

**NORTH CAROLINA DEPARTMENT OF STATE TREASURER  
INVESTMENT ADVISORY COMMITTEE  
MEETING MINUTES FOR February 24, 2021**

Time and Location: The Investment Advisory Committee (“IAC” or the “Committee”) met on Wednesday, February 24, 2021, at 9:00 a.m. via conference call and GoToWebinar.

Members Present: State Treasurer Dale R. Folwell (Chair), John Aneralla, Lentz Brewer, Michael Mebane, Greg Patterson, Loris Colclough via Webinar.

Staff Present (in person and virtual): Ben Garner, Casey High, Gail Kadash, Kathy O’Neill, Matthew Krimm, Christopher Morris, Jeff Smith, Brett Hall, Rhonda Smith, Greg Taylor, Jack Wilson, Joe Farley, Loren de Mey, Ron Funderburk, Ty Powers, Meryl Murtagh, Anne Roof, Deana Solomon, Fran Lawrence, Michael Nichols, Nicholas Langley, Chris Ward, Brian Bolcar, Brian Jackson, Tinh Phan, Renee Guerin, Craig Demko, Elizabeth Hawley, Frank Lester, Joan Fontes, Laura Rowe, Thomas Causey, Dan Way, Molly Kovacs, Powell Baggett, Stewart Sturkie.

Others in Attendance: G. Scott Kreft, Ben Beaulieu (BlackRock), Robert Bartilucci (NYU), Chris Smith (NCSU), Lindsay Saienni, Lindsay Rouff (Voya), Ulf Marxen (Strategas), Daniel Clifton (Strategas), Michael Reeves, Emily Raby (Pageant Media), Robin Clifford.

**AGENDA ITEM – OPENING REMARKS**

The meeting was called to order at approximately 9:03 a.m. by Treasurer Folwell. Meeting etiquette information, and Webinar/Conference line use was shared.

The Treasurer confirmed that a quorum was met, then asked the Members present to declare any conflicts of interest and, there being none declared, the meeting commenced.

**AGENDA ITEM – APPROVAL OF MINUTES**

Mr. Patterson moved, Mr. Brewer seconded, and there was a member roll call to approve the minutes. The minutes were approved.

**AGENDA ITEM – PERFORMANCE UPDATE**

The Chair recognized Jeff Smith, Co-CIO and Director of Fixed Income, and Chris Morris, Co-CIO and Chief Risk and Operating Officer, to present the Performance update.

Mr. Smith provided a brief update on the cost efficiencies initiative underway in the Investment Management Division (IMD). He noted good results as the initiative has realized \$350 million of savings since January of 2017, exceeding the 4-year goal of \$100 million.

Mr. Smith provided an update on the U.S. economic environment for the 4th quarter of 2020, mentioning the current quarter changes.

Mr. Morris presented an update on Assets Under Management (AUM), as of December 31, 2020. He stated the total AUM was \$156.4 billion, up \$8.3 billion since the 3rd quarter. The NCRS market value increased by \$7.5 billion.

Mr. Morris reviewed the asset allocation as of December 31, 2020. He noted the over- and underweights, particularly within the Growth and Rates and Liquidity sleeves. He also discussed how those over and underweights have changed quarter over quarter as equity markets rallied.

Mr. Morris presented the Total Net Portfolio Returns vs. Benchmarks slide, discussing the periodic performance from both an absolute and relative perspective across multiple time horizons.

Mr. Morris discussed the Growth of a Dollar Charts that illustrate how the total pension and alternatives sleeve have performed relative to the long-term policy benchmark over the 5- and 10-year periods, and since 1997, the start of the NCRS performance record.

Mr. Morris moved onto the Contribution to Total Plan Return slide. He discussed the dollar amount each asset class contributed to the earnings of the plan for the prior 1-year period, noting the strong gains in Investment Grade Fixed Income and in Public Equity, followed by Private Equity.

Mr. Morris next walked the committee through the Net of Fees Return Attribution charts, noting the portfolio outperformed the benchmark by 0.03% over the 1-year period. He discussed how the selection effect added value, while the allocation effect detracted value over all three-time horizons.

Mr. Morris presented the Net of Fees Risk Metrics slide variety of metrics. He pointed out the spike in volatility creating an interesting year.

Mr. Morris discussed the peer universe comparison slides, which show our percentile rank, and which is still quite favorable relative to peers when considering return and risk.

Mr. Morris moved on to the liquidity slides, hitting on the structural liquidity, benefit payments, and cash flows within the Alternatives sleeve.

There was a discussion on the expectation of higher benefit payments in the future as retirements increase and with the now lowered actuarial rate of return.

Mr. Smith reported on Asset Class Performance and spoke about the Calendar Year Asset Class Return chart, highlighting the strong performance in Public Equity, Private Equity, and Investment Grade Fixed Income. He pointed out that calendar year 2020 is the first year in the chart where Public Equity and IG Fixed Income were both toward the top of the performance rankings and no inflation showing up now.

Mr. Smith next discussed new and incremental investments and the current level and continued downtrend of unfunded commitments.

Mr. Smith moved along to Asset Allocation History and the Top 20 Investment Managers slide, noting that there have been no material changes to either slide since the prior meeting.

## **AGENDA ITEM – PUBLIC POLICY OUTLOOK**

Mr. Dan Clifton, of Strategas, was introduced to provide an economic review.

Mr. Clifton provided a political review of impacts across economy and investment activity.

Mr. Clifton discussed that the federal election has removed the party of power in 7 of the past 8 elections. He discussed the political power volatility and how social and economic dynamics are driving further polarization.

Mr. Clifton discussed four transformational events in 2020: recession, pandemic, social unrest, and the elections.

Mr. Clifton believed inflation concerns mirror those in 1968. However, economy is not sole issue as in 1968. Mr. Clifton went on to discuss voting history and margins.

Mr. Clifton continued to discuss the impact of the stimulus bill and, specifically, that another stimulus is coming as the bond market declares COVID is over. There is weakness in climate change stocks notwithstanding the fact that Biden is the first climate change President that we have ever had.

Mr. Clifton also mentioned that we can expect tax increases. He compared Biden's tax plan as similar to 1968 as part of the war on poverty.

Questions included impact of mortality spike as related to funding status or pension liability.

The Treasurer thanked Mr. Clifton for his report and introduced Ronald Funderburk for an asset class review.

### **AGENDA ITEM – INFLATION SENSITIVE ASSET CLASS REVIEW**

Mr. Funderburk gave an overview of how Inflation Sensitive plays a role in the portfolio, how the strategy has evolved and diversified over time, and the benefits of the evolution.

Mr. Funderburk reviewed the decrease in the unfunded amount and discussed the reasonable underweight of target allocation. He next discussed the vintage and strategy diversification for the portfolio.

Mr. Funderburk reviewed the portfolio's performance over various time horizons. He mentioned that over the long-term, the portfolio has outperformed its benchmark. In the shorter term, the portfolio underperformed its benchmark due to flaws in the benchmark construction. The benchmark utilizes Treasury Inflation Protected Securities (TIPS), which increase in value when interest rates decline or markets experience weakness, while prices of most risk assets decline during the same market weakness. Mr. Funderburk noted that Covid-19 caught many investors off guard last year. Additionally, energy markets were negatively impacted because of Covid-19; Russia and other leading energy nations began increasing energy supplies. Although the commodity and energy markets have recovered substantially, additional recoveries are expected as the economy reopens. He also mentioned the quarter lag in reporting has negatively impacted relative results but expects improved relative performance in the coming quarters as private valuations begin to reflect the current environment and re-opening of the economy.

Mr. Funderburk stated his outlook for technical advancements and subsequent potential impact on inflation expectations. He mentioned that the strong housing demand and low housing inventory may increase inflation expectations as housing costs represent a large portion of CPI (Consumer Price Index).

Mr. Funderburk presented that, looking forward in 2021, investment staff plans are to rationalize manager lineup and focus on high conviction opportunities. Vintage and strategy diversification is a risk reduction method that should continue to be employed. Mr. Funderburk mentioned portfolio gaps and investment strategies that would add value: cell towers, data infrastructure, music royalties, real estate, and various stores of value.

Mr. Funderburk concluded his presentation and opened for questions. There were no additional questions from the IAC or the audience.

### **AGENDA ITEM – Governance, Operations, & Investment Practice Review**

Mr. Morris next presented on the recent study and report completed by Aon Investments. Aon recently completed a statutorily required governance and operational review, which included both a review of main policies and investment practices and also various recommendations. The specific policies under review were the NCRS Investment Policy Statement, Investment Management and Vehicle Monitoring and Termination Policy, and the External Management Selection Policy. Aon found our policies to be comprehensive and in line with peers and best practices. The compliance review suggested that further segregation of staff duties should be considered, especially with respect to operations versus portfolio management functions. The report also showed that our Department is doing very well with respect to compliance, transparency, accountability, and ethics. Mr. Morris stated that we will review and apply these recommendations as appropriate.

### **AGENDA ITEMS – IAC MEMBER Q&A**

IAC Members were provided with the opportunity to pose questions to the Treasurer and IMD staff.

Mr. Aneralla had one question regarding to whom the Insider Trading Policy applies; legal counsel confirmed.

The Treasurer asked Ben Garner and Jeff Smith to provide information on recent personnel updates.

Ben Garner advised of Meryl Murtagh's departure and thanked her for her years of service as counsel to the Investment Division.

Jeff Smith advised of Jack Wilson's upcoming departure and thanked him for his contributions to the Real Estate team over the last few years.

There were no additional comments.

### **AGENDA ITEM – PUBLIC COMMENT**

No one signed up for public comments.

### **ADJOURNMENT**

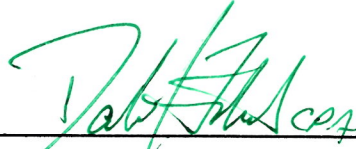
The IAC board members all thanked the Treasurer and his staff and expressed appreciation for the insightful review by Strategas.

The Treasurer next thanked Jeff Smith, Christopher Morris, and the IMD team for stepping up for their roles, and stated his tremendous amount of confidence in, and appreciation for the stability of, the Investment Management Division. The Treasurer then requested a motion to adjourn the meeting.

Mr. Patterson motioned to adjourn. Mr. Aneralla seconded the motion.

Mr. Colclough, Mr. Brewer, and Mr. Mebane all agreed to adjourn.

The Treasurer officially adjourned meeting at approximately 11:12 am.



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**DALE R. FOLWELL, CPA**  
**NORTH CAROLINA STATE TREASURER AND CHAIR**