



# ARIZONA STATE RETIREMENT SYSTEM

3300 NORTH CENTRAL AVENUE • PO BOX 33910 • PHOENIX, AZ 85067-3910 • PHONE (602) 240-2000  
4400 EAST BROADWAY BOULEVARD • SUITE 200 • TUCSON, AZ 85711-3554 • PHONE (520) 239-3100  
TOLL FREE OUTSIDE METRO PHOENIX AND TUCSON 1 (800) 621-3778

*Paul Matson*  
Director

## MINUTES PUBLIC MEETING ARIZONA STATE RETIREMENT SYSTEM INVESTMENT COMMITTEE

June 17, 2019  
1:30 p.m.

The Arizona State Retirement System (ASRS) Investment Committee (IC) met in the 14<sup>th</sup> Floor Conference Room of the ASRS Office, 3300 N. Central Avenue, Phoenix, Arizona 85012.

Mr. Clark Partridge, Chair of the IC, called the meeting to order at 1:30 p.m.

The meeting was teleconferenced to the ASRS office at 4400 E. Broadway Boulevard, Suite 200, Tucson, Arizona 85711.

### 1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Clark Partridge, Chair  
Mr. Michael Lofton

Excused: Mr. Jim Hillyard

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

### 2. Approval of the Minutes of the November 9, 2018 Investment Educational Seminar of the ASRS IC

**Motion:** Mr. Michael Lofton moved to approve the minutes of the November 9, 2018 Investment Educational Seminar of the ASRS IC. Mr. Clark Partridge seconded the motion.

By a 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. Clark Partridge – approved  
Mr. Jim Hillyard – excused  
Mr. Michael Lofton – approved

### 3. Approval of the Minutes of the March 25, 2019 Public Meeting of the ASRS IC

**Motion:** Mr. Michael Lofton moved to approve the minutes of the March 25, 2019 public IC meeting. Mr. Clark Partridge seconded the motion.

By a 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. Clark Partridge – approved  
Mr. Jim Hillyard – excused  
Mr. Michael Lofton – approved

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

Mr. Karl Polen, Chief Investment Officer (CIO), reviewed current portfolio positioning with the committee noting that it remains conservative with a 2.5% underweight in stocks reflecting the low growth environment of the late cycle with asymmetric risks to the downside. Mr. John Kwon, Portfolio Manager of Public Equities, presented house views on equities, noting stretched values in the United States reinforced by strong fund flows. While valuation metrics are more favorable abroad, fundamentals are weaker with higher exposure to trade disruptions. Mr. Al Alaimo, Sr. Portfolio Manager of Fixed Income, Cash, and Liquid Alternatives, presented views on credit and rates, noting that direct lending remains favorable along with non-correlated strategies in insurance, aviation and other markets. Earlier pressure from rising rates has dissipated and the portfolio is now positioned neutrally to duration. Mr. Micheal Copeland, Assistant Portfolio Manager of Real Estate, presented views on the real estate market, noting that space supply and demand is generally in balance across property markets. In some cases, valuations exceed historic norms due to low interest rates and low borrowing costs leading to caution and measured deployment of resources to the sector.

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

The investment team reviewed performance noting the following:

- Fiscal year to date total fund performance is a little over 5% with approximately 1.5% excess performance compared to the benchmark.
- Total fund performance for one, three, five and ten year periods ended March 31, 2019 is 4.7%, 9.3%, 6.8% and 11.3%, respectively. These returns exceeded benchmark returns by 3%, 2.5%, 1.8% and 1.3% resulting in \$1 billion of added value to the fund for the most recent year and nearly \$4 billion for the last ten years.
- Allocation effect was low for the most recent year with gains from underweight equity positions being offset by losses from underweight duration positioning. Allocation effect has been strong over longer periods, particularly from underweights to bonds and commodities.
- Excess returns in asset classes were the primary driver of one year excess performance, with notable outperformance in private equity and credit. Over a five year period, all major asset classes contributed excess performance.
- Mr. Cole Smith, Assistant Portfolio Manager of Equities, presented public equity performance, noting that positive contributions were made from internally managed enhanced passive strategies, which were more than offset by adverse results in index selection and factor strategies. The committee discussed the current investment environment richly rewarding high growth companies which may or may not have earnings. The ASRS portfolio is organized around historically sound parameters which lean the portfolio toward smaller companies with reasonable valuations and positive earnings, a strategy which is out of favor in the current environment.
- Mr. Alaimo reviewed performance in the credit and interest rate sensitive sectors. ASRS credit investments performed well during the sell-off of late 2018 resulting in strong excess performance relative to the benchmark tradable bond index. ASRS core bond investments have performed well over longer periods but recently underperformed due to lower duration positioning, anticipating rate increases that did not materialize.
- Mr. Copeland reviewed private equity and real estate performance noting strong performance in private equity, especially in the recent period of weaker equity markets. Real estate investments have exceeded benchmarks in all time periods reported with strongest performance from the separate account and operating company strategies.

#### **6. Presentation, Discussion, and Appropriate Action Regarding the Real Estate Implementation Plan**

Mr. Gadi Kaufmann, Managing Director, RCLCO, Mr. Taylor Mammen, Sr. Managing Director, RCLCO, and Mr. Jomar Ereso, Managing Director, RCLCO, presented the real estate implementation plan. Their presentation covered the following key points:

- The portfolio will be implemented with target weights of 50% for residential assets, 25% for office assets (including medical office) and 25% for retail and bulk distribution assets.

- The implementation will focus on separate accounts with select direct investments in operators.
- The portfolio with risk managed with diversification across geographic and life cycle with 50% to 75% of the portfolio in a stable status depending on market cycle and other factors.
- The portfolio is expected to generate excess returns of 1.5% per year compared to its ODCE benchmark.

## **7. Presentation, Discussion, and Appropriate Action Regarding Independent Reporting, Monitoring and Oversight**

Mr. Allan Martin, Partner, NEPC, presented results and observations from NEPC's oversight of the ASRS investment program, noting the following key points:

- NEPC has reviewed return calculations from the custodian and ASRS and confirmed their accuracy.
- NEPC reviewed performance compared to board goals, noting that total fund returns have exceeded their benchmarks, asset class returns have generally exceeded their benchmarks, ASRS ranks in the top quartile of public pension plans and adequate cash is maintained to fund benefits.
- NEPC has reviewed asset implementation, confirming compliance with the approved strategic asset allocation.
- NEPC monitors investment process, confirming compliance with applicable rules concerning process and diligence.

## **8. Presentation, Discussion, and Appropriate Action Regarding Risk Management**

Mr. Polen reviewed the MSCI risk report noting that MSCI modeled risk of the ASRS portfolio is in line with the approved strategic asset allocation.

## **9. 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 material instances in non-compliance with public markets trading, private markets monitoring, statutory compliance and restricted country tests.

## **10. Request for Future Agenda Items**

There were no requests for future agenda items.

## **11. Call to the Public**

No members of the public requested to speak.

## **12. The next ASRS Investment Committee Meeting is scheduled for Monday, September 16 at 1:30 p.m., at 3300 N. Central Avenue, 14<sup>th</sup> Floor Conference room, Phoenix, Arizona.**

Mr. Partridge noted the next IC meeting is scheduled for Monday, September 16 at 1:30 p.m.

## **13. Adjournment of the ASRS IC Meeting.**

**Motion:** Mr. Michael Lofton moved to adjourn the meeting at 3:57 p.m. Mr. Clark Partridge seconded the motion.

By a 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. Clark Partridge – approved  
Mr. Jim Hillyard – excused  
Mr. Michael Lofton – approved

Respectfully submitted by:

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