Minutes of the meeting held on December 11, 2017

Present: Francis Murphy - Chair, Jim Monagle, Michael Gardner, John Shinkwin, David Kale, Ellen Philbin, Rafik Ghazarian, and Chris Burns.

Left Early: Nadia Chamblin-Foster (Left following BlackRock presentation)

The meeting was called to order at 1:05 PM. The meeting was digitally recorded.

Agenda Item # 1 – Manager Reviews
Ghazarian reviewed Segal Marco's written analysis of investment performance for the period ending September 30, 2017. The third quarter saw positive returns across all asset classes. Overall, the Total Fund was valued at $1.297 billion, representing a gain of 3.5% during the quarter. The fund underperformed with the policy index return of 3.64%. Returns to date in the 4th quarter have been strong. Ghazarian noted it was possible that the system could return 14% for the full year. Reviewing individual managers, Ghazarian noted that both Aberdeen and Lazard were short of their benchmark over the last year.

Ghazarian reviewed the fund's asset allocation. The fund remains overallocated to equities, with new managers in real estate and timber waiting to be funded. The new infrastructure manager, IFM, called the system's full commitment, bringing that sleeve in-line with the target allocation.

Ghazarian reviewed a memo he had written describing potential changes to the domestic equity sleeve. At present, the sleeve has five funds. They are Russell 1000 Growth and Russell 1000 Value, both managed by Rhumbline; S&P 500 and Russell 2500 Growth, both managed by SSGA; and an active Midcap Value fund managed by Wedge. The system will be required to issue RFPs for the Wedge and SSGA funds within the next year, due to Chapter 176 requirements. Ghazarain stated that the Board may wish to consider consolidating those funds before issuing any RFPs. At present, the system pays about $600,000 in fees to these managers. Ghazarian reviewed three potential options:

1. Issue a search for a Russell 1000 core index fund by consolidating the Russell 1000 Growth, Russell 1000 Value and S&P 500 fund.
2. Issue a search for a Russell 1000 core index fund by consolidating the Russell 1000 Growth, Russell 1000 Value and S&P 500 fund and issue a search for a Russell 2000 index fund by consolidating the Russell 2500 Growth fund and half the Wedge fund.
3. Issue a search for a Russell 1000 core index fund by consolidating the Russell 1000 Growth, Russell 1000 Value and S&P 500 fund and issue a search for a Russell 2000 index fund by consolidating the Russell 2500 Growth fund and the entire Wedge fund.

Ghazarian noted potential advantages to the consolidation. It would result in fewer managers to supervise and save on fees. By eliminating separate growth and value funds, it would eliminate the duplicate holdings between those funds. He stated that there seems to be little advantage in holding both growth and value funds. While one fund may temporarily be favored over the other, over the long term, this tends to balance out. Ghazarian also presented a report showing the system's history of using active managers in the domestic equity sleeve over the last twenty years. He noted that the system seems to have seen neutral-to-negative returns with active managers. Ghazarian described the difference between the various Russell index funds, and which market capitalizations each one focuses on. He stated that Segal would recommend using both the Russell 1000 and Russell 2000 in order to maintain an appropriate allocation to small cap stocks. Gardner stated that he would favor the third option, stating that the system has benefited from a move toward indexing. Chamblin-Foster noted that the searches under Option 3 would appear to cover the funds currently managed by Rhumbline, which is currently the only minority owned business within the fund. They manage 19% of assets. She stated that she would want to consider that carefully when evaluating the responses to the search.

Kale asked if the memorandum was developed in response to Cambridge's concerns, or if Segal was making similar recommendations to other clients. Ghazarian stated that among his clients, about 50% are invested primarily in passive funds, and that he has prepared similar reports for other clients.

Gardner moved to request that Segal issue RFPs to reallocate the domestic equity sleeve in accordance with the third option in the memorandum. Shinkwin seconded the motion and it was voted unanimously. Ghazarian stated that, in addition to the equity searches, the system would also have to issue RFPs for the fixed income managers, Pyramis and IRM, within the next year. The Director stated that she would also issue an RFP for an investment consultant in 2018, as required by Chapter 176.

Erin Lane and Leo Chenette represented BlackRock. A written review of the portfolio was presented to the Board. There have been no changes to the investment strategy or the management team at BlackRock. Chenette described the firm's growth over the last year, but stated that they were not having issues finding new investment opportunities. He noted that prices were high, but the firm remains selective and has expanded to invest more outside the US. Cambridge currently has investments in DivPEP Fund II and DivPEP Fund V. Both funds have performed well. Chenette reviewed the construction of the portfolios. The DivPEP portfolios are primarily fund-of-funds, but about one-third of the portfolio is direct co-investments, and a smaller amount in secondaries. Fund II is well into the harvesting phase. Cambridge committed $10 million to the fund. The portfolio currently has a net IRR of 10.7%, and has returned over $15 million in distributions to Cambridge since inception. Chenette stated that he was considering offers to liquidate the fund by selling the tail-end assets on the secondary market. Fund V is entering the harvesting phase. Cambridge has committed $6.5 million, and paid in $4.4 million. The first distribution from this fund was paid in November. The firm is likely to call an additional $1 million over the next two years. The fund differs from Fund II, in that it includes some investments in energy funds, and also includes investments in Asia and Latin America. The fund is heavily weighted toward buyouts, with smaller amounts in energy, venture capital and distressed debt. The fund is about 15% direct co-investments, with the rest structured as a fund-of-funds. Fund V is likely to run another ten years, ending around 2028. The firm is now offering a fund which participates only in co-investments, which allows them to charge lower fees. The firm will also raise a new fund-of-funds in 2018.

Tim D'Arcy and Jackie Rantanen represented Hamilton Lane, with Rantanen participating by phone. A written overview of the portfolio was presented to the Board. Cambridge has investments in Fund VI and Fund VIII. D'Arcy described the firm's work as the private equity consultant for the PRIT fund. As of March, Hamilton Lane is a publicly traded company. The firm is still 75% employee owned, with the remaining shares traded on the NASDAQ exchange. Cambridge made a $10 million commitment to fund VI. The fund has a 9% net IRR. The fund is well into the harvesting phase. The fund is weighted toward buyouts, and to investments in North America. Gardner noted that the system is currently paying 330 basis point in fees since inception. Rantanen noted that the spread between gross and net returns would narrow as the portfolio winds down. Hamilton Lane will not make any further capital calls on this fund. Cambridge has committed $6.5 million to Fund VIII. The fund is now fully committed although the underlying managers are still making investments. The fund has drawn 67% of the commitment. The portfolio has a net IRR of 6.8%. The fund currently lags the public markets, but Rantanen stated that she expected performance to improve as the underlying funds mature. This fund is not as heavily weighted toward buyouts, with larger amounts of distressed debt and venture capital. D'Arcy described the fee structure in more detail. Hamilton Lane charges 72 basis points, but many of the underlying managers charge 200 basis points, plus a 20% incentive fee for strong performance.

Mark Andrew and Lee Tesconi represented Lexington Capital Partners. A written review of the portfolio was presented to the Board. There have been no changes to the portfolio management or strategy over the last year. Andrew reviewed the history and growth of the firm, noting their history of strong returns. Tesconi reviewed the LCP VIII portfolio. Most of the funds are buyout-focused and based in the United States. The fund closed with $10.1 billion in commitments, and has made investments totaling $7.7 billion to date. Lexington used a credit facility to fund early investments, at a very favorable interest rate. Tesconi stated that he felt the use of leverage in this fund could add up to 300 basis points of returns. The fund is well diversified by vintage year. Strategically, the fund is weighted toward buyouts and US funds. The fund comprises 50 separate transactions, acquiring 373 partnership interests. The fund will likely make its final acquisitions by mid-2018, and the begin fundraising for their next fund. Cambridge's commitment to the fund was $20 million, with $10.4 million called to date. The fund will likely draw close to the full commitment, including amounts in late 2018 to pay off the credit facility.

Michael McGirr and Paul Todisco represented the PRIT Fund. A written portfolio report was submitted to the Board. Todisco reviewed changes to the Advisory Committees membership, and staffing changes in the office. He stated that PRIT was currently reviewing their asset allocation strategy, and would likely make changes in the beginning of 2018. Over the last year, the total fund has returned 13% gross of fees. Private equity returned 23.5% and hedge funds 8%. Todisco stated that hedge funds were the best performing asset class on a risk-adjusted basis. He described the continued move to managed accounts within the hedge fund sleeve, which has resulted in fee savings.
McGirr reviewed the performance of the private equity sleeve. He noted that PRIM is now making a number of direct co-investments, which allows the system to save on fees. The system has made six direct investments to date. The co-investments are made alongside the highest-performing general partners of existing funds. The vast majority of the portfolio remains invested through funds, where PRIT is a limited partner. Going forward, PRIT has targeted up to 10% of the sleeve be in co-investments. The fund is focusing new investments on small buyouts and venture capital. Overall, the private equity sleeve is weighted 74% to buyouts with the rest in venture capital. Todisco reviewed the last three years of private equity investment targets. In 2015, PRIT committed $1.492 billion, short of the target of $1.7 billion. In 2016, PRIT has committed $750 million, short of the target of $1.4 billion. For 2017, PRIT targeted $1.4 billion, and committed $1.404 billion. McGirr stated that he expects in 2018 to mostly recommit to follow-on funds from well-performing managers, adding only one or two new managers. Todisco stated that the private equity managers tend charge about 130 basis points, plus a 20% incentive fee on profits. He stated that the PRIT's financial statement would provide more specific information.

Eric Dooley and Logan Roise represented Hancock Timber. A written overview of the portfolio was presented to the Board. Dooley stated that he was aware that Cambridge has a pending investment in Hancock timber/farmland fund, but that his presentation would cover only the existing investment in Hancock Timberland X. Dooley reviewed the structure of the Hancock Natural Resource Group, noting different subgroups investing in timber, farmland and renewable energy. He also reviewed staffing changes. The portfolio is now fully invested, and in the holding period. The fund will begin to wind down in 2023. Cambridge committed $6 million and the entire amount has been called. The fund has made $1,000,000 in distributions. The current value of the fund is appraised at $8.6 million. The total portfolio consists of just under 500,000 acres of timberland. The properties are located in the Pacific Northwest, Louisiana and Queensland, Australia. Distributions are made based on sales of harvested timber, as well as some small land sales. The fund has generated a nominal IRR of 7.8%, and outperforms the NCREIF Timberland index since inception. In the last year, returns have come mainly from land value appreciation, with some income from timber sales. Dooley noted that the portfolio is likely to benefit from tariffs imposed on Canadian softwoods earlier in the year. Dooley reviewed the economic outlook for timber products. He noted that US housing starts continue to trend upward, although they remain below their long-term average. Dooley stated that he believes that there is still a pent-up demand for new housing. A recession or slowdown in construction would have a significant impact on profits. Chinese lumber imports continue to rise, with New Zealand and Australia exporting more.

The Board reviewed a written analysis of the system's investments in private equity. Ghazarian stated that Segal performed a cash flow analysis after speaking with managers and getting their input about likely capital calls and distributions. Based on this analysis, the system will likely remain underallocated to private equity until 2021. For 2018, Segal recommends that the system commit $33 million to the PRIT private equity fund. Ghazarian stated that it appears that PRIT would be able to draw close to the full commitment in 2018. He stated it is important that the system continue to run a cash flow model every year to adjust for any commitment shortfall.

Gardner moved to invest $33 million in the PRIT 2018 private equity fund. Monagle seconded the motion and it carried on a 4-0 vote, with Chamblin-Foster absent.

Ghazarian distributed materials describing Segal's service of managing proxy votes on behalf of clients. He noted that most of his union clients used it, and that it was becoming more popular with public funds. He offered to set up a presentation with Maureen O'Brien, who manages the service. He noted that the service could only be applied to equity fund separate accounts. Pooled funds will not allow clients to vote their individual shares.

Monagle moved to adjourn at 3:45 PM.