THE INVESTMENT COMMITTEE
OF THE
MARYLAND STATE RETIREMENT AND PENSION SYSTEM

MINUTES OF OPEN MEETING

November 27, 2018

The Investment Committee convened on Tuesday, November 27, 2018 at 9:02 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 (1) David Brinkley (1) Eric Brotman Peter Franchot (1) James Harkins Linda A. Herman, Vice-Chair Sheila Hill (1) F. Patrick Hughes, Chairman	Charles W. Johnson Stephen Kitsoulis Nancy K. Kopp Theresa Lochte Richard Norman Douglas Prouty Michael J. Stafford, Jr. Lamont "Monte" Tarbox
Committee Members Not Attending:	Jamaal Craddock	David Hamilton
Also Attending:	Victor Adekoya Anish Bedi Frank E. Benham (Meketa) Susanne Brogan Robert Burd, Deputy CIO Antionette Butcher Rachel Cohen, OAG Eric Farls David Ferguson Anne Gawthrop Michael Golden Dimitri Grechenko Alex Harisiadis, OAG Levar Hewlett Faina Kashtelyan Gregory Kasten Larry Katsafanas	Dean Kenderdine John Kenney Stephen J. MacLellan (Meketa) Michael McCord Leanne Moore (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 Kathleen Wherthey, OAG Patricia Wild

Mr. Hughes, Chairman, called the Investment Committee meeting to order at 9:02 a.m.

Item 1: CLOSED SESSION

On a motion made by Ms. Lochte and seconded by Mr. Norman, the Investment Committee voted without objection to meet in closed session at 9:02 a.m. for the purposes of:

(a) reviewing the closed session special Investment Committee minutes, pursuant to General Provisions Art., Section 3-103(a)(1)(i), the exercise of an administrative function;

(b) discussing an advice of counsel regarding the Investment Division's proposed policy on the use of System assets as collateral, pursuant to General Provisions Art., Section 3-305(b)(7), to consult with counsel to obtain legal advice; and

(c) discussing contract negotiations with potential futures commissions merchants, pursuant to: General Provisions Art., Section 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art., Section 4-335 preventing the disclosure of trade secrets and confidential commercial or financial information; and General Provisions Art., Section 3-305(b)(14), to discuss, before a contract is awarded, a matter directly related to a negotiating strategy or the contents of a bid or proposal, if public discussion or disclosure would adversely impact the ability of the public body to participate in the competitive bidding or proposal process.

Item 4: Motion by the Investment Committee to adjourn Closed Session and return to Open Session
On a motion made by Ms. Hill and seconded by Ms. Lochte, the Investment Committee voted to adjourn closed session and return to open session at 9:21 a.m.

OPEN SESSION

Committee Members Attending: (2) Via telephone	Michael K. Barry (1) David Brinkley (1) Eric Brotman Peter Franchot (1) James Harkins Linda A. Herman, Vice-Chair Sheila Hill (1) F. Patrick Hughes, Chairman	Charles W. Johnson Stephen Kitsoulis Nancy K. Kopp Theresa Lochte Richard Norman Douglas Prouty Michael J. Stafford, Jr. Lamont "Monte" Tarbox
Committee Members Not Attending:	Jamaal Craddock	David Hamilton
Also Attending:	Victor Adekoya Phillip Anthony (MLIS) Anish Bedi Frank E. Benham (Meketa) Susanne Brogan Robert Burd, Deputy CIO Antionette Butcher Billy Charlton (Pavilion) Rachel Cohen, OAG Eric Farls David Ferguson Anne Gawthrop Michael Golden Dimitri Grechenko Alex Harisiadis, OAG Levar Hewlett Faina Kashtelyan Gregory Kasten Larry Katsafanas Dean Kenderdine John Kenney Thomas Kurowski (Alex Brown)	Stephen J. MacLellan (Meketa) Michael McCord Leanne Moore (Meketa) Stephen Muturi Jennifer O'Dell (LiUNA!) 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 Frederick "Beau" Smith Jared Synnestvedt (Wellington Mgmt.) Toni Voglino Laura Vykol (MLIS) Kathleen Wherthey, OAG Patricia Wild Brad Young (Pavilion)

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 18, 2018 meeting; and

The Committee received legal advice regarding a proposed policy granting the CIO the authority to pledge security interests in margin and other collateral in trading futures contracts and other derivative instruments. Investment staff also provided an update regarding contractual negotiations with Futures Commissions Merchants.

Item 5: Ratification of Open Session Minutes
On a motion made by Mr. Brotman and seconded by Mr. Norman, the Investment Committee ratified the September 18, 2018 open meeting minutes.

Item 6: Next Year's Investment Committee Meeting Dates
The Committee received potential Investment Committee meeting dates for Calendar Year 2019. The meeting schedule that was presented for the Committee's consideration was as follows: Tuesday, February 19, 2019; Tuesday, May 21, 2019; Tuesday, September 17, 2019; and Tuesday, November 19, 2019.

On a motion made by Mr. Norman and seconded by Ms. Lochte, the Investment Committee unanimously approved the 2019 Investment Committee meeting dates as submitted.

Item 7: Meketa Reports
Mr. Benham, Ms. Moore, and Mr. MacLellan from Meketa presented Meketa's third quarter 2018 review detailing economic performance in the quarter as well as the System's portfolio performance.

Mr. Hughes asked whether the Board should be modifying the System's equity allocation in light of recent market volatility. Mr. Benham commented that staff has the ability to invest tactically around the asset allocation targets set by the Board. Short-term market movements do not warrant a shift in the long term-allocation. Mr. Brotman commented that according to page 59 of Meketa's report, the System is underweight US stocks vs. peers and that this allocation should pay off when equity markets decline.

Mr. Stafford asked whether the custom manager benchmarks aggregate to the System's overall policy benchmark. Mr. Benham responded that the policy benchmark is independent of the custom manager benchmarks.

Mr. Stafford commented on the use of a different number of sectors shown on different slides in Meketa's reports. He additionally asked whether the Private Equity benchmark was reported with a lag. Mr. Palmer responded that the Private Equity benchmark is lagged by one quarter.

Mr. Stafford asked about a difference in reported performance in the inflation-linked sector in Meketa's report. Mr. Benham responded that he would follow up on this item.

Mr. Stafford asked about the performance of the cash sector in Meketa's report. Mr. Palmer responded that the performance is the result of the cash equitization program which invests the System's cash in ETFs that reflect the System's overall asset allocation and the impact of the income from the System's securities lending program being credited to the cash account.

Mr. Stafford asked about the performance of the real estate sector during the third quarter. Mr. Reilly responded that the third quarter performance contains no performance data from the System's open-end real estate funds, which impacts the performance due to the System's significant allocation to open-end real estate funds. Mr. Reilly noted that this time lag should be reversed in the second quarter of 2019 when the System leaves the accounting records open longer and records two quarters of returns.

Mr. Stafford commented that he would like more clarity in terms of how the implementation of the Policy Benchmark compares to the Board's approved Policy Benchmarks. He asked how the underlying manager benchmarks roll-up relative to the Policy Benchmark. Mr. Stafford explained that, without this information, it was difficult for a trustee to understand implementation of the Policy Benchmarks.

Ms. Herman commented that she would like to see data which shows the System's deviation from the Policy Benchmarks. Additionally, she asked whether the System's overweights & underweights were intentional. Mr. Palmer responded that the System's allocations are estimated and evaluated on a monthly basis, and that all deviations from targets are measured and intentional.

Ms. Herman commented that she would like a quarterly update showing the over/underweights in the portfolio. Mr. Palmer commented that the information is already included in the quarterly updates.

Mr. Stafford asked when the System lowered its equity risk exposure following the Great Financial Crisis. Mr. Palmer responded that there was a major asset allocation change in 2008/2009, but much of this was moving to illiquid asset classes, which took time to implement. The more significant factor in contributing to the lower performance relative to peers was the move to a global public equity benchmark, which eliminated the home country bias. The pivot away from U.S. equities had a significant negative impact on relative performance during a period when U.S. stocks outperformed foreign stocks. Treasurer Kopp and Mr. Hughes both recalled the Board's lengthy discussion relating to this change, and noted that the shift was implemented to enhance the diversification profile of the fund.

Mr. Kitsoulis commented that the Sharpe Ratio data on page 23 of Meketa's report shows that in implementing the Board's asset allocation, staff has done an effective job at generating risk-adjusted returns.

Treasurer Kopp asked about the peer comparison on page 59 of the Meketa report relative to the TUCS comparison on page 21. She also stated that achieving a certain ranking within a peer universe is not one of the Board's objectives. Mr. Benham responded that the TUCS data does not provide much transparency with respect to the contributing plans and that Meketa utilized other information to supplement this data.

Ms. Herman asked whether Meketa has other large state plan clients that have a ranking as low as the System in the performance universes. Mr. Benham responded that Meketa recently was retained by South Carolina, which has performed similarly to the System and a state plan in Illinois, which has performed closer to the median. He commented that the funded status at the Illinois plan was the result of insufficient employer contributions, and not investment performance. Ms. Herman asked what happened to the peer group that Staff had created with similar asset sizes and allocations. Staff said they had not been updating the peer group returns but would research further.

Mr. Brotman commented that the System's weighting to US equities is roughly half of peers while the weighting to emerging market equities is roughly double peers. He added that he does not think that this is the time to adjust that positioning.

Item 9: Report from CIO

Mr. Palmer began his report by commenting on a recent editorial in the Washington Post which referenced a report produced by JP Morgan that analyzed the state's fiscal health. Maryland was given a low ranking in the report based on a high combined debt per capita when including the unfunded pension liability, the OPEB liability and the State's assumption of unfunded liability for county teacher plans. Mr. Palmer noted that he communicated with the author of the report, who emphasized that the large debt burden was not a function of the unfunded pension liability as much as the OPEB and teacher liabilities. In fact, the projected funded status for the System remained stable under the report's conservative assumptions. Mr. Hughes commented that this should be a call for more funding. Comptroller Franchot commented that over the past several years the pension has been funded with $375 million in reinvested savings, despite being promised $1.2 billion. He noted that the pension is not being funded as it was promised by the legislature.

Mr. Palmer then offered Committee members the opportunity to ask questions about the System's investment in ManorCare through Carlyle Fund V, which was an investment from 2007. Treasurer Kopp asked how news like ManorCare flows into the investment process. Mr. Palmer replied that this would be factored into the ESG evaluation process. Mr. Franchot commented that he brought the article to Mr. Kenderdine's attention to highlight the risk of excess leverage, not bad operating performance. Mr. Kitsoulis asked whether there were lessons learned from this experience. Mr. Palmer offered to discuss the situation in greater detail during closed session.

Mr. Palmer continued with a performance review by discussing October's performance and performance for the third quarter.

Mr. Kitsoulis asked about the securities lending program and the guidelines associated with the collateral management account. Mr. Palmer offered to follow up with details.

Mr. Palmer asked the Committee for clarification and guidance on overall ESG policy. Mr. Hughes and Mr. Brotman indicated that the Committee likely has a wide dispersion of opinions on ESG policy and that arriving on a consensus Committee policy would be a challenge. Treasurer Kopp noted that ESG issues were important for the Committee to consider. Mr. Benham stated that Meketa may be able to help facilitate a discussion. Mr. Hughes suggested that a longer discussion at a later meeting may be warranted. Mr. Palmer suggested that the education session may be an effective forum to discuss this topic should the Committee wish to pursue it.

Item 8: 2018 Risk Report

Mr. Palmer presented a draft report regarding the System's investment risks including climate change pursuant to House Bill 993. Mr. Brotman asked for a clarification on the funded status data on page 6 and highlighted a graphical error on page 8. Mr. Palmer highlighted the Misfit Risk data on page 13. A report is required to be submitted to the legislature by January 31. Treasurer Kopp asked the Board members to review and Mr. Palmer suggested that it would be discussed again at December's Board meeting.

Item 10: The Pavilion Alternatives Group Report

Mr. Young and Mr. Charlton from Pavilion Group presented an update of the System's private equity program. This review included a discussion of Pavilion's acquisition by Mercer, an update on the System's pending secondary sale, the state of the private equity market and the performance of the System's Private Equity portfolio.

Mr. Kitsoulis asked if there were any significant deviations from expected prices versus the received bids. Mr. Charlton responded that there were no significant surprises in the bids received.

Mr. Stafford asked if the System expects to sell all the interests it wanted to. Mr. Ferguson commented that there were some fund interests which did not receive sufficient bids to warrant a sale.

Mr. Kitsoulis asked what the goal of the sale was. Mr. Young responded that a secondary sale is a natural part of a maturing Private Equity portfolio. The goal was to relieve the System's investment staff of monitoring manager relationships that were not going to be renewed going forward, and to concentrate the portfolio with only the highest conviction managers.

Ms. Herman asked to see the quartile rankings by fund. Mr. Palmer stated that he would make sure they were posted to the Director's Portal.

Mr. Stafford asked about the correlation between public and private sectors. Mr. Charlton responded that private market assets are typically slower to react to changes in the economic landscape. Mr. Young added that the correlations tend to increase over longer time periods.

Treasurer Kopp asked about portfolio construction by geography and strategy. Mr. Young stated that the System's Private Equity program is diversified by geography and strategy, with heavier weights to buyout funds in the U.S. Mr. Ferguson commented that performance has been driven mainly by manager selection, as opposed to geographic exposure.

Mr. Hughes asked whether the pace of investment by managers would be expected to increase during a down market. Mr. Young responded that historically the pace of investment slows during down markets, likely a result of a widening of the bid/ask spread on transactions, as potential sellers are reluctant to lower their price to reflect current market conditions.

Mr. Hughes asked for clarification on the performance data on page 18. Mr. Young responded that the performance does not include private assets in the Credit and Real Assets asset classes.

Mr. Hughes asked about the impact of Blackrock's retail Private Equity product. Mr. Young responded that Private Equity may not be a good fit for retail investors due to liquidity constraints, which may limit the impact.

Mr. Stafford asked about warning signs that may signal a peak in Private Equity. Mr. Charlton commented that Pavilion does not currently believe that any of their indicators are flashing a warning sign. He added that focusing on quality managers with operational expertise should mitigate the risk of a downturn.

Item 11: Investment Policy Manual

Mr. Burd reviewed the proposed updates to the IPM. The first amendment was to allow the CIO to grant security interests in margin, and other collateral. The second change was to clarify the CIO's authority to manage System assets internally, delegate investment responsibility to staff, describe the framework for selecting assets for internal management and the policies required to be in place in support of an internal management program.

Mr. Brotman asked whether the start-up costs relating to internal management had been estimated. Mr. Palmer responded that an estimate of the cost had been calculated and presented previously in the Cutter Funston report.

Ms. Herman asked if the proposed changes would grant internal management authority without necessary policies and procedures in place. Mr. Burd responded that the authority could not be exercised without the policies and procedures being presented to the Board.

Ms. Herman asked when the policies and procedures would be completed. Mr. Burd indicated that they may be available for the February 2019 Investment Committee meeting.

Mr. Harkins, Treasurer Kopp, and Ms. Herman asked whether the policies and procedures associated with internal management should be presented with the change in the IPM granting authority to manage assets internally.

Mr. Brotman asked whether the proposed amendment associated with FCM agreements could be approved separately from the internal trading authority. Mr. Palmer replied yes.

On a motion made by Mr. Brotman and seconded by Mr. Johnson, the Board approved the amendment authorizing the CIO to pledge security interests in margin, and other collateral, deferring action on the remaining policy change recommendations.

Item 12: Investment Reports

Treasurer Kopp asked if there could be a review of the Terra Maria program at a later date.

The Committee received the following investment reports:

- State Street Performance Reports
- Terra Maria Performance Reports
- Private Markets Performance Reports
- Securities Lending Report
- Division's FY19 Travel Plan - Update
- Quarterly ORP Performance Report
- OPEB-PHBT Update
- New Hire Manager Report

On the Directors Desk:

- Broker Commission Reports
- Manager Fee Report

Item: 13: Motion by the Investment Committee to meet in Closed Session

On a motion made by Ms. Lochte and seconded by Mr. Norman, the Investment Committee voted without objection to meet in closed session at 12:37 p.m. for the purposes of:

(a) presenting by staff of a sample Manager Due Diligence report including the analysis of staff and The Townsend Group, the System's real estate consultant pursuant to General Provisions Art., Section 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure of trade secrets and confidential commercial or financial information; and

(b) discussing the System's investment in Carlyle, pursuant to General Provisions Art., Section 3-305(b)(5), to consider the investment of public funds in a private equity fund and a specific portfolio company of the fund; and General Provisions Art., Section 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art., Section 4-335 preventing the disclosure of confidential commercial or financial information, or trade secrets, related to a portfolio investment of a private equity fund.

CLOSED SESSION

Committee Members Attending:	Michael K. Barry (1)	Charles W. Johnson
	David Brinkley (1)	Stephen Kitsoulis
	Eric Brotman	Nancy K. Kopp
(3) Via telephone	Peter Franchot (1)	Theresa Lochte
	James Harkins	Richard Norman
	Linda A. Herman, Vice-Chair	Douglas Prouty
	Sheila Hill (1)	Michael J. Stafford, Jr.
	F. Patrick Hughes, Chairman	Lamont "Monte" Tarbox
Also Attending:	Victor Adekoya	Larry Katsafanas
	Anish Bedi	Dean Kenderdine
	Susanne Brogan	John Kenney
	Robert Burd, Deputy CIO	Michael McCord
	Antionette Butcher	Stephen Muturi
	Rachel Cohen, OAG	Andrew Palmer, CIO

Eric Farls
David Ferguson
Anne Gawthrop
Michael Golden
Dimitri Grechenko
Alex Harisiadis, OAG
Levar Hewlett
Faina Kashtelyan
Gregory Kasten
Stephen Reilly
David Rongione, Chief Internal Auditor, Internal Auditing Div.
Dan Schick
Jody Shaw, OAG
Frederick "Beau" Smith
Toni Voglino
Kathleen Wherthey, OAG
Patricia Wild

On a motion made by Ms. Lochte and seconded by Mr. Johnson, the Investment Committee voted to adjourn closed session and returned to open session at 1:19 p.m.

OPEN SESSION

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

The Committee received and discussed a presentation from staff regarding its due diligence process generally and with regard to a recent real estate investment and discussed the System's investment in Carlyle.

Adjournment

There being no further business before the Investment Committee, on a motion made by Mr. Brotman and seconded by Ms. Lochte, the meeting adjourned at 1:19 p.m.

Respectfully submitted,

Andrew C. Palmer

Andrew C. Palmer
Chief Investment Officer