



DRAFT
MINUTES

INVESTMENT SUBCOMMITTEE OF THE SUPPLEMENTAL RETIREMENT BOARD OF TRUSTEES

The regular quarterly meeting of the Supplemental Retirement Investment Subcommittee was called to order at 9:02 a.m., August 23, 2018, by the Chair, State Treasurer Dale R. Folwell, CPA. The meeting was held in the Dogwood Conference Room of the Longleaf Building at 3200 Atlantic Avenue, Raleigh, NC 27604. The Chair indicated there would be a public comment period for organizations and individuals to address the Subcommittee later in the agenda.

Members Present

The subcommittee members present were: Treasurer Dale R. Folwell, CPA, Melinda Baran, and Heyward McKinney (by telephone).

Members Absent

No subcommittee members were absent.

Guests Present

The guests attending were: Billy Weber from Galliard; Will Dillard from Mercer; Michael McCann, Ann Cashman (by telephone), Kelly Keen (by telephone), and Aaron Koval from Prudential Retirement.

Department of State Treasurer Staff Present

The staff members present were: Mary Buonfiglio, Reid Chisholm, Patti Hall, Cathy Jarboe, Rekha Krishnan, Karah Manning, Loren de Mey, April Morris, Maja Moseley, and Steve Toole.

Ethics Awareness and Identification of Conflicts or Potential Conflicts of Interest

The Chair asked, pursuant to the ethics rules, about conflicts of interest of subcommittee members. No conflicts of interest were identified by the subcommittee members.

Minutes from May 23, 2018, Supplemental Investment Subcommittee Meeting

The minutes were approved during the Supplemental Retirement Board meeting on June 21, 2018, and were attached for reference.

Request for Proposals for Investment Consulting Services

The Chair recognized Mr. Chisholm who noted that the current investment consultant's contract was last evaluated in 2014 and will expire on March 31, 2019. The current Invitation to Bid is being conducted jointly with the Investment Management Division (IMD) in order to optimize economies of scale. Mr. Chisholm added that the Evaluation Committee for the supplemental retirement plans (SRP) is comprised of Mr. Toole, Ms. Buonfiglio and Ms. de Mey. IMD will have an evaluation committee as well.

NC Stable Value Portfolio Review

The Chair recognized Mr. Weber. Mr. Weber provided the company update and detailed information regarding the NC Stable Value Fund's performance, quality and cash flow for the quarter. He highlighted the change in the fund's asset balance due to the GoalMaker transition and discussed the replacement of Great-West Life and Annuity Insurance Company by Transamerica Premier Life Insurance Company as contract issuer. Mr. Weber also provided Galliard's forward-looking, 12-month analysis of the potential impact of rising interest rates on the fund's crediting rate and market-to-book ratio, noting that the fund's market-to-book ratio performs well even under the assumptions of significant asset outflows and rising rates.

The Chair inquired whether the fund has underperformed in any given year since inception and Mr. Weber confirmed that, to date, the participants have not experienced any negative returns. Mr. Toole noted that an important feature of the fund is that it allows the participants to receive the book value of their savings in the event of fund's investment manager termination. Ms. Buonfiglio suggested that a three to five year sustainability period be added to the forward-looking interest rate analysis.

Investment Updates

The Chair recognized Ms. de Mey who provided a summary of investment compliance monitoring efforts, noting that all managers were adhering to their respective guidelines and none of the restricted holdings listed in applicable divestment policies were found in the Plans' portfolio. Ms. de Mey noted that a detailed review of the GoalMaker transition will be provided to the trustees during the September board meeting and emphasized the successful outcome of the change.

Ms. de Mey directed the attention of Subcommittee members' to the memorandum included in the meeting materials and stated that the SRP staff recommends termination of PIMCO as the investment manager of the Inflation Response Multi-Asset Fund (IRMAF) due to an increase in the expense ratio, a concern fees may continue to rise with interest rates and limited flexibility and control over of the mutual fund structure. She noted that the recommendation applies to both the Plans and the NC 403(b) Program.

Ms. Baran recalled the background of the Board's initial decision to add PIMCO IRMAF to the investment lineup, and inquired about potential replacement alternatives. Ms. de Mey responded that the staff is reviewing several diversified strategies, which would include TIPS, REITs and commodities, noting that a potential candidate must be a good fit for the GoalMaker product.

The Chair entertained a motion to act upon recommendation, and Ms. Baran so moved. Mr. McKinney seconded and the motion passed unanimously.

Annual Review of the NC 401(k) and the NC 457(b) Stable Value Fund

The Chair recognized Mr. Dillard who provided the analysis data, which included responses from seventeen of the largest collective trust Stable Value providers. He described the main trends that occurred in the first quarter of the year and continued on to review Galliard's company profile and investment philosophy, the NC Stable Value Fund portfolio characteristics, and included remarks about its fee comparison and market-to-book ratio. Mr. Dillard noted that due to Galliard's leveraging of scale, the fund's operating expenses are 33 basis points while the median is 41 basis points. Overall, Mercer views the NC Stable Value Fund favorably and considers it to be a good investment option for the members.

Ms. Baran, Mr. Dillard and Mr. Weber briefly discussed Wells Fargo's (Galliard's parent company) negative headlines associated with the recent legal proceedings. Mr. Weber

emphasized Galliard's autonomy and noted that the current events are being diligently monitored. The Chair added that such oversight is warranted by the Department's corporate governance principles.

2nd Quarter 2018 Investment Performance Report/NC 401(k) and NC 457(b) Plans

Mr. Dillard continued on the executive summary of the NC Supplemental Retirement Plans' investment structure and performance. He provided the market and performance data for the quarter, offering a detailed overview of the economic environment, investment managers' and funds' performances, market sector changes, and fees.

Ms. Baran inquired about Mercer's overall ability to forecast within the industry, given the volatile political environment and Mr. Dillard replied that while the company is aware of the political climate, Mercer's investment focus remains a long-term one. The Chair inquired about Mercer's view regarding the PIMCO recommendation and Mr. Dillard confirmed that the firm is comfortable with the staff's recommendation.

2nd Quarter 2018 Investment Performance Review/NC 403(b) Program

Ms. de Mey reviewed the Program's investment performance, asset balances and allocation for the quarter of the mutual funds within the Program. She noted robust data regarding consumption and strong performance of the domestic equity funds. Ms. de Mey further offered individual, detailed updates regarding the performance of Metropolitan West Total Return Bond, PIMCO IRMAF, T Rowe Price Blue Chip Growth, and the newly added Baillie Gifford International Equity Fund.

Subcommittee Comments

Mr. McKinney thanked Ms. Hall and the staff for expedient delivery of board meeting materials.

Public Comments

No comments were offered.

Adjournment

There being no further business before the Board, the Chair entertained a motion to adjourn. Ms. Baran so moved and Mr. McKinney seconded. The meeting was unanimously adjourned at 10:14 a.m.

Chair

Secretary