accounting position.

Mr. Palmer then provided an update on recent meetings with the Joint Committee on Pensions. One of the meetings focused on climate change. Ms. Cohen provided the Joint Committee a presentation regarding fiduciary responsibility, with emphasis on how it intersects with Economically Targeted Investing, the Department of Labor and ERISA. He reported that he and Ms. Voglino then explained the System's processes that focus on being a responsible shareholder and incorporating environmental, social and governance elements, including climate change, into the overall investment process. They highlighted the groundbreaking work of the Board, working with Meketa to incorporate climate change into the System's asset allocation process and how it informed a different recommendation. There were two other presenters at the meeting. The first focused on the things responsible investors should consider, many of which are already incorporated in the System's investment process. The second person focused on divestment as the primary tool to promote best practices.

Mr. Palmer explained that the division was in the process of reviewing the practices of other peer public plans that have adopted divestment policies to learn from their experience. Mr. Palmer noted that he hopes to include the results of this review in the annual risk analysis provided in January.

The second meeting of the Joint Committee focused on in-state investing. As part of that presentation, Mr. Palmer and Ms. Johns spoke about the System's work to promote a strong venture ecosystem in Maryland, while maintaining our commitment to excellent investment results. Other speakers from Johns Hopkins and TEDCO talked about their efforts to support business formation and job growth in Maryland. Both speakers highlighted areas in Maryland that could be improved to promote a successful venture environment. Mr. Palmer noted that it does not appear that TEDCO intends to reconstitute itself to be able to fulfill its obligations under the existing arrangement. As a result, the System may need to look for an additional partner. He added that the division will continue to try to work with TEDCO to understand and identify the opportunities coming out of the State's universities, as they are uniquely set up to review them.

Several committee members stressed the importance of being able to review in-state venture capital opportunities.

Treasurer Kopp noted that while there is overlap between in-state job creation, economic development and investment returns, the goals and missions of the parties are different. This may result in less money being directed to the pension and more capital directed to economic development.

Mr. Brotman noted that those assets would not be a part of the pension.

Mr. Brinkley commented that venture-backed private enterprises serve as the engine of economic development on the West Coast and Silicon Valley. He added that there is talent in Maryland that could act as a similar engine.

Mr. Stafford commented that a fiduciary's responsibility is to make money for the System to meet plan objectives, not to grow Maryland's economy.

Mr. Brinkley noted that everyone supports Maryland's economic growth but acknowledged the difficulty of a direct financial mandate given fiduciary responsibility.

Mr. Palmer explained that staff is committed to be a part of the solution through its network of venture capital managers.

Mr. Palmer highlighted two new internal portfolios - a U.S. small-cap equity mandate and a U.S. securitized bond strategy.

Mr. Palmer then discussed the liquidity of the plan, focusing on the liquidity of each asset class based on a sliding scale of how quickly assets could be sold for capital. Illiquid assets comprised about 32 percent of the portfolio. Mr. Palmer added that there is some level of illiquidity in public asset classes like stocks and bonds.

Mr. Tarbox suggested showing a historical trendline of the total illiquid assets percentage to show the year to year evolution of the liquidity profile of plan assets. Mr. Tarbox also suggested adding a column to the liquidity table to reflect the System's uncalled capital.

Mr. Palmer indicated that this information will be included in future reporting.

Mr. Stafford inquired about the proposed increase to the allocation range for private credit. Mr. Palmer responded that the range increase is due to the reduction in the overall target allocation to the Credit asset class. The range expansion will allow the System to maintain its target exposure to private credit.

Item 4: Liquidity Analysis with Private Assets

Mr. Palmer noted that Ms. Shelton asked about the System's liquidity profile to meet traditional pension obligations, as well as private market capital calls, during periods of stress during the last Investment Committee meeting. He explained that staff and Meketa had worked together to respond to this question.

Mr. Benham commented that since the last Investment Committee meeting, staff and Meketa, in a collaborative effort, researched the question relating to liquidity for each asset allocation. A liquidity stress test was conducted using an existing model. The time period for the analysis was extended from 5 to 10 years and analyzed what happened in previous financial crises. The analysis showed that asset allocation will change over time and there are constraints to the System's ability to generate liquidity. However, the conclusion is that there is ample liquidity to meet obligations of the pension system. The System has sufficient liquid assets to cover expected net outflows for benefits and private market contributions. The System would need to sell assets at depressed levels, which is primarily due to the return environment and not necessarily liquidity. For the alternative policy adopted in September, the market value would shrink and only modestly recover, but there is still ample liquid assets to meet obligations.

Ms. Shelton expressed her appreciation for the efforts of Meketa and staff in completing this analysis.

Mr. Benham responded that it is helpful to look at models differently and add different assumptions and inputs to them.

Mr. Brotman asked Mr. Benham to confirm that there is ample liquidity to sustain and recover from a major market event like the Great Financial Crisis and the tech bubble.

Mr. Benham confirmed that was the case.

Item 5: Hamilton Lane

Ms. Moore explained that Hamilton Lane's report will include the private equity and private credit portfolios, and will cover pacing, liquidity, and opportunities on the horizon. Private equity time-weighted returns over one-year and over ten years look very good. Private equity was not terribly hit by the pandemic or current inflation trends. Some industries like healthcare even benefited from the effects of the pandemic. She indicated that Hamilton Lane and staff will focus on pacing and liquidity. On average, around 20 percent of capital commitments is returned on an annual basis as distributions. There are also some regulatory concerns and ESG transparency challenges. More companies than ever are owned by private equity funds. Purchase price multiples and valuations are important - on a five-year look-back, they look

expensive. However, the System would not have experienced the significant appreciation over the last five years if it had not been an active investor.

Ms. Moore added that credit markets have performed well. When equity funds generate strong returns, so too do credit funds typically. Higher inflation has led to the belief that credit funds will thrive under future rate hikes. Whether inflation is transitory or a long-term shift remains to be seen. Private equity is an asset class that offers more ways to affect positive change for portfolio companies. It has been a great year for performance as the since inception IRR has improved 300 basis points. There has also been an uptick in the percentage of the plan that private equity makes up – currently around 17% whereas the new target is 16%, up from 13%. The ratio of distributions to paid-in capital is strong across the portfolio. There is interest in direct co-investments. Growth has been driven by the capital invested in the strategies. Ms. Moore explained that the performance of the portfolio has performed well against both the custom, Hamilton Lane, and public equity benchmarks. She recommended maintaining the \$1.5 to 2-billion-dollar range of annual commitments. She noted that the System has partnered with strong managers, with a core group of 14 to 18 firms.

Mr. Eckroth provided an update on the private credit portfolio. At inception, initial commitments were in distressed debt and mezzanine funds. There is 4.7 billion in committed capital. Commitment pacing was reduced for a few years and the team is focused on building out the portfolio. Capital commitments have increased recently and performance has been strong, with the 1-year IRR of 24.4 percent. By strategy, distressed and mezzanine have been present for a long time. Specialist lending has been a recent addition and is attractive. The distressed debt performed well over the year. CarVal, Castlelake, and Whitehorse have been driving performance. There was a record amount of commitments in 2020, taking advantage of the market dislocation. The System has typically met or exceeded the Hamilton Lane median benchmark. Cashflow was negative in 2020 because of greater commitments, but distributions increased in 2021. 2021 saw the most distributions since 2017. The goal is to be relatively consistent with commitment pacing. The pacing model results in \$700 – \$950 million in annual commitments to get to 4 - 4.5% of plan assets. The team will continue finding attractive opportunities, with existing and new managers. Separate accounts and co-investments will also be evaluated in the private credit space.

Mr. Brotman noted that he enjoyed the presentation and asked if private credit could be a tool for inflation hedging.

Ms. Moore responded that most of the portfolio consists of floating rate credit, so there is some inflation hedging properties.

Item 6: Meketa Reports

Ms. Mustard provided an update on third quarter performance. She noted that relative underperformance was driven mainly by real estate, but when the reporting timing differences are accounted for, this will correct itself. There was also a low return from the absolute return portfolio. The underweight to fixed income drove strong 1-year performance. Relative to the Investmetrics peer group, the System was in the 9th percentile net of fees for 3 years. There was also strong risk adjusted performance over the last the 3 and 5-years, as reflected in the Sharpe Ratio ranking. Ms. Mustard also highlighted the China and inflation research insights from Meketa available on their website.

Mr. Brotman noted that the risk-adjusted returns are extraordinary.

Item 7: Recommendation for Implementation of Asset Allocation Changes and Benchmark Changes

Ms. Mustard then summarized the recommended changes to the policy benchmarks, as well as the implementation timeline for the new asset allocation. The Real Assets policy benchmark change reflects shifts in weights based on the approved new asset allocation. There is a change in the Absolute Return

benchmark. The current benchmark is an HFRI Fund-of-Funds +100 basis points. When adopted, it reflected the goals of the asset class. However, constituents have been shrinking and are now down to twenty. The proposed new benchmark for Absolute Return is an asset-weighted blend of 50% HFRI Relative Value, 25% HFRI Global Macro, and 25% HFRI Event-Driven. This benchmark better aligns with the implementation of the Absolute Return portfolio. She added that Meketa prefers the blended option because it allows for better attribution comparisons; it represented the least bad option for hedge fund benchmarks.

Mr. Brotman asked Ms. Mustard to comment on some of the unattractive performance statistics of the new benchmark such as high negative skew and whether it reflects negatively on use of the asset class.

Ms. Mustard responded that the current benchmark has a very limited number of constituents. She noted that Meketa evaluated other options in an attempt to identify a benchmark that had similar beta and correlations to the Absolute Return portfolio. The proposed benchmark has greater transparency, weight considerations, and is better than the alternatives. Some of the current benchmark statistics are preferable but the benchmark need to be phased out due to lack of constituent diversification.

Mr. Stafford asked if for the Natural Resources/Infrastructure asset class, there were alternatives to using indexes composed of only public stocks.

Ms. Mustard responded that it will take time to build out a private market portfolio. In the meantime, the public market benchmark is appropriate as it represents the majority of the current assets. As private market exposure increases, the benchmark may have to be adjusted to reflect a private market peer universe.

Mr. Brotman asked Mr. Palmer if the Committee needs to approve these benchmark changes and implementation plan.

Mr. Palmer confirmed that Committee approval is needed.

Mr. Stafford asked about the amount of time to implement a 1 percent allocation change.

Ms. Mustard replied that a one percent move may sound small, but in dollar terms it is significant. Also, redemptions from Absolute Return require planning around liquidity windows and advance redemption notifications to the managers.

On a motion made by Mr. Tarbox and seconded by Mr. Prouty, the benchmark changes and asset allocation implementation timeline were approved unanimously.

Item 8: Recommend IPM Changes

Ms. Voglino explained that the three proposed changes to the Investment Policy Manual include the addition of the Responsible Contractor Policy approved by Board on June 15th; the new asset allocation changes approved by Board in September; and the changes approved today regarding the asset allocation implementation timeline and benchmark changes.

Mr. Brotman asked Ms. Voglino to confirm that all these changes have already been approved, and there are no new additional changes.

Ms. Voglino confirmed that was the case.

Mr. Prouty made a motion to approve the proposed changes to the Investment Policy Manual, which was seconded by Mr. Tarbox. The motion passed unanimously.

Item 9: Committee Led Discussion

No items were discussed.

Item 10: Investment Reports

The Committee received the following investment reports:

- State Street Performance Reports
- Terra Maria Performance Reports
- TUCS Report
- Private Markets Performance Reports
- Securities Lending Report
- Division’s FY22 Travel Plan - Update
- Quarterly ORP Performance Report
- OPEB-PHBT Update
- New Hire Manager Report

On the Directors Desk:

- Broker Commission Reports
- Quarterly Manager Fee Report

Item 11: Motion by the Investment Committee to meet in Closed Session

On a motion made by Mr. Tarbox and seconded by Ms. Shelton, the Investment Committee voted without objection to meet in Closed Session at 12:58 p.m. for the purposes of:

- (a) reviewing the closed session Investment Committee minutes, pursuant to General Provisions Art., § 3-103(a)(1)(i), the exercise of an administrative function, and General Provisions Art., § 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art., § 3-306(c)(3)(ii), requiring that the minutes of a closed session be sealed and not be open to public inspection; and
- (b) presenting by staff of a sample Manager Due Diligence report including the analysis of staff and Meketa, the System's general consultant, pursuant to General Provisions Art., Section 3-305(b)(5), to consider the investment of public funds; and General Provisions Art., Section 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art. Sec. 4-335, preventing the disclosure of trade secrets and confidential commercial or financial information, General Provisions Art. Sec. 4-344, requiring denial of inspection of confidential interagency memoranda, and State Personnel and Pensions Article, Section 21-123(g) and Code of Maryland Regulations 22.01.02.03E, protecting from disclosure certain investment records.

CLOSED SESSION

Committee Attending:	Members	David Brinkley Eric Brotman, Chairman Peter Franchot Sheila Hill Nancy K. Kopp	Richard Norman Douglas Prouty Anne L. Shelton Michael J. Stafford, Jr., Vice Chair Lamont Tarbox
Also Attending:		Linda Allen (Trustee) Michael Baker	Faina Kashtelyan Larry Katsafanas

Anish Bedi	Ratna Kota
Frank Benham (Meketa)	Charles Lee
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Robert Burd, Deputy CIO	Mary Mustard (Meketa)
Rachel Cohen, OAG	Stephen Muturi
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Alex Harisiadis, OAG	Janet Sirkis
John Harris (Meketa)	Kevin Slack
Justin Hayes (Comptroller's office)	Frederick "Beau" Smith
Angie Jenkins	Toni Voglino
Dana Johns	Jack Wheatley
Danita Johnson	

Item 14: Motion by Investment Committee to adjourn closed session and return to open session

On a motion made by Mr. Prouty and seconded by Treasurer Kopp, the Investment Committee voted to adjourn closed session at 1:30 p.m. and returned to open session.

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

The Investment Committee reviewed and ratified the Closed Session minutes from the September 21, 2021 meeting.

The Committee received and discussed a sample Manager Due Diligence report including the analysis of staff and Meketa, the System's general consultant.

OPEN SESSION

Committee Members Attending:	David Brinkley	Richard Norman
	Eric Brotman, Chairman	Douglas Prouty
	Peter Franchot	Anne L. Shelton
	Sheila Hill	Michael J. Stafford, Jr., Vice Chair
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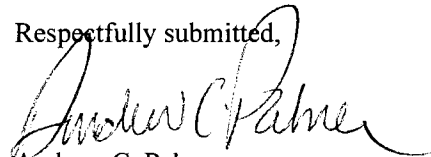
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Item 15: Motion by the Investment Committee to adjourn meeting

Adjournment There being no further business before the Investment Committee, on a motion made by Mr. Prouty and seconded by Treasurer Kopp, the meeting adjourned at 1:32 p.m.

Respectfully submitted,



Andrew C. Palmer
Chief Investment Officer

