

**Minutes  
Investment Advisory Council  
February 14, 2022**

**Call to Order**

The Investment Advisory Council (IAC) met at 12:00 p.m. on Monday, February 14, 2022. The Chair of the IAC determined that an in-person meeting was not practical or prudent because of the current COVID-19 health pandemic. As is permitted under the Open Meeting Law in these conditions, the IAC meeting was conducted via Zoom for Government video conferencing software and over the phone. Attendance and all votes were conducted by roll call.

**MEMBERS PRESENT:** Doug Anderson, Dennis Duerst, Kim Faust, Susanna Gibbons, Morris Goodwin Jr., Jennifer Hassemer (for Jim Schowalter), Peggy Ingison, Erin Leonard, Gary Martin, Dan McConnell, Nancy Orr, Carol Peterfeso, Martha Sevetson Rush, Jay Stoffel, Shawn Wischmeier, and Public Member Emeritus Malcolm McDonald.

**MEMBERS ABSENT:** Denise Anderson.

**SBI STAFF:** Mansco Perry, Patricia Ammann, Paul Anderson, Shirley Baribeau, Nate Blumenshine, Tammy Brusehaver, Andy Christensen, Dan Covich, Stephanie Gleeson, Aaron Griga, Cathy Hua, Andrew Krech, Steve Kuettel, Melissa Mader, John Mulé, Charlene Olson, S. Emily Pechacek, Erol Sonderegger, Jonathan Stacy, Reece Tolkinen, David Velasquez, and Jeff Weber.

**OTHERS ATTENDING:** Leslie Hill, Zahira Habib-Dewji, and Andrey Rumyantsev, Record Currency; Kristen Doyle and Katie Comstock, Aon Investments; Allan Emkin, Sarah Bernstein, Gordon Latter, and Ghiane Jones, Meketa Investment Group; Sean Crawford, Arabella Wuchek, and James Kakoza, Albourne America; Luz Frias and J. Adam Sorenson, Attorney General's Office; Karl Procaccini, Governor's Office; Ramona Advani, State Auditor's Office.

Members of the public attended the meeting, however, due to the meeting being held via virtual teleconference the SBI was unable to track the information.

**Approval of Minutes**

The minutes of the November 15, 2021 meeting were approved unanimously by roll call vote. Morris Goodwin was not present for the vote.

**Introduction of New Staff Members**

Mr. Christensen introduced five of the newest members of the SBI staff and noted that the SBI is in various stages of filling positions for two Investment Officers, two Investment Analysts, and an

Accounting Officer. Mr. Christensen also mentioned two job vacancies as one Investment Officer recently left and an Investment Accounting Specialist will be retiring soon.

### **Performance Summary**

Mr. Perry, Executive Director, referred members to the December 31, 2021 Performance Summary provided in Tab A of the meeting materials. Mr. Perry informed the Board that as of December 31, 2021 the SBI was responsible for almost \$136 billion in assets and that the Combined Funds represent \$94 billion of those assets. Mr. Perry reported that the Combined Funds continue to exceed its long-term objectives by outperforming its Composite Index over the ten-year period ending December 31, 2021 (Combined Funds 11.6% vs. Combined Fund Composite Index 11.2%) and provided a real rate of return above inflation over a 20 year time-period (Combined Funds 8.6% vs CPI-U 2.3%). The Combined Funds matched the composite index for the quarter and exceeded the composite index for all other reporting periods.

Mr. Perry noted that the Combined Funds actual asset mix is in-line with the asset allocation targets. He commented on the quarter-end returns for each asset group and that Public Equities performed slightly below its benchmark mainly from global equities, and to a lesser extent, domestic equities underperforming their respective benchmarks. Mr. Perry stated that for the quarter, the Total Fixed Income segment slightly underperformed its composite benchmark and the Private Markets invested allocation returned 6.4% and the uninvested allocation returned 11.1%. Next, Mr. Perry noted that the Volatility Benchmark Comparison shows the Combined Funds portfolio added value for all time-periods listed on a risk-adjusted basis. Lastly, Mr. Perry stated that the Combined Funds performance ranked in the first quartile for the quarter and the second quartile for the year ending December 31, 2021 compared to other public plans with over \$20 billion in assets in the Trust Universe Comparison Service (TUCS).

### **Executive Director's Administrative Report**

Mr. Perry referred members to Tab B of the meeting materials for the Executive Director's Administrative Report. He stated that the Administrative Budget gives an indication as to how close Staff has tracked the budget for the last six months and provided in the Tab is a copy of the SBI's Legislative Auditor letter, which has no written findings or recommendations; with the financial audit completed, the Fiscal Year 2021 Annual Report has been distributed. Mr. Perry continued that the Administrative Report included the Iran and Sudan summary and that there was no litigation during the quarter.

### **Report from Record Currency Management**

Mr. Martin, Chairperson on the IAC, introduced Mr. Sonderegger, Assistant Executive Director, Portfolio Management and Risk Analysis, to review the currency overlay program. Mr. Sonderegger referred members to Tab C of the meeting materials and reminded members that the Board authorized the implementation of the Currency Overlay Program for the Combined Funds as part of the Board Resolution passed in May 2020 Concerning the Management of Combined Funds Asset Allocation and Liquidity. Mr. Sonderegger stated that the scope of that authorization called for the Currency Overlay Program to be used primarily as a risk management tool to hedge the SBI's non-dollar equity exposure using a gradual implementation process using three phases, which was outlined in the meeting materials.

Mr. Sonderegger introduced Ms. Hill, CEO of Record Currency Management, who presented on the currency overlay strategy and the performance and scope of the hedging program since its gradual roll out in October of 2020.

### **Private Markets Commitments**

Mr. Perry referred members to Tab J of the meeting materials for the Private Markets Commitments. He stated with his forthcoming retirement, Staff accelerated the schedule for approval of twenty-one private market recommendations, which would normally be presented over a six month to one-year time-period. Mr. Perry noted that he preferred not to be bringing forth any new commitments for consideration this time nor during his remaining tenure as Executive Director, but he agreed that moving forward with this tranche would be beneficial for the portfolio. He stated we would not be bringing forth any deals at the next meeting.

Mr. Perry introduced Mr. Krech, Director of Private Markets, to provide a summary of the private market recommendations. Mr. Krech reminded the Council that the due-diligence process continues even after Board approval as more documents and fund details become available throughout the year. Mr. Krech and Mr. Stacy responded to questions on the three new private market manager relationships, Clearlake Capital Partners, Siris Partners, and TSG Consumer Partners. Mr. Krech provided information on the annual capital raising timeline and general due diligence process, specifically with the three new private equity funds during a remote work environment. There were additional questions related to the sizing of the commitments with each manager, typical range of commitments, how sizing is determined, and selection process to determine a final list of private market investments to recommend. Mr. Krech addressed questions specifically to Minnesota Asia Investors regarding challenges completing due diligence with Asian based firms. Mr. Krech stated that the objective with Asia Alternatives, a fund of funds, was their ability to select successful local Asian managers given the limited resources the SBI has with a small staff, travel limitations, and language barriers. Mr. Krech reminded the Council that the Minnesota Asia Investors is divided into two pools of capital: the balanced pool, which invests alongside Asia Alternatives commingled fund vehicles; and the co-investment pool that makes direct commitments, or co-investments, in the underlying funds as well as in individual companies.

Mr. Krech stated that Staff is recommending investments in the following three funds with new private market managers: Clearlake Capital Partners VII (Private Equity), Siris Partners V (Private Equity), and TSG9 (Private Equity); and the following eighteen funds with existing private market managers: Advent International GPE X (Private Equity), Apax XI (Private Equity), Blackstone Capital Partners IX (Private Equity), Blackstone Growth II (Private Equity), Bridgepoint Europe VII (Private Equity), Brookfield Capital Partners VI (Private Equity), IK X Fund (Private Equity), KKR Core Investments Fund II (Private Equity), KKR Europe VI (Private Equity), MN Asia Investors, LP (Private Equity), Nordic Capital XI (Private Equity), Thoma Bravo XV (Private Equity), TPG Partners IX (Private Equity), WCAS XIV (Private Equity), Wind Point X (Private Equity), HPS Strategic Investment Partners Fund V (Private Credit), Oaktree Special Situations Fund III (Private Credit), and Värde Fund XIV (Private Credit).

A motion was made that the IAC endorse the twenty-one private markets commitments. The motion was seconded and approved unanimously by roll call vote.

### **Treasury Protection Portfolio Duration Report**

Mr. Sonderegger presented on the Treasury Protection Portfolio Duration report and Staff Policy Paper included in Tab D of the meeting materials. Mr. Sonderegger stated that Staff conducted a review of the Treasury Protection Portfolio target duration and benchmark as inflationary pressures are expected to persist and pose the risk of a significant rise in interest rates from the recent low yield environment. As the Federal Reserve works to contain inflation in this scenario, staff suggested lowering the target duration range to nine years from the current target of twelve years as a risk mitigation strategy. In addition, staff suggested using interest rate triggers that would shift the target duration and benchmark to a dynamic target duration and policy benchmark based on prevailing interest rates as represented by the Ten-Year Treasury Note. Mr. Sonderegger addressed comments from the Council regarding suitable duration range for the portfolio, other risk-off hedge opportunities, increasing the active risk budget for managers rather than changing their benchmark, and equity risk premium triggers. As part of the discussion, Mr. Perry noted that the primary objective of the Treasury Protection Portfolio had less to do as a hedge and more to do with preservation of capital and to maintain a degree of liquidity. He noted that there is not enough scale in this allocation to provide an appropriate hedge and that the benchmark is not ideal as he would prefer not being at the long end of the curve and putting more dollars at risk. After discussion, Mr. Perry stated that since there was not a strong consensus among IAC members to move forward, he would not bring Staff's recommendation to change the current policy benchmark that would allow for a reduced duration in the portfolio from twelve years to nine years.

### **Stewardship Items**

Mr. Mulé, Director Legal and Policy Services, informed the Council that the SBI's first annual Stewardship Report, which provides a comprehensive accounting of the SBI's work with Environmental, Social, and Governance (ESG) activities, can be found in the SBI's 2021 Annual Report and on the SBI's website. Mr. Mulé also noted that the smaller ESG reports continue to be distributed on a quarterly basis. Lastly, Mr. Mulé introduced Mr. Blumenshine, Investment Officer, Stewardship and ESG, to introduce the next two agenda items: Diversity, Equity and Inclusion (DEI) Task Force and Meketa's Climate Risk Project.

### ***Report from the DEI Task Force***

Mr. Blumenshine referred members to the DEI Task Force Report provided in Tab E of the meeting materials. He reminded members that the Task Force was created by the Executive Director to identify opportunities and make recommendations to the Executive Director on how to increase DEI in the SBI's investment program. Mr. Blumenshine introduced Ms. Gibbons and Mr. Goodwin, co-chairs of the DEI Task Force, to share their initial recommendations as well as provide an update on progress made towards future objectives.

Mr. Goodwin began the discussion noting the large amount of credible data on the benefits of considering investment practices, policies, and beliefs with a DEI viewpoint. Next, Ms. Gibbons stated that the research supports both the economic and performance benefits of having diverse teams. Ms. Gibbons stressed that every step in the Task Force research was as fiduciaries and recommendations of the Task Force was to lead to improved investment results and economic outcomes that benefit plan participants and beneficiaries, the State of Minnesota, and its taxpayers. Ms. Gibbons asked for the Council's input into the Task Force findings. Ms. Gibbons commented on the importance to lean on the consultants to expand the list of DEI managers under

consideration. Ms. Comstock with Aon and Ms. Jones with Meketa commented on advancements their respective firms are making with DEI manager coverage.

Lastly, Mr. Perry discussed next steps with the DEI Task Force recommendations outlined in Tab E of the meeting materials. Mr. Perry stated that he will have further discussions with Meketa, who helped frame the original investment beliefs, and others. Mr. Perry also stated that he would bring any final edits back to the IAC for their input before going to the Board if he decides to update the investment beliefs prior to his retirement.

### ***Meketa Climate Risk Project Report***

Mr. Blumenshine introduced Mr. Emkin and Ms. Bernstein from Meketa who were retained in August 2021 to complete a climate special project that reviews the impact of climate risk and address how best to mitigate its impact on investment assets. Ms. Bernstein stated that this project would be issued in three reports. Phase One - Climate Global Trends, is included in Tab F of the meeting materials. Phase Two will survey global pension plans on how they manage climate risk and opportunities and how they approach investments in order to align with the Paris Climate Accords. Phase Three, Ms. Bernstein noted, will analyze the SBI's current total portfolio exposure to climate risk and opportunities across all of the asset classes and provide options for the SBI to discuss potential implementation for a successful climate transition strategy consistent with the Paris Climate Accords. Ms. Bernstein noted Phase One, Climate Global Trends, covers climate change global outlook, developments on the energy transition away from fossil fuels, how climate change is interacting with financial markets, how climate policies, regulations and institutional collaborations are evolving, and background on available climate data and metrics and risk ratings and analytic tools such as climate scenarios analysis. Through this research, Meketa has found overwhelming evidence that global warming is real and that physical climate risk and the energy transition will affect everything.

### **Report on Combined Funds Portfolio by SBI Consultants**

Mr. Martin introduced the next agenda item, which includes reports from each of the SBI's consultants on the Combined Funds portfolio.

### ***Albourne Partners***

Mr. Christensen, Assistant Executive Director, Investment Strategy and Administration, introduced Mr. Crawford and Mr. Kakoza with Albourne Partners, SBI's private market consultant, to present the information provided in Tab G of the meeting materials. Mr. Crawford began by identifying Albourne's capabilities and the resources available to Staff. Albourne acts as an extension of Staff and helps with back and middle office duties that include custodial reconciliation, and fee reporting and validation, and assists with advisory services with pricing models, asset allocation work, and due diligence on items like ESG and DEI initiatives within private markets. Mr. Crawford noted that Albourne has an established New and Emerging Managers program where they are looking for the next generation of talent and provided information on their diverse manager coverage. Mr. Kakoza provided additional information on the project they are working on with Staff, which incorporates ESG and DEI data collection as part of the SBI's due diligence during the managers fundraising process. He noted a recent initiative at Albourne has been to include further integration of the DEI questionnaire into their operational due diligence process.

### ***Aon Investments***

Mr. Christensen introduced Ms. Doyle and Ms. Comstock of Aon Investments to give their overview of the SBI's portfolio. Ms. Doyle started with comments that they believe the SBI's governance structure follows best practices with the different committees of the Board and the use of investment experts on the IAC to help with investment decisions. Ms. Doyle noted that there are not a lot of U.S. public pension plans with a similar governance structure and believes this structure allows for constructive dialogue and ultimately leads to effective decision-making across the organization and at the Board level. Aon would encourage further discussion with the level of delegation that Staff has in terms of selection of investment managers. Aon surveyed the top fifteen U.S. public pension plans and found the SBI to be at the lower end of the spectrum compared to its peers in terms of the amount of delegation allowed. Currently, in the public markets, Staff has the discretion to allocate dollars and terminate, but require Board approval to hire. Mr. Perry noted that this is a historical practice and that the Board could delegate the hiring of managers to Staff. He also noted that in the future when having the discussion on delegation it should address the benefits and the risks.

Ms. Doyle also stated that Aon would also recommend adopting a formal investment policy statement to use as a guide for the IAC; and given the support they provide to staff, Aon would encourage more interaction with the consultants at these meetings. Ms. Doyle noted that many of the portfolio recommendations have been incorporated since Aon made their initial recommendations when hired. This included increasing the private markets allocation and taking larger sizes at the manager levels, the addition of a return seeking fixed income sub-asset class and ability to fund an opportunistic manager. Lastly, Ms. Doyle noted the shift to passive in areas where active risk is not compelling; mainly within domestic equity and developed international equity.

Ms. Comstock highlighted Aon's thoughts on opportunities and areas of focus for the SBI to consider. These include an allocation to core real estate, additional diversification within private markets, more commitments to private credit and non-core real estate, resources towards an opportunistic asset group, complete a formal asset liability study, active management aligned with Staff's conviction, and periodic review of benchmarks for both public market and private market managers.

### ***Meketa Investment Group***

Mr. Martin next introduced Mr. Emkin and Ms. Jones of Meketa Investment Group to provide their assessment and overview of the SBI's portfolio. Mr. Emkin stated that the most important decision that will impact the portfolio and the highest priorities should be to look at asset liability management across all the portfolios focusing on liquidity and defining risk. Mr. Emkin believes that the IAC and the Board should focus on higher-level items that include strategic asset allocation and structured portfolios and to spend less time on manager selection. Lastly, Mr. Emkin noted that the SBI has had the rare benefit of 35 to 40 years of continuity and history in its leadership and that now is the time to maintain the culture and keep Staff motivated and feeling valued. Mr. Emkin introduced Ms. Jones to provide comments on the Combined Funds portfolio. Ms. Jones suggested revisiting the allocation to active and passive management with a focus towards high conviction active managers. She continued that a reduction in the number of managers in the public equity and fixed income asset classes could provide potential fee savings

and enhance returns. Ms. Jones noted investment opportunities for the portfolio include an inflation protection sub-asset group of Treasury Inflation-Protected Securities (TIPS) and commodities, core real estate portfolio, and other risk mitigating strategies.

### **Executive Director Search Committee Report**

Mr. Martin updated the Council on the Executive Director Search Committee, which is comprised of one designee from each Board Member, the three directors from the Statewide Retirement Systems, and three members of the IAC, which included Mr. Martin as Chair, Ms. Faust and Mr. Wischmeier. Mr. Martin stated three executive search firms responded to the SBI's Executive Search Firm Request for Proposal and he provided a draft timeline of the search process to select Mr. Perry's replacement. Mr. Martin stated the dates are fluid but anticipates a recommendation to the Board for a replacement in July.

### **Adjournment of Meeting**

The motion to adjourn the meeting was seconded and approved by roll call vote. The meeting adjourned at 3:24 p.m.

Respectfully submitted,



Mansco Perry III  
Executive Director and  
Chief Investment Officer