

MINUTES

PUBLIC MEETING OF THE ARIZONA STATE RETIREMENT SYSTEM INVESTMENT COMMITTEE

September 21, 2020
1:30 p.m.

The Arizona State Retirement System (ASRS) Investment Committee (IC) met telephonically.

Mr. Kevin McCarthy, Vice Chair of the IC, called the meeting to order at 1:34 p.m.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Kevin McCarthy, Vice-chair – via teleconference
Mr. Clark Partridge – via teleconference

Excused: Mr. Michael Lofton

A quorum of the IC was present for the purpose of conducting business.

Ms. Joyce Williams, ASRS Board Administrator, provided all attendees with telephonic meeting guidelines.

2. Approval of the Minutes of the June 15, 2020 Public Meeting of the ASRS IC

Motion: Mr. Clark Partridge moved to approve the minutes of the March 23, 2020 public IC meeting. Mr. Kevin McCarthy seconded the motion.

By a roll call vote of 2 in favor, 0 opposed, 0 abstentions, 1 excused, and 0 vacancies, the motion was approved. The trustee votes were as follows:

Mr. Michael Lofton – excused
Mr. Kevin McCarthy – approved
Mr. Clark Partridge – approved

3. Presentation, Discussion, and Appropriate Action Regarding Investment Related Matters in the ASRS Board Governance Policy Handbook

Mr. Paul Matson, Director, gave the IC a brief background of the Board Governance Policy Handbook (the Handbook) and discussed the recommended changes to the IC-related items in the Handbook which included minor technical edits, replacing acronyms with complete titles, and clarifying the duties and responsibilities of the General Investment Consultant. Chairman Hillyard asked clarifying questions which were responded to by Director Matson.

Motion: Mr. Clark Partridge moved to accept the recommended revisions to the ASRS Board Governance Policy Handbook and forward it to the full Board for approval. Mr. Kevin McCarthy seconded the motion.

By a roll call vote of 2 in favor, 0 opposed, 0 abstentions, 1 excused, and 0 vacancies, the motion was approved. The trustee votes were as follows:

Mr. Michael Lofton – excused
Mr. Kevin McCarthy – approved
Mr. Clark Partridge – approved

4. Presentation, Discussion, and Appropriate Action Regarding Portfolio Positioning, House Views, and General Discussion

Mr. Karl Polen, Chief Investment Officer (CIO), introduced the topic noting that the ASRS is currently positioned neutrally with equities positioned within 1% of its strategic asset allocation target. He further stated that the investment team had recently rebalanced the portfolio from a prior position of approximately 2% overweight equities. The team believes that a neutral position is warranted in light of valuation analysis and heightened volatility expectations in the coming months. The prior excess equity position resulted from recent high returns and is now held in cash for potential rebalance and liquidity needs.

Mr. Samer Ghaddar, Sr. Portfolio Manager of Equities, presented a macro overview and equity markets information. He reported that economic statistics reflect a gradual recovery from the virus pandemic though unemployment levels remain stubbornly high. The pandemic's economic effects have been mitigated through unprecedented fiscal and monetary stimulus targeted to protect incomes, stabilize credit markets, maintain liquidity, and support asset prices. With respect to equity markets, Mr. Ghaddar noted that the S&P 500 has rallied through the summer, driven primarily by lower interest rate expectations with particularly strong performance in the tech sector. Private equity has seen a large reduction in deal volume. However, the rapid recovery in public equity markets is expected to be reflected in both deal volume and valuations in coming quarters.

Mr. Al Alaimo, Sr. Portfolio Manager of Fixed Income, provided an outlook on credit markets, noting that the ASRS private credit portfolio held up well with minor unrealized write-downs and minimal realized losses. He said that spreads for credit have widened in private markets providing for compelling near-term investment opportunities. He further reviewed interest rate markets with near record-low rates for United States Treasury Securities, which are expected to continue for the foreseeable future.

Mr. Taylor Mammen, Sr. Managing Director and Director of Institutional Advisory Services, RCLCO, presented the real estate outlook noting differential impacts by property type. He noted that multi-family properties have held up well in this recession, with collections and leasing activity experiencing only minor impacts. Stay at home orders have accelerated the trend toward e-commerce, and this is having a positive effect on industrial properties. Office properties have seen limited impact so far with generally long-term leases. However, there is uncertainty regarding office utilization if physical distancing standards remain an expectation in the longer term. Retail and hotel are seeing severe impacts with low occupancy in hotels and many store closures leading to rent collection problems. Mr. Mammen noted that spreads between real estate yields and interest rates have widened, providing attractive opportunities in some sectors. He also pointed out that the hotel sector is under severe pressure, which may provide attractive opportunities for the recapitalization of over-leveraged properties.

5. Presentation, Discussion, and Appropriate Action Regarding Investment Performance

Mr. Polen reviewed investment performance for periods ended June 30, 2020. He noted that total fund returns of .8%, 5.5%, 6.1%, and 8.9% for the one-, three-, five- and ten-year periods were .8%, 1.3%, 1.7%, and 1.2% above the benchmark for the one-, three-, five-, and ten-year periods.

Mr. Ghaddar and Mr. Micheal Copeland, Portfolio Manager for Private Markets, presented information regarding equities performance. Total equity performance was -1.6%, 5.0%, and 6.2% for the one-, three-, and five-year periods. This performance underperformed benchmarks by .3% for the one-year period but outperformed benchmarks by .2% for the three- and five-year periods.

Mr. Mammen reported real estate results for periods ended March 31, 2020, which are included in June 30 total fund results on a quarter lagged basis. Real estate returns of -.8%, 4.6%, 7.1%, and 7.5% for the one-year, three-year, five-year, and inception periods underperformed their benchmarks by 4.6% and .5% for the one- and three-year periods but outperformed by .3% and 1% for the five-year and inception-to-date periods. Mr. Mammen noted the strong performance of categories where ASRS retains investment control rights with inception-to-date returns of 10.2% and 15.6% in the separate account and operating company categories, respectively. The recent underperformance is driven almost entirely by poor performance in a credit portfolio, which held positions in REIT credits, which sold off heavily in the first quarter. The manager of this portfolio has forecast a substantial recovery of these losses.

Mr. Alaimo reported credit results for periods ended June 30, 2020 of 4.4%, 7.3%, 7.5%, and 7% for the one-, three-, five-, and ten-year periods. These results outperformed their benchmarks by 11.3%, 5.8%, 4.1%, and 4.1% for the one-, three-, five-, and ten-year periods. Mr. Alaimo continued his presentation with a discussion of the interest rate sensitive portfolio. He reported that this portfolio earned 9%, 5.4%, and 4.6% for the one-, three-, and five-year periods, which outperformed the benchmark by .3%, .1%, and .3% for the same time periods.

6. Presentation, Discussion, and Appropriate Action Regarding Independent Reporting, Monitoring, and Oversight

Mr. Allan Martin, Partner, NEPC, presented the NEPC oversight. He noted that NEPC reviews ASRS team calculations as presented to the IC to confirm their accuracy and consistency with the State Street official book of record. Mr. Martin reviewed compliance with ASRS board goals, noting full or partial compliance in all cases. He commended the ASRS team for liquidity management during financial turmoil related to the pandemic's onset, maintaining high liquidity throughout. He also noted that ASRS performance compared to other pension plans placed it in the 59th, 26th, 22nd, and 10th percentile for the one-, three-, five-, and ten-year periods.

7. Presentation, Discussion, and Appropriate Action Regarding Risk Management

Mr. Polen presented the risk report from MSCI, noting that the MSCI estimate of value at risk increased to 29% during the quarter ended June 30, 2020.

8. Presentation, Discussion, and Appropriate Action Regarding Compliance

Ms. Kerry White, Assistant Chief Investment Officer for Reporting, Compliance, and Administration, presented the compliance report, noting that there were no instances of non-compliance to report for the period.

9. Presentation, Discussion, and Appropriate Action Regarding the 2021 Investment Committee Meeting Calendar

Mr. Kevin McCarthy reviewed the proposed 2021 IC meeting schedule. There were no alternative dates requested.

Motion: Mr. Clark Partridge moved to approve the proposed 2021 Board IC Meeting Schedule. Meetings are set to occur on the third Monday of the third month of each quarter as follows:

- Monday, March 15, 2021, at 1:30 p.m.
- Monday, June 21, 2021, at 1:30 p.m.
- Monday, September 20, 2021, at 1:30 p.m.
- Monday, December 20, 2021, at 1:30 p.m.

Mr. Kevin McCarthy seconded the motion.

By a roll call vote of 2 in favor, 0 opposed, 0 abstentions, 1 excused, and 0 vacancies, the motion was approved. The trustee votes were as follows:

Mr. Michael Lofton – excused
Mr. Kevin McCarthy – approved
Mr. Clark Partridge – approved

10. Request for Future Agenda Items

No requests for future agenda items were made.

11. Call to the Public

No members of the public requested to speak.

12. The next ASRS Investment Committee Meeting is scheduled for Monday, December 21, 2020 at 1:30 p.m.

Mr. McCarthy noted the next IC meeting is scheduled for Monday, December 21, 2020 at 1:30 p.m.

13. Adjournment of the ASRS IC Meeting.

Motion: Mr. Clark Partridge moved to adjourn the meeting. Mr. Kevin McCarthy seconded the motion.

Mr. Kevin McCarthy adjourned the meeting at 3:42 p.m.

Respectfully submitted by:

Joyce Williams/Karl Polen
Investment Committee Administrator/Chief Investment Officer
ARIZONA STATE RETIREMENT SYSTEM