

**Minutes of the Meeting of the Investment Committee  
September 28, 2018**

The Investment Committee of the Tennessee Consolidated Retirement System (TCRS) met on September 28, 2018 in the Cordell Hull Building. The Honorable David H. Lillard, Jr., State Treasurer, called the meeting to order at 9:00 AM. Investment Committee members in attendance included: Treasurer Lillard; Honorable Tre Hargett, Secretary of State; Bill Kemp, Sumner County Clerk; Bob Wormsley, President/CEO of Local Government Insurance Pool. Additional attendees included: Keith Boring, Director of Policy & Research; William Wood, Comptroller's Office; Michael Brakebill, Chief Investment Officer; Derrick Dagnan, Deputy Chief Investment Officer; Michael Keeler, Director of Equity; Thomas Kim, Director of Fixed Income; Daniel Crews, Director of Private Equity; Jennifer Selliers, Investment Compliance Officer; Austin Monsrud, Junior Investment Analyst; Julia Brown, Intern

Treasurer Lillard began the meeting with a motion to approve the minutes from June 29, 2018 and August 28, 2018. The Motion was seconded by Mr. Wormsley and was approved unanimously by voice vote. The Treasurer then called on Mr. Michael Brakebill of TCRS and Mrs. Margaret Jadallah of Verus Investments to give an overview of the Investment Report.

Mrs. Jadallah reviewed the Verus Executive Summary Report, which showed the fund ended fiscal year 2018 with \$49.7 billion in assets. The overview began by describing the key characteristics of 2018 within the markets which included global synchronized growth, low yet rising inflation, and a strong US Dollar. Mrs. Jadallah then stated that GDP growth for the second quarter was recently revised upward to 4.2% and that inflation came in at 2.2% which is above the Federal Reserve's target, implying that rate hikes will continue.

Mrs. Jadallah then reviewed the TCRS portfolio, which returned 8.19% for the year, beating its benchmark by 0.43% and the Allocation Index by 0.79%, in addition to beating actuarial rate of return. Portfolio characteristics highlighted were the neutrality of total plan allocation and the alternative assets underweight compared to the target allocation. As the alternative assets are multi-year strategies, this underweight is expected to converge with the target weightings as the portfolios continue to be built. Mrs. Jadallah concluded by again noting the neutrality of the total plan, stating that it is adhering to the same risks as the benchmark and being implemented in a very risk aware manner.

Mr. Brakebill then introduced the fall semester intern, Ms. Julia Brown, who is pursuing her MBA at Vanderbilt University. Ms. Brown discussed a project that she has been working on with the private equity team involving the concept of replicating a private equity portfolio using public market instruments.

The Treasurer then called upon Mr. Michael Brakebill to review the portfolio and discuss the proposed policy changes. Mr. Brakebill began by stating the value of the portfolio increased by \$2.7 billion during the year while also overcoming net outflows of \$1.1 billion. The alternative asset classes continue growing toward their intermediate target of 7%, with a long-term target of 10%. Regarding changes in the portfolio, Mr. Brakebill highlighted the success of the large cap overlay portfolio (which outperformed by 0.63%), the successful completion of the international

and real estate manager transitions and the recent implementation of a small cap quantitative portfolio.

Mr. Brakebill then gave an overview of the proposed policy revisions. The policy revisions were discussed in context of investment related changes, non-investment changes, and minor editorial changes.

There were six investment related changes related to benchmarks, cash and short term fixed income security management, liquidity, geographic diversification for alternative investments, and co-investment and secondary transactions for alternative investments. A new feature involves liquidity stress testing, which has been performed on an ongoing basis over the past three years and is designed to help monitor risk. This change memorializes a key risk control activity. With respect to geographic diversity and limits for alternative investments, the policy was adjusted to clarify permissible activities and better align alternative investment activity with the intent of geographic opportunities and limitations. Mrs. Jennifer Selliers explained that public asset data is easy to access and monitor whereas alternative asset restrictions must be put in to place during the drafting of a funds legal documents. Mr. Derrick Dagnan continued by stating that the policy changes are to clarify restrictions with respect to public and private investments that had not been explicit before. The final investment related revision improves the flexibility of the alternative asset programs when controlling risks, reducing fees, and exploiting unique investment opportunities through strategies such as co-investment and secondary transactions.

Secretary Hargett asked about the private equity secondary market. Mr. Brakebill described how the market has developed whereby limited partners in funds can purchase, or sell, interests in partnerships. At some point, other limited partners may want to exit a fund that staff finds attractive. For example, in 2009 many groups were forced to sell their interests in quality partnerships at inopportune times and this change would allow for TCRS to take advantage of a situation like that in the future. Mr. Brakebill continued by explaining that there are brokerage firms who act as match-makers and that staff is currently evaluating the capabilities of these firms to either acquire or dispose of LP interests in the future.

Mr. Michael Brakebill then turned to non-investment related revisions in the proposal. The first revision involves the removal of language surrounding the Investment Advisory Council which was dissolved via legislation in 2018. The next revision concerns external pension onboarding, allowing management of assets that do not conform to policy to be accepted in to the group trust. The final revisions are intended to clarify and reduce duplication of conflict monitoring efforts in policy and procedures. Mr. Brakebill then explained that the remaining changes are inconsequential and editorial in nature, including definition changes and other minor corrections.

Treasurer Lillard then stated that the policy updates are in accordance with best practice and with legislative changes. Mr. Bill Kemp asked for more clarity on the geographical policies in place surrounding investment activity in the State of Tennessee. Mr. Brakebill replied by stating that direct investment in Tennessee real estate is not allowed, and staff believes the policy language is adequate. Mr. Dagnan elaborated and stated that the current changes in policy impact comingled alternative investments where TCRS is a minority partner. Mr. Brakebill concluded by saying that

there are systematic ways staff evaluates direct real estate investments, and that the Investment Committee would be made aware of any relevant issues.

The Treasurer motioned to approve the revisions to the investment policy and was seconded by Secretary Hargett. The motion was approved by a unanimous voice vote.

The Treasurer then adjourned the meeting at 9:47 am.

Respectfully submitted,

Michael Brakebill  
Chief Investment Officer

APPROVED:

/s/David H. Lillard, Jr.  
David H. Lillard, Jr. Chairman  
TCRS Board of Trustees