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3 NEW YORK CITY TEACHERS' RETIREMENT SYSTEM

4 INVESTMENT MEETING

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7 Held on Thursday, February 7, 2019, at 55 Water

8 Street, New York, New York

9

10 ATTENDEES:

11 JOHN ADLER, Chairman, Trustee

12 THOMAS BROWN, Trustee

13 DEBRA PENNY, Trustee

14 SUSANNAH VICKERS, Trustee, Comptroller's Office

15 DAVID KAZANSKY, Trustee

16 PATRICIA REILLY, Teachers' Retirement System

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18

REPORTED BY:

19 YAFFA KAPLAN

JOB NO. 2467349

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2 ATTENDEES (Continued):

3 SUSAN STANG, Teachers' Retirement System

4 RON SWINGLE, Teachers' Retirement System

5 ROBIN PELLISH, Rocaton

6 MICHAEL FULVIO, Rocaton

7 MATT MALERI, Rocaton

8 PAUL RAUCCI, Teachers' Retirement System

9 VALERIE BUDZIK, Teachers' Retirement System

10 LIZ SANCHEZ, Teachers' Retirement System

11 SHERRY CHAN, Office of the Actuary

12 DAVID LEVINE, Groom Law Group

13 CYNTHIA COLLINS, Mayor's Office

14 SUMANTE RAY, Mayor's Office

15 SANFORD RICH, BERS

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2 MR. ADLER: Good morning, everybody.
3 Welcome to the Teachers' Retirement System of
4 the City of New York investment meeting for
5 February 7, 2019.
6 Patricia, will you please call the roll?
7 MS. REILLY: John Adler?
8 MR. ADLER: I am here.
9 MS. REILLY: Thomas Brown?
10 MR. BROWN: Here.
11 MS. REILLY: David Kazansky?
12 MR. KAZANSKY: Present.
13 MS. REILLY: Lindsey Oates? Debra
14 Penny?
15 MS. PENNY: Here.
16 MS. REILLY: Susannah Vickers?
17 MS. VICKERS: Here.
18 MS. REILLY: We do have a quorum.
19 MR. ADLER: Thank you very much. So as
20 our usual custom, I will hand it over to
21 Rocaton.
22 MS. PELLISH: Yes. I am just going to
23 -- I feel like we are a little bit -- I will
24 have to shout, so I am just going to move
25 forward a little bit. I want to introduce my

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2 colleague Matt Maleri who is hopefully going
3 to follow me. We will see. And you have met
4 Matt before I believe, and Matt is part of a
5 number of efforts at Rocaton, but he is here
6 in his role as part of the asset allocation
7 team. And since there was, as you know, a
8 resolution discussed at the CIM yesterday
9 regarding beginning an asset allocation study,
10 we thought this might be a good opportunity to
11 talk to you about our capital market
12 assumptions, look at our capital market
13 assumptions as of year-end versus those that
14 we used in the last asset allocation study.
15 Of course, this is one small step in the whole
16 process, and we will be collaborating closely
17 with the Bureau of Asset Management on this
18 process and going over the assumptions. We
19 thought it just might be an opportune moment
20 to set the stage.

21 So with that, we will start with the
22 Passport Funds's December review. Everyone
23 should have that performance deck as of 12/31.
24 You can see as year-end the -- well, very
25 difficult performance during December and we

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2 went through that at the CIM yesterday, and I
3 think everyone is well aware of that. I will
4 say that relative to the Russell 3000, the
5 Diversified Equity Fund benefited from its 10
6 percent allocation to the defensive strategies
7 composite, which was down about 60 percent of
8 the Russell 3000 decline. So it did its job
9 in the month of December.

10 So for the month, the return of the
11 Diversified Equity Fund was negative 8.24
12 percent compared to the Russell 3000 return of
13 minus 9.3 percent. For the calendar year,
14 that means that the Diversified Equity Fund
15 had a negative return of about 7.3 percent,
16 and that is about 200 basis points below the
17 Russell 3000. Primary contributor to that
18 below US market return is, of course, the
19 approximately 20 percent allocation to
20 international equities, and as we are all
21 aware, international equities significantly
22 underperformed the Russell 3000 from the
23 dollar-based investor's perspective during
24 2018. In addition, we did have
25 underperformance by the actively managed US

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2 composite, and we will be talking about that
3 composite in additional detail later on.
4 What I wanted to also note here is that
5 for the month of December, the Balanced Fund
6 fell by about 1.4 percent. So for the
7 one-year return, that's a negative 2 percent.
8 The International Equity Fund, as we first
9 noted, underperformed for the year but for the
10 one-month period in December actually
11 outperformed the US equity market by -- it was
12 a loss about 4 and a half percent. Compared
13 about half of the loss of the US equity market
14 during that month. The Inflation Protection
15 Fund, which has exposure to the US equity
16 market lost about 3 and a half percent, and
17 the Socially Responsive Fund followed the S &
18 P 500's return with a loss of over 9 percent.
19 So a very difficult month for December.
20 We can talk more about the month of
21 December or we can turn to January. I vote
22 for turning to January.
23 MR. KAZANSKY: Before we do though, I do
24 want to note and appreciate the fact that the
25 defensive composite really did its job --

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2 MS. PELLISH: Yes.
3 MR. KAZANSKY: -- in December.
4 MS. PELLISH: Yes. Any other comments
5 or questions on December? Hearing none, we
6 have preliminary performance.
7 MR. ADLER: I don't think I have that
8 page. Is it possible --
9 MS. PELLISH: No, I have it. It was
10 just done the other day.
11 MR. ADLER: I am still dizzy from the
12 roller coaster.
13 MS. CHAN: The market roller coaster?
14 MR. ADLER: Yes, the market roller
15 coster. Or the V shape as they referred to it
16 yesterday.
17 MS. PELLISH: So as you all heard in the
18 CIM yesterday, a very significant rebound in
19 January, and Mike talked about some of the
20 reasons behind that but just to note the
21 numbers for the month of January, the Russell
22 3000 was up 8.6 percent. So again, up 8.6
23 percent in January, down 9.3 percent in
24 December. The International Composite
25 benchmark lagged the US equity market in

1 Proceedings
2 January by about 200 basis points. So up
3 about 6.7 percent. Where the Defensive
4 Strategies benchmark earning about the same
5 amount and so we -- our best guess for the
6 benchmark return for January is positive 8
7 percent. So that same hybrid benchmark was
8 down 8 percent in December, up 8 percent in
9 January. You know, what's really -- what I
10 always find very interesting is looking at the
11 impact even on longer term numbers of rolling
12 out one month.
13 So if we look at the five-year average
14 annual return for the Russell 3000 index
15 ending January 31, 10.4 percent. So you gain
16 a month, a mere month, and lose a month five
17 years ago. If you look at the same number as
18 of 12/31, it's 8 percent. That's a huge
19 difference. Two hundred basis points on a
20 five-year average annual number.
21 MR. ADLER: That's amazing.
22 MS. PELLISH: And that's the impact of
23 volatility. I mean, that's sort of one way to
24 look at it. If you look at the Balanced Fund
25 benchmark, that was also up about 3 percent in

1 Proceedings
2 January. International equities I already
3 noted rebounded. Not to the extent of the US
4 equity market but still pretty strongly. Our
5 International Composite benchmark rebounded by
6 almost 7 percent. And we can see the Real
7 Return Mutual Fund was up over 4 percent, and
8 the Neuberger-Berman Socially Responsive Fund
9 was up almost 8 percent. So strong rebound in
10 January. February, do we have to date?
11 MR. MALERI: You are sort of up for the
12 first few days but not quite as exciting as 8
13 percent.
14 MS. PELLISH: So certainly a return -- I
15 mean, this is extreme volatility in one month,
16 but I think as we launch into a discussion of
17 the asset allocation study, we are certainly
18 mindful of the need to discuss how volatility
19 going forward may affect our decisions around
20 that policy.
21 MR. ADLER: Also speaks to how much the
22 end point that you look at is so -- has so
23 much effect on, you know, what the returns are
24 that even a month's difference in the end
25 point makes this kind of --

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2 MS. PELLISH: Huge difference.
3 MR. ADLER: -- huge difference.
4 MS. PELLISH: And the only way -- the
5 best way to deal with that is look at rolling
6 periods of time.
7 MR. ADLER: But even rolling returns as
8 you pointed out the five-year --
9 MS. PELLISH: So when we present manager
10 returns to you, one of the things we try to
11 present is this graph that shows rolling
12 five-year returns or three-year returns at
13 different end points, so it isn't quite as
14 significant an impact but it's -- and it also
15 -- it's also -- that end point dependency is
16 exacerbated by the fact that humans tend to
17 anchor onto recent experience and project that
18 over forward. You overweight recent
19 experience and the whole thing gets
20 exacerbated and you really try to repeat the
21 last five years. Of course, that's rarely
22 successful.
23 MR. ADLER: Right. And one of the
24 things you guys often say to us I think is
25 that truthfully recent performance in terms of

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2 markets -- not necessarily manager but
3 sometimes managers too doesn't -- generally
4 means like if there is a low point, that's
5 when you want to buy. Not oh, you know,
6 international has done so poorly so let's
7 leave international. It's really the opposite
8 that you want to go into.
9 MS. PELLISH: Unless you can identify a
10 fundamental reason why you think that
11 performance will persist, which is hard to do.
12 So unless there is any more questions about
13 performance, maybe we can launch into our
14 capital market assumptions.
15 So just to remind everyone, we have
16 capital market assumptions that we update
17 every quarter and more often if there is an
18 extreme event, and these capital market
19 assumptions form the basis of the projections
20 of asset classes, that is -- that are used
21 when we think about how we might want to alter
22 our strategic asset allocation policy. We
23 collaborate with BAM who is also using all of
24 the other consultants' capital market
25 assumptions, so we discuss those assumptions

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2 and you know, we have flexibility so if there
3 is a -- if there is a compelling argument to
4 modify some of them, we will happily do so,
5 but these are the assumptions that we
6 developed as of year-end, and they will form
7 the basis of our discussions with you and BAM.
8 MR. MALERI: Great. Good morning. So I
9 guess just to start, if I had to boil down our
10 assumptions in maybe one or two sentences,
11 it's really simple. When markets have done
12 well, our assumptions go down, and when
13 markets have done poorly, our assumptions go
14 up. So I can leave it there and call it a
15 day, but I think you want a bit more detail as
16 to how we actually build the assumptions, but
17 to the point that was made earlier when
18 markets have done well like we have
19 experienced, notwithstanding the fourth
20 quarter, that generally means our outlook
21 going forward is lower. You should expect
22 lower returns after you just experienced very
23 high positive returns, and the opposite is
24 true as well. When markets perform poorly,
25 our expectation is from that point forward you

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2 should experience greater returns. So that's
3 the general framework for how we create
4 assumptions.
5 I will start on page 3. There is a lot
6 of words on that slide, so I will try to boil
7 it down to just some of the key takeaways
8 there. The first that is really, really
9 important in our assumption setting process is
10 when we sit around and develop assumptions, we
11 are most focused on economic factors.
12 Interest rates, equity market valuations,
13 credit spreads for fixed income markets. We
14 are never -- we rarely, if ever, are sitting
15 around thinking what should the return be for
16 US equity. What we are thinking about is how
17 should US market valuations play out over the
18 next three years, five years, ten years, and
19 that in turn influences our return expectation
20 for US equities. Similarly, for all fixed
21 income asset classes, we generally don't sit
22 around and think well, what should the US bond
23 market return be for the next ten years. We
24 sit around and ask ourselves what do we think
25 interest rates will do for the next ten years,

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2 what do we think inflation and credit spreads
3 will do for the next ten years, and that in
4 turn will influence our return and risk
5 assumptions for fixed income markets.
6 So everything you see when we get to the
7 actual numbers for asset class return risk and
8 correlation, all of that is an output rather
9 than an input. What is an input is again, all
10 the different factors that I mentioned
11 earlier, and you can see on the top left part
12 of page 3 we list out, you know, just a decent
13 sampling of what those factors are, where all
14 those factors are today. And then we come up
15 with an assumption for where we think those
16 factors are going to be under kind of
17 long-term scenarios. We call it equilibrium.
18 So for example, what we think is the normal
19 ten-year yield for a US treasury bond and we
20 know where we start off today and come to a
21 forecast of what we think is normal. I would
22 also point out that for all of this, there is
23 a range of outcomes. So when we look at a lot
24 of the data and a lot of the numbers in here,
25 it's very, very specific. You know, 4.5

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2 percent return for US equities. It sort of
3 leaves you with this impression that we have
4 the crystal ball and there is a very precise
5 number and there is for the expected case, but
6 I think what again is important here is we
7 develop a wide range of outcomes, and as we do
8 the capital markets modelling, as we go
9 through asset allocation studies with clients,
10 not only do we focus on what is the expected
11 outcome, but we look at what are downside
12 outcomes, what are worst-case scenarios, so
13 really we focus on trying to get that range of
14 outcomes right and try not to get too excited
15 for what the expected number is for each asset
16 class.
17 MR. ADLER: Can I just ask a question?
18 What you gave us is your projected returns,
19 and you told us what your projected returns
20 were when we did this in 2016. But you don't
21 tell us what the actual returns have been.
22 MR. MALERI: We can. Absolutely.
23 MR. ADLER: I think that would be useful
24 just to understand how far off you were.
25 MR. MALERI: So there is a couple of

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2 ways.
3 MR. ADLER: I guess we can do it by
4 looking -- we can look at the benchmarks that
5 you just gave us.
6 MR. MALERI: Exactly and again, back to
7 my opening comments, if you look at the
8 January benchmark report or the December
9 numbers, which are probably more relevant for
10 your assumptions, any asset class that's done
11 really well, so US equities, you know, again
12 even in spite of the poor fourth quarter, I
13 think we are up close to 14 percent for the
14 last decade, so as a result, expectations for
15 that asset class are very low going forward.
16 MS. PELLISH: So let me just add one
17 point. So you are right. As I looked at this
18 again -- and I looked at this a lot before it
19 was mailed out, but as I looked at this this
20 morning, I thought that would have been nice
21 if we include the ten-year and I talked about
22 this before we sat down. So we can give you a
23 few of those numbers for the major asset
24 classes, and that will give you a sense how
25 different our projections are versus history.

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2 MR. MALERI: Again, just to look at the
3 January page that we just looked at because
4 it's right in front of us, the most striking
5 difference in our return assumptions and what
6 you would have experienced historically is
7 this spread between US equity return
8 assumptions and emerging market equity return
9 assumptions and for the seven-year period at
10 this time. There is not a ten-year number on
11 this page but seven years.

12 MS. PELLISH: There is --

13 MR. MALERI: N/A for emerging markets
14 but for seven years you have 13 percent
15 annualized for the Russell 3000. You have 2
16 percent annualized for emerging market
17 equities, so a huge, huge gap over 11 percent
18 annualized for seven years. To us that spread
19 shouldn't exist. If you are investing in
20 equity markets here domestically or
21 internationally over the very long term
22 defined as seven, 10, 15 years, you should
23 largely expect similar results, and in our
24 mind you should expect somewhat of a premium
25 for investing in things such as emerging

1 Proceedings
2 equities and not just developed equities.
3 MS. PELLISH: So just to be clear, so
4 this premium of 11 percent per year that you
5 earned in US equity versus emerging markets,
6 we are largely forecasting that to be reversed
7 over the next decade. Now, I will tell you we
8 have been forecasting that for a while so --
9 MR. ADLER: A broken clock is right
10 twice a day.
11 MS. PELLISH: -- at some point we will
12 be right.
13 MR. MALERI: If we keep rolling off
14 those good months.
15 MS. PELLISH: But that's an important
16 point to be cognizant of, and the fact that we
17 along with I think virtually everyone else has
18 been forecasting that is why you continued to
19 hold onto nonUS equity markets, and in fact,
20 during the last seven years, you have added to
21 emerging equities in your portfolios.
22 MR. MALERI: And one of the questions --
23 we get similar questions from clients that say
24 exactly what Robin described. You have been
25 recommending international, it hasn't worked

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2 out, and what we have done and certainly happy
3 to do this is shown the realized return for
4 the asset class and where they fall on our
5 range of outcomes, and what is a good --
6 perhaps a positive takeaway from this is
7 everything we have experienced was in the
8 range of outcomes that we forecasted ahead of
9 time. So certainly as we would expect, we
10 don't get every number right, but what we want
11 to make sure we capture is that range of
12 outcomes. So the 2 percent annualized that we
13 have gotten from emerging equities over the
14 last seven years, that would have been in our
15 range of distributions if we turned back the
16 clock and ran our assumptions seven years ago.
17 If we experienced something that was way
18 outside our range of expectations, I think
19 that would be concerning. If you go back to
20 2008, in fact, a lot of the work that we have
21 done on our assumptions over the last decade
22 plus has been centered around that 2008 event,
23 and admittedly 2008, that outcome wasn't in
24 our assumptions in 2007 and 2006. So now we
25 have been really focused on making sure that

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2 events that have happened and we think might

3 happen are at least captured in the modelling.

4 It's really difficult to show up at a meeting

5 and say that that was a really tough

6 environment that we lived there, and oh, by

7 the way, we didn't actually capture that when

8 we built the forecasting four years ago, five

9 years ago. At least we can show up and say

10 tough environment but this is in the realm of

11 what we expected. At least kind of gives you

12 comfort that the decisions you made, you had

13 the right information to make those decisions.

14 MS. PELLISH: And maybe just to add one

15 more point. Maybe more importantly looking

16 forward when we look at the range of

17 distributions, we can give you a sense of what

18 is the the worst-case outcome, what's the 1

19 percent outcome, and you can make a collective

20 decision about whether that is an outcome you

21 can live with.

22 MS. VICKERS: I was just wondering do we

23 see the range of outcomes that you are talking

24 about?

25 MR. MALERI: We do have a couple of

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2 slides in here that have that.

3 MS. VICKERS: Page 4, are these the

4 averages?

5 MR. MALERI: Expected case.

6 MS. PELLISH: The 50th percentile.

7 MS. STANG: Matt, just the 2 percent

8 that we realized in emerging markets over

9 seven years, what percent of all the outcomes

10 was that? Was it the worst 10 percent?

11 MR. MALERI: Actually, if you go --

12 hopefully, I am going to turn to the page and

13 it bears this out. If you go to page 9, you

14 will see here, this is again the range of

15 outcomes for the asset classes. The first --

16 and this is a decade so not quite seven years,

17 but it will give you a decent idea. The first

18 percentile is about 1 and a half percent

19 annualized, and second percentile was about 4

20 and a half percent annualized.

21 MS. STANG: So pretty lousy.

22 MR. MALERI: Pretty long outcome.

23 That's why the expectation going forward is

24 much better. So I will just skip over page 5.

25 Has all the detailed different time periods,

1 Proceedings
2 three, five, and ten years. And just the one
3 takeaway from this page is when we show you
4 these numbers, they are all -- each period is
5 built upon the prior forecast. So our model
6 -- let me say it differently. Our model is a
7 series of one-year returns. So the three-year
8 number is really year one, year two, year
9 three. When you move out to five years, it's
10 the same three-year period but plus the
11 additional one-year period. So everything
12 hangs together in our modelling. The
13 three-year number should intuitively factor
14 into the five-year expectation as well as the
15 ten-year expectation. So I think what's
16 probably most helpful at this point, pages 6
17 and 7, we can sort of look at collectively and
18 this is really one of the key items of our
19 discussion this morning is preparing our
20 assumptions today versus what they were at the
21 time we did the last study, and so the
22 assumptions we used at that time were our
23 March 31, 2016 assumptions. So almost three
24 years ago at that point or at this point and
25 what we have on page 6, again, these are just

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2 some of the factors that we use so try to give
3 you a sense of how valuations have changed. A
4 couple key takeaways here. So you can see
5 that treasury yields from the last time we did
6 the study three years ago until today have
7 generally risen, but importantly you will note
8 that short-term rates, so one-year treasury
9 bills as we know the yield on that has moved
10 up quite significantly in the last couple
11 years. So 2.6 percent today versus just about
12 60 basis points almost three years ago whereas
13 if you look at the 30-year treasury bond, that
14 yield today or at year-end was about 3 percent
15 versus 2.6 percent the last time we went
16 through this exercise. And so we have made
17 the color highlighting there hopefully to make
18 it somewhat obvious. We will call it kind of
19 risk assets. Credit markets, corporate bonds,
20 high-yield bonds, emerging market debt, and
21 then the regular emerging markets collectively
22 even in spite of the poor performance for
23 emerging markets valuations have generally
24 gotten higher, and as a result returns are
25 generally lower.

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2 MS. PELLISH: Forecasted.
3 MR. MALERI: Forecasted returns,
4 correct. So you can see US equities, the
5 valuation, we use the Shiller PE methodology
6 there that went from 25 and a half times
7 earnings to 28 and a half times earnings, and
8 this again includes the very poor performance
9 as we experienced in the fourth quarter. Some
10 of this reversed in January. Sometimes when
11 we see extreme market moves like that, we
12 rewrite our assumptions. So as we get closer
13 to doing the study, that might be something we
14 want to take into consideration. Generally
15 month to month you don't see much change, and
16 I should say that we update our assumptions
17 quarterly. So from one quarter to the next,
18 you generally don't see a whole lot of
19 movement. In the extreme case like January
20 where the market is up almost 9 percent that
21 sometimes it's worse revisiting the
22 assumptions because a move like that can
23 change the expected outcomes. On slide 7,
24 here is again probably one of the more
25 important slides of this morning is looking at

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2 the actual return assumptions for each asset
3 class from the last time we did the study
4 until today. A little bit of a mix. The back
5 there you can see again the color highlighting
6 a few asset classes which we generally have
7 higher expectations and then a few asset
8 classes which are generally lower. So I would
9 say on balance if you are going to run a
10 portfolio and try to understand, okay, what
11 was the expected portfolio return from three
12 years ago versus today, I would say it's
13 generally pretty similar and maybe even
14 slightly a few basis points higher. Again
15 fixed income generally have higher return
16 expectations whereas some of the public equity
17 markets and the alternatives to asset classes
18 are a bit more mixed.
19 MR. ADLER: Just a question. US core,
20 that's corporate?
21 MR. MALERI: Traditional investment
22 grade like a Barclays aggregate-type exposure.
23 MR. ADLER: So sort of one-third,
24 one-third, one-third?
25 MR. MALERI: Yes. Corporates,

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2 mortgages, and treasuries.

3 MS. VICKERS: I was going to ask is

4 there any asset class that's missing from here

5 that -- I mean, I don't know if this reflects

6 our current portfolio or should we talk about,

7 you know, anything exciting that we should

8 look at?

9 MR. MALERI: So these assumptions here

10 are what we call the core asset class return

11 assumptions. We actually model I think it's

12 up to 44 different asset classes at this

13 point. A lot of those additional ones that

14 aren't on this page are sort of variations of

15 existing asset classes. So you know, we model

16 US small cap equity, nonUS small cap equity.

17 Within investment grade fixed income, we model

18 all the different sectors like corporate and

19 mortgages.

20 MS. PELLISH: And that's likely what we

21 will actually use in the study because that's

22 how you allocate your fixed income.

23 MS. VICKERS: Is there anything in the

24 TDA that we don't have in the QPP?

25 MR. ADLER: Convertibles.

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2 MS. PELLISH: Yes, converts. You had
3 them and got rid of them.

4 MS. VICKERS: Maybe we should just keep
5 everything open.

6 MS. PELLISH: Yes. So you have -- as we
7 talked about, EMD is a permissible asset class
8 that we are not using.

9 MR. KAZANSKY: So in the asset
10 allocation that we adopted a few years ago,
11 except for I guess place holders, we got out
12 of TIPS, got out of REITS, and got out of the
13 convertibles, and so at least looking at this
14 page, that seems to have paid off to some
15 degree.

16 MR. ADLER: Well, I mean, it might not
17 -- well, it would be given -- it would pay off
18 going forward but it may not have -- might not
19 have paid off for the last years because with
20 us, one of the reasons you lower
21 forward-looking assumptions is because they
22 may have done well, you can't really tell from
23 this necessarily.

24 MR. MALERI: The other kind of
25 complicating factor is what did you sell those

1 Proceedings
2 asset classes in favor of? So if you sold
3 convertibles and bought US equities, that
4 worked out really well. If you sold
5 convertibles and bought emerging markets
6 equity, it didn't really work out so well. So
7 you have to think of it in a portfolio
8 context: What did I buy and what did I sell
9 to know if you made a good decision or not.
10 MS. PELLISH: But I think the point that
11 occurs to me with that question is one of the
12 things we should do in the asset allocation
13 study is look back at the progression of
14 decisions that have been made, and you know,
15 it's hard evaluating whether that was the
16 right decision over 36 months, but I think it
17 would be good to look at the progression of
18 changes to the policy, and I think that will
19 set a context how everything moved in terms of
20 risk and in terms of targeting US asset
21 classes.
22 MR. MALERI: You would think at a
23 minimum -- and we say this to all our clients
24 when we are doing an asset allocation study,
25 we want to look at the full opportunity set

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2 and reunderwrite. If they removed
3 convertibles last time, what was the rationale
4 then. Does the rationale still hold? So we
5 shouldn't just make the assumption that
6 because we removed asset classes last time
7 that they should still be excluded. We should
8 always kind of reunderwrite what the right
9 opportunity set is.
10 MR. ADLER: A couple of notes. The two
11 asset classes that had the biggest change are
12 I think buyouts and commodities. And we don't
13 have an allocation of commodities, and
14 commodities strike me as very high risk. So
15 you know, I am not an advocate of these things
16 until you guys say oh, you really should think
17 about commodities.
18 MR. FULVIO: You would take cash.
19 MR. ADLER: Except cash is a very low
20 return asset.
21 MS. PELLISH: Not so much anymore
22 because T bonds are up. Very few of our
23 clients have dedicated allocations to
24 commodities. Because there is so much
25 volatility and they do have some

1 Proceedings
2 inflation-sensitive properties and sometimes
3 they can be very diversifying, but the
4 expected return is fairly low and so volatile
5 themselves.
6 MR. ADLER: I am curious A, if you could
7 explain why buyouts have such an increase
8 when, you know, equity and you just have large
9 cap equity and I think buyouts were more with
10 mid cap and small cap. So maybe that's the
11 distinction, but you know, you have large cap
12 equity diminished by 90 basis points and
13 buyouts gone up by 170.
14 MR. MALERI: So I should have
15 highlighted this earlier that the change in
16 assumptions is not purely a reflection of
17 changes in market conditions. There is also
18 methodology enhancements that we make over
19 time. And buyout in particular, I can recall
20 two changes that we made in the last three
21 years. One is that our buyout assumption now
22 includes some exposure to nonUS buyout funds,
23 so historically it had been purely US
24 exposure. We have now come to the view that
25 when you are investing in buyout, typically

1 Proceedings
2 funds allow some investments outside of the
3 US, so that's one part of it. We also went
4 back and revisited what the liquidity premium
5 should be for buyout and we have raised that a
6 touch. So the combination of including more
7 nonUS exposure in our buyout assumption plus
8 just our kind of what we think is the
9 long-term normal expectation for illiquidity
10 we increased a bit as well, so those two
11 factors have really led to what you see there
12 in terms of the change.
13 MR. ADLER: I appreciate that. I do
14 note that the equity assumptions for developed
15 market has gone down even lower. There is
16 very little buyout in emerging markets. So I
17 am not saying you guys are off your rockers
18 but just curious to me.
19 MR. MALERI: And again, it's more of a
20 function of the latter, the illiquidity
21 premium that we revisited. As you might
22 imagine, there is a lot of moving pieces
23 behind the scenes in terms of how the numbers
24 actually get put together, so without a kind
25 of detailing every little piece to sum it up

1 Proceedings

2 and say there is methodology changes that are

3 largely responsible for that difference.

4 MS. PELLISH: And even though nonUS, the

5 forward-looking forecast has gone down, it's

6 still significantly higher than US.

7 MR. ADLER: Yes. That's true and again

8 higher than the buyout assumption even if it's

9 gone down.

10 MR. MALERI: So again, if you think

11 about it, you know, historically it was 100

12 percent and I will tell you it was 100 percent

13 US equity. It's again slightly different than

14 that, so even if you moved some of it and

15 added to nonUS as Robin pointed out, that

16 still moves you in the right direction.

17 And I think my guess is if you look at

18 mid cap and small cap in US, that's higher

19 still and you think that's correlated with

20 buyouts than the large cap. I will skip

21 slides 8 and 9. I think we covered it a bit.

22 The point is there is a range of outcomes for

23 each of the asset classes that all the

24 modelling we do captures those different

25 scenarios and we would do the same thing for

1 Proceedings
2 portfolio level results. So as we look at
3 different alternative portfolios, we will show
4 the range of outcomes. I think we think
5 that's particularly helpful when you are going
6 through the portfolio and developing process.
7 Just to the next kind of set of slides,
8 there is two parts left here. One is color of
9 how we come up with our fixed income
10 assumption and how we come up with our public
11 equity assumptions. So the first set of
12 slides there, pages 10 and 11 provides some
13 more color and how we come up with our fixed
14 income return assumptions, and as I mentioned
15 earlier, we really focus on factors. In the
16 face of fixed income, your treasury rate
17 forecast is really the key component there.
18 So what we have on slide 10 is a graphic
19 which shows historical yields for the 10-year
20 treasury as well as the 30-year treasury, and
21 then not only our expected path but the range
22 of outcomes that sits around it. So maybe
23 just to focus on the 10-year treasury, which
24 is the left-hand side of that page, you can
25 see at the end of 2018, the 10-year treasury

1 Proceedings
2 yielded about 2.7 percent. The blue dotted
3 line there is our expectation over the next
4 ten years. So about a 1 percent rise in
5 yields, and while that may sound low, what we
6 have done for context is put the market's
7 expectation which is that forward curve. So
8 based on market prices, you can see there is
9 even -- there is a much lower expectation of
10 how yields will rise over the next decade. So
11 I think this for us is a helpful sanity check
12 to see not that we -- we always want to follow
13 what the market expectations are, but I think
14 it's helpful to be cognizant of how different
15 or how similar our forecast is for yields
16 versus what the market is expecting.
17 MR. ADLER: So your forecast is the blue
18 dot, and you are saying the market expectation
19 is the brown dot?
20 MR. MALERI: Correct, yes.
21 MS. PELLISH: It's the forward curve.
22 MR. MALERI: And importantly the bright
23 yellow bars that sit around each of those
24 dotted lines are the range of expectations.
25 So we got questions or we do get questions a

1 Proceedings
2 lot about if you wind up in this scenario
3 where the rates stay low or go lower, you can
4 see the range of outcomes are different
5 percentiles. Certainly not the expected case
6 but we do build in cases where rates go lower
7 and stay low. That was something historically
8 we really haven't anticipated, and over the
9 last couple of years we have more prominently
10 featured that in our forecasting.
11 MR. ADLER: Question. This is as of
12 December 31st. In January the Fed kind of
13 changed its smoke signals, so would you think
14 that you guys would change a bit now? And my
15 guess is the market has changed a bit.
16 MR. MALERI: Yes. Actually what we
17 found interesting about January, we didn't
18 spend too much time on this when we covered
19 performance in January, but yields didn't
20 react much in January, which to us is a bit
21 surprising. So you have fourth quarter rates
22 fell a lot as equity markets fell, and as
23 equity markets performed really well in
24 January, interest rates didn't move hardly at
25 all, and you would typically think in that

1 Proceedings
2 sort of strong market environment that fixed
3 income investments would do poorly and that
4 wasn't the case. So I guess that sort of
5 where I am headed is our assumptions for fixed
6 income likely would not -- if we had rerun
7 this at the end of the January likely would
8 not have changed much from where we were at
9 year-end, so I think perhaps the Fed's stance
10 was well telegraphed, and that's why the rates
11 did not move much in January. But again, if
12 we reran these numbers as of today or as of
13 the end of January, they likely wouldn't be
14 much different.
15 MR. ADLER: That's helpful.
16 MR. MALERI: And then I think page 11 is
17 a helpful visual looking at the yield curve
18 where we were three years ago in 2016 where we
19 did the study as well as today, and then
20 Rocaton what we call our equilibrium or normal
21 level of yield curve. Hopefully it's quite
22 obvious that today's yield curve is very, very
23 flat. There is almost no pick up in yield
24 going from say treasury bills, very short-term
25 treasury bills all the way out to owning a

1 Proceedings
2 30-year treasury bond. And we think the
3 expectation is that you should get paid some
4 premium for owning longer duration fixed
5 income. You can see actually despite being as
6 low as the yields were back in 2016, yields
7 were what we consider to be normally shaped or
8 sloped and you don't see that at all today.
9 So that to us, there is some excitement around
10 short-term yields being higher, but the
11 unexciting part is that you are not getting
12 paid to take on extra duration at this point.
13 Then just the last couple of slides, I
14 won't go through these last three
15 individually, but these are hopefully helpful
16 in explaining -- giving a sense of why our
17 expectations for equity markets are the way
18 they are, and you know, the one we get asked
19 about most as you might imagine is US equity
20 forecast. So what we have done here is simply
21 we look at starting valuations. We just make
22 cyclically adjusted P. That goes all the way
23 back to 1928, so we have about 90 years' worth
24 of data here and we break it up into ten
25 different deciles, ten different starting

1 Proceedings

2 groups, and we say for each of those starting
3 groups from most expensive to least expensive,
4 what was the expectation five years forward.
5 So for example, just focusing on the left-hand
6 side of the page when valuations were in the
7 10 percent of most attractive observations,
8 from that point forward on average you got
9 about 18 percent a year for five years.

10 The unfortunate thing is that we are at
11 the other end of the vehicle today. So if you
12 look at the valuations today, they are in the
13 top 10 percent of the most expensive market
14 and what that generally led to -- you can see
15 over five years that generally led to flat or
16 slight return over five years. Importantly
17 that's why we put the data on here. We do
18 point out the maximum/minimum so no guarantee.
19 There is a wide range of outcome, but in
20 general when you are at this point in the
21 cycle for US equity markets, it's generally
22 pretty much unfavorable going forward five
23 years.

24 MS. PELLISH: So is this chart clear?
25 Because I find this chart incredibly

1 Proceedings

2 compelling.

3 MS. VICKERS: To me it's not.

4 MS. PELLISH: Let me restate it. So

5 what this chart says, if you look back over

6 the past 90 years of data and you look at I

7 think it's quarterly --

8 MR. MALERI: I think it's monthly.

9 MS. PELLISH: Look monthly and you

10 figure out what the PE ratio was of the US

11 stock market at the end of every month for the

12 past 90 years and you array those PE ratios in

13 deciles most expensive to least expensive, so

14 you have a huge amount of data, and you take

15 the most expensive decile, so when PE ratios

16 were highest, you take all those months where

17 PE ratios were highest and look out over the

18 subsequent five years an average for that

19 decile of PE ratios.

20 The average return over the subsequent

21 five years was negative 60 basis points. The

22 highest return for the five-year period in

23 that decile of PE ratios was almost 11

24 percent. The lowest was negative 22 percent.

25 So it's a very intuitive fact, which is when

1 Proceedings
2 you are paying a lot for stocks, which is what
3 the PE ratio is. It's just how much -- how
4 many dollars you are paying for every dollar
5 of earning. When you are paying a lot over
6 the next five years, you tend to have a lower
7 return because your starting point is pretty
8 expensive. Conversely, if you go to the other
9 end of the extreme and you say what happened
10 in the periods of time when stocks were
11 cheapest, the lowest decile of PE ratios, the
12 average five-year return for those periods of
13 time were 18 percent. The best return over
14 any one five-year period was almost 31
15 percent. The lowest was about 7 percent. So
16 the interesting thing -- so one of the things
17 when you look at charts like this, there is
18 lot of charts like this going over historical
19 periods of time, but it's a pretty consistent
20 pattern and it's so intuitive. The cheaper a
21 stock is, the cheaper the stock market is in
22 general, the better you tend to do. The more
23 expensive it is, the worse you tend to do in
24 the subsequent five-year period and it's
25 pretty consistent. There is this blip in the

1 Proceedings
2 seventh decile but this is an unusually
3 consistent pattern of returns and it's a very
4 long period of time and it's a very
5 intuitively appealing concept. You pay more,
6 you earn less. You pay less, you earn more.
7 And so when we put in PE ratios as one of the
8 inputs to the expected -- calculating the
9 expected return, it leads us to have a lower
10 expected return for the next five, seven, ten
11 years, and if you look back at history, that
12 has also tended to be the case in history.
13 MS. VICKERS: What about the most recent
14 couple of years? Was it not the case?
15 MS. PELLISH: Yes, it was. It was.
16 MR. MALERI: And that's why again, we
17 point out the maximum and minimum. It's -- we
18 wish it was a guarantee. We wish we could
19 rely on this with, you know, extreme
20 confidence, but you know, there was a period
21 of time where you were -- stocks were as
22 expensive -- they were the most expensive
23 decile and you earned 10 percent annualized
24 for five years. That one result is not very
25 intuitive but it happens and so -- and I don't

1 Proceedings
2 have the exact number, but I am guessing the
3 most recent five-year period we lived through
4 probably falls in that category of stocks were
5 really expensive, but you did really well for
6 five years, and as Robin I think said earlier,
7 it's why you just don't abandon some asset
8 classes because they look expensive on paper.
9 MR. FULVIO: I think that's the headline
10 on this. There is another dynamic also when
11 you look at these numbers. So if the
12 valuation of the equity markets are in any of
13 the four deciles to the right, the variability
14 in returns over the following five-year time
15 period is a lot wider. It's anywhere from 30
16 to 40 percent as opposed to in the other time
17 periods anywhere from 20 to 25 percent.
18 MS. PELLISH: We should show that 18 as
19 well.
20 MS. STANG: So you get the delta.
21 MR. FULVIO: It's not only the direction
22 but it's also the spread.
23 MS. PELLISH: The volatility and the
24 spread. So building on the point you raised,
25 Susannah, it's important again when we do this

1 Proceedings

2 asset allocation study, we are going to look
3 at the expected outcome, but we are also going
4 to look at the range of possible outcomes
5 because we want to identify scenarios that may
6 well occur even if a small probability, and if
7 those are completely untenable, then we need
8 to move away from those.
9 MR. MALERI: We don't need to start
10 there, but the next two pages show the same
11 exact thing for nonUS developed and emerging
12 equities. One we have lots of data there only
13 back to 2005, and with that small data set,
14 you can see it's not as well-behaved. I think
15 generally you can see the pattern that Robin
16 pointed out kind of moving from left to right,
17 but it's not quite as well-behaved where we
18 have data for the 90 years in the US equity
19 market. And again, it's sort of introducing
20 uncertainty and all of that leads back to
21 wanting to own a diversified portfolio, and
22 maybe on the market we like US -- nonUS equity
23 markets, but it's a sort of cautionary tale
24 that nobody has the crystal ball.
25 Unfortunately, we don't have the crystal ball

1 Proceedings

2 and we try to use intuition to make decisions,
3 but we know there is some level of uncertainty
4 always and so you have to go back to kind of
5 basic investing principles of owning a
6 diversified portfolio, don't make extreme
7 decisions, and that's I think really important
8 to cope in the back of your minds as we go
9 through the asset allocation exercise.
10 MS. PELLISH: Anything else in here?
11 MR. MALERI: No. That's all I have
12 planned.
13 MS. PELLISH: So much more to come in
14 terms of assumptions, in terms of asset
15 classes to be considered, and in terms of I
16 guess a timetable for the study.
17 MS. PELLISH: Thanks, Matt. Mr.
18 Chairman, should we move on?
19 MR. ADLER: Yes, sure. Let's move on.
20 MR. FULVIO: So right now based on the
21 agenda item what we are handing out are the
22 ten principles associated with the United
23 Nations Global Compact. So there has over the
24 years been a number of resolutions from the UN
25 as it relates to human rights practices, labor

1 Proceedings
2 practices, environmental factors, and
3 anticorruption guidance, and this guidance
4 that the UN offers not only to governmental
5 organizations but to corporations across the
6 globe. And so what they have done is
7 synthesized all these different resolutions
8 over the years into ten principles that they
9 have provided as in their mind responsible
10 approaches to conducting not only business but
11 as a government organization -- governmental
12 entities hire regulating companies in your
13 jurisdiction, so we thought this was something
14 that was interesting and perhaps creates some
15 sort of framing or lens that might be helpful
16 as we work through other projects such as
17 looking at the screening for emerging market
18 portfolios. We have continued to make
19 progress on that with the working group, and
20 Robin and I continue to have conversations
21 with the vendors and requested some follow-up
22 items. We tried to think of constructive ways
23 of framing out the evaluation of portfolio
24 companies and using the data and the insights
25 that the vendors can provide on how those

1 Proceedings
2 companies are scoring, but also trying to
3 marry the beliefs statement with how we are
4 framing out those screens is proving to be
5 challenging but I think a challenge that all
6 institutional investors that are focused in
7 this space are wrestling with. We have had
8 more conversations with others in the
9 marketplace on not only the Global Compact but
10 just in general. This has really been the
11 crux of the struggle for folks which factors
12 do we care the most about and how do we hone
13 in and measure those factors. So yes, it's
14 easy to go back out and hire a data provider,
15 but we want to make sure that we are creating
16 something more actionable based on what they
17 could provide and how the board or any other
18 board approaches the space. So we found that
19 the things that are called out in these ten
20 principles which we can talk through, they are
21 intentionally high level, and as you start
22 peeling back the layers, the UN's Global
23 Compact has specifics in terms of how they are
24 looking to measure and score and how companies
25 should be reporting, self-reporting to some

1 Proceedings
2 degree, how they are conducting themselves to
3 be either in accordance with these principles,
4 and interestingly enough, we can use the data
5 vendors to highlight where companies are not
6 in compliance or in direct contrast with the
7 spirit of these specific principles. So
8 something we wanted to talk through a little
9 bit and preview I would say, and Robin, kick
10 me up under the table if you disagree. We are
11 not experts on these principles themselves and
12 the resolutions behind them and how they
13 structured the evaluation process, but in our
14 mind as we spent time looking at these and
15 talking to others in the marketplace about
16 them, they struck a chord in terms of I think
17 what the spirit of what TRS was looking for in
18 the beliefs statement, and it seemed like it
19 might be an interesting way to communicate
20 what you are focused on to not only your
21 managers but the data vendors who will be
22 evaluating or providing some sort of
23 assessment of company controversies and
24 company scores. So I will pause there.
25 MS. PELLISH: So to add to what Mike is

1 Proceedings
2 saying, so we didn't expect that this would
3 provoke a detailed conversation at the board
4 level because we are working with the working
5 group on the details of this process, but what
6 we did do -- but we thought it was worth
7 spending a few minutes introducing this
8 concept to the board, getting any feedback you
9 might have at this time on this subject, and
10 then also informing you that as follow-up to
11 the previous conversation we had regarding how
12 to solicit follow-up from Sustainalytics and
13 MSCI that would help us distinguish between
14 their two processes, we have asked them to
15 look at an emerging markets portfolio -- not
16 one of our current portfolios, but to look at
17 an actual emerging markets portfolio and
18 provide feedback on how that portfolio would
19 score if you used the UN Compact principles as
20 a framework to evaluate those holdings and
21 this -- and we have shared the investment
22 beliefs of the board with the providers as you
23 know, but this is a set of ten principles that
24 they are used to using in their processes.
25 MS. VICKERS: What's striking me, isn't

1 Proceedings

2 there the UN Principles of Responsible

3 Investing, UNPRI? And my understanding is

4 that's sort of the standard when we ask

5 managers we work with. Do you know the

6 difference between this and that?

7 MR. FULVIO: So my understanding is that

8 while that references this, this is specific

9 in looking through to underlying company

10 business practices as opposed to investment

11 principles that a portfolio manager would, for

12 example, employ.

13 MS. PELLISH: So we can come back. We

14 have looked at this. Still a little murky to

15 us but we will come back to you with a more

16 specific response.

17 MS. VICKERS: So this is specific for

18 the business, how business is operating?

19 MS. PELLISH: Yes.

20 MS. STANG: PRI is more general.

21 MS. VICKERS: Because I feel this is

22 pretty general.

23 MS. PELLISH: It is. It's very high

24 level.

25 MR. ADLER: Except in labor. I think

1 Proceedings
2 it's very precise in labor. It lists four
3 different aspects of labor, which is obviously
4 very important to this board, which you know,
5 I think is really interesting. Like what it
6 doesn't go into, for example, the issue of
7 supply chain, but it says businesses should
8 uphold -- I don't know the limitation of all
9 forms of forced and compulsory labor, child
10 labor, discrimination. I mean, there is a lot
11 there on labor. Not like -- so maybe not on
12 all the other things but --
13 MS. PELLISH: So we are not recommending
14 the board adopt this as its framework at this
15 point. We wanted to introduce it and perhaps
16 it's most useful because the data providers
17 are used to working with this. So your
18 investment beliefs statement is a custom
19 statement obviously that they are committed
20 to, you know, working with, but this is
21 something they have worked with already and so
22 we gave -- we said to them, we said to both
23 firms, come back to us and highlight the
24 holdings in this portfolio that are
25 significantly inconsistent with these

1 Proceedings
2 principles and so we have just gotten that --
3 those reports back from the two providers and
4 we will go over it with the working group.
5 MS. VICKERS: Just to confirm, so the
6 feedback from both MSCI and Sustainalytics and
7 I don't know anybody else --
8 MS. PELLISH: No. Those are the two.
9 MS. VICKERS: -- is this is a framework
10 that they have employed for other clients and
11 they are used to working with and think is
12 effective and --
13 MS. PELLISH: Well, they don't have
14 opinions on it, but they are very familiar
15 with it and they have employed it.
16 MS. VICKERS: Is there another framework
17 that they have told you they employed, or is
18 this the only one?
19 MR. FULVIO: No. I think honestly the
20 big sell for them is the ability to customize
21 and focus in on specific factors, so specific
22 items that I think you would even say underlie
23 each of these ten principles and measures
24 those for those. So I will give you one
25 specific example would be controversies

1 Proceedings

2 surrounding workplace conditions and safety
3 and well-being of employees, and so that
4 specific factor they would say the
5 controversies they can identify relate to that
6 factor, then feed into these higher level
7 principles, and they will specifically link
8 how they have mapped their underlying factors
9 like that safety issue to these fact -- to
10 these principles and they -- it's really a
11 helpful way of sort of outlining the different
12 things you are focused on while letting the
13 data provider specifically identify how they
14 would express this preference.
15 MS. VICKERS: That makes a lot of sense.
16 Just in the conversations that we have had
17 internally at BAM trying to utilize the MSCI
18 system, so if I asked a certain question and
19 asked for a report to be run, sometimes there
20 is a determination question and trying to
21 figure out which range, which factors to
22 employ. So if there is kind of -- I don't
23 want to call it a cheat sheet, but you know,
24 if I have a question about child labor, child
25 labor is here, and then there are factors that

1 Proceedings
2 are in MSCI or Sustainalytics that are linked
3 to that.
4 MS. PELLISH: That are linked to that.
5 MR. FULVIO: Kind of helps connect the
6 dots.
7 MS. PELLISH: That's exactly -- and the
8 data providers didn't come to us with this.
9 MR. FULVIO: So there was -- in one of
10 the vendor presentations they did refer to the
11 Global Compact and what they said was look, we
12 track all these factors. You could use this
13 as a way of looking things up, but they
14 weren't recommending it or suggesting that was
15 the approach. They like to use that though
16 because I think there are plan sponsors or
17 investment asset owners who see certain things
18 within this that they want to be more focused
19 on, so it's an easy way of saying I want this
20 and this.
21 MS. VICKERS: It's a summary because
22 there is so much in the systems and it's very
23 hard to sort of figure out how it -- how to
24 make it useful for the questions you want to
25 ask. So if you have these kind of summary

1 Proceedings
2 level buckets, if that's what they are,
3 buckets or factors, then I think it can go a
4 long way in sort of helping to focus and make
5 the data more useful.
6 MS. PELLISH: And because the process
7 that we are currently contemplating -- and
8 there is still discussion about that process
9 but because the process that at least we have
10 been contemplating is one in which we are not
11 precluding any investments but we are asking
12 managers to be mindful of principles and then
13 we are periodically evaluating their
14 portfolios using certain screens, we can -- we
15 would then have a discussion about any
16 securities that pop up as inconsistent with
17 these principles and screens and we would have
18 a discussion about them. So there is a lot of
19 room for -- we would expect the managers to
20 present a compelling case about why that
21 holding isn't inconsistent with the investment
22 beliefs of the board despite the score, and so
23 there is room -- there is room in the process
24 that acknowledges that data can be wrong. The
25 data can be old and there may be a nuance that

1 Proceedings
2 the board -- that mitigates the issue.
3 MS. VICKERS: Right. And with active
4 management, that's what we want to see. We
5 want them to be taking a deeper dive into each
6 company that they choose.
7 MS. PELLISH: Yes.
8 MR. FULVIO: There is one other wrinkle
9 that became apparent to us as we were talking
10 to the vendors that we think is an important
11 consideration. So what we said when we gave
12 the vendors this task, they provided this in
13 their feedback at the onset, we said in
14 addition to finding or highlighting
15 inconsistencies with this, also let us know to
16 the extent there is anything that for whatever
17 reason is not included by this but poses some
18 sort of significant --
19 MS. PELLISH: Reputation.
20 MR. FULVIO: -- reputational risk.
21 Exactly. So one of the companies that
22 actually passes the factors they have outlined
23 for this but something they would put, for
24 example, on watch or that they have
25 highlighted which wasn't flagged from this was

1 Proceedings

2 -- and I would argue maybe you could include
3 it under number 10, anticorruption, but if
4 there was, for example, at one of the
5 portfolio companies in the sample portfolio a
6 bad actor who embezzled money, so that does
7 not necessarily mean the company did something
8 wrong or incorrect. And perhaps they did, but
9 I think it still prompts the same kind of
10 conversation we would have with the manager,
11 which is have you evaluated the company for
12 what might potentially be a lack of controls
13 or you know, lack of oversight to identify
14 something like this. And we recognize bad
15 actors can show up anywhere --
16 MS. PELLISH: At good companies.
17 MR. FULVIO: -- at good companies and it
18 may not warrant a sale of the company but it
19 does require an additional screen or something
20 else to be focused on.
21 MR. ADLER: I just want to make a
22 comment because you said something, Robin,
23 that I don't think we have agreed to, which is
24 that we are not talking about potentially
25 eliminating companies and I think that is not

1 Proceedings
2 our understanding, at least not yet. I
3 thought that what we were doing is looking at
4 the potential for saying some companies we are
5 not considering investable. Some companies we
6 may engage with, and some companies we are
7 going to -- and the rest we are going to say
8 fine. Then obviously we are going to revisit
9 this periodically, but you said we are not
10 considering eliminating any companies and I
11 don't think that's true, and in particular I
12 think we are saying that with indexing as
13 opposed to active management, we may limit the
14 universe. So am I incorrect about that?
15 MS. PELLISH: No. I think there is --
16 and you have articulated that very clearly
17 before, and that's why I was trying to
18 reference Rocaton's perspective. So let's
19 divide out active versus passive because the
20 passive is a really, really important but
21 separate discussion and I think we can focus
22 on the active at the outset because we are
23 going to have primarily active portfolios. So
24 if you focus on the active, I would agree that
25 there well may be companies that the board

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2 decides to exclude. I think the difference in
3 the perspective you have outlined is when you
4 make that decision about excluding them, do
5 you look at the entire universe of the
6 emerging markets index and say to managers we
7 don't want you to own these ten stocks, or do
8 you periodically look at portfolios of active
9 managers to see whether any of the stocks they
10 own violate these whatever criteria we end up
11 defining and using with a database provider?
12 And then have a discussion about it, and so I
13 think it's a question when and how you exclude
14 companies, not whether there is any
15 possibility of excluding companies.

16 MS. VICKERS: That was my understanding.
17 The result will be the exclusion of certain
18 securities, but you know, sort of the
19 framework is principles-based.

20 MR. ADLER: Well, okay. I am not saying
21 it's not a principles-based framework, but I
22 also thought that what we were going to do and
23 I think this is part of the idea of giving
24 companies examples to score was that we may
25 decide that certain companies are, you know,

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2 under the benchmark that we set and we do want
3 to exclude and we want to say from the get-go
4 these companies are beyond the pale, and so we
5 want to say to active managers we don't want
6 you to invest in it. I thought that's where
7 we landed, and honestly I am not sure whether
8 this discussion took place here or in the
9 working group and I think some of this is
10 working group discussion, not --
11 MS. VICKERS: But I kind of -- I agree
12 with what you are saying, but I think that the
13 managers would agree if we give them a kind of
14 clear roadmap, we say we don't want to invest
15 in any of this, and you know, with our
16 research at the begining it was ten companies.
17 Oh, yes, those ten companies are on our list
18 too based on the principles that you are
19 giving us.
20 MS. PELLISH: So you are talking about
21 defining the permissible universe?
22 MR. ADLER: I am and I thought from the
23 get-go what we saying was we were moving from
24 a country screen process to a company
25 screening process and I thought again where we

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2 -- I thought where we arrived -- I thought it
3 was kind of consensus but I may be wrong --
4 was that, you know, we are going to divide the
5 emerging market universe into three buckets:
6 The no bucket, the yes bucket and the
7 engagement bucket. And then obviously
8 companies can move back and forth.
9 MS. VICKERS: I don't remember those
10 three buckets.
11 MR. KAZANSKY: I have to say I don't
12 think what we ultimately arrived -- I believe
13 that what we were kind of focused on was if we
14 provide the managers with clear and concise
15 direction about what we are interested in and
16 what we are looking for, that we were pretty
17 much trusting them to make the right decisions
18 because ultimately if we have given them our
19 principles and our statement of beliefs that
20 outline these are the things we are looking
21 for, at least these are the things we are
22 looking to stay away from, and then they go
23 ahead and find those things and do the
24 opposite of what we wanted them to do, that's
25 not necessarily a smart move for them to

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2 retain them to stay our manager. So I think

3 what I remember was we were kind of giving

4 them the rulebook and saying do what you need

5 to do. Don't bring us anything a year from

6 now that we are going to be like why did you

7 do that, that didn't make any sense, and then

8 if there was something that occurred in that

9 time period that we would sit down and say

10 okay, well, what do we do at this point? Do

11 we engage, do we walk away, do we take some

12 other action?

13 MR. ADLER: Based on that, why are we

14 hiring a data provider then?

15 MS. VICKERS: We haven't decided.

16 MS. PELLISH: To evaluate the

17 portfolios.

18 MS. VICKERS: I think we -- what we

19 haven't ever decided is sort of the sequence

20 of what comes first. The data provider

21 running the screen or the investments and then

22 every year after a certain date, we do an

23 annual check. We haven't gotten there. I

24 think --

25 MR. ADLER: Honestly, I think this is

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2 working group discussion.
3 MS. PELLISH: All right. So more to
4 come which I think in any event we are going
5 to need a data provider because if we change
6 the process, we are going to need a different
7 process to evaluate companies whether we
8 develop a screened universe at the outset or
9 just need a process to find, and I think there
10 is some consensus that that would include a
11 data provider, so we would be back to the
12 working group with the results from the data
13 providers and more discussion about the steps
14 in the process.
15 MR. ADLER: Okay.
16 MS. PELLISH: All right. I think that
17 concludes what we want to cover in the public
18 session.
19 MR. ADLER: Okay. So unless anybody has
20 anything else -- oh, wait a second. I think
21 the ILPA sign on is a public item; is that
22 right?
23 MS. BUDZIK: It can be a public item.
24 MR. ADLER: So I think folks have in
25 front of them the proposed sign on letter with

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2 ILPA that I think we did discuss yesterday in
3 public session, and so if folks have had a
4 second to review it, I think there is other
5 three other systems that caucused at the
6 system all agreed to sign onto this yesterday.
7 I think BERS is doing a poll of its trustees;
8 is that correct, Mr. Rich?

9 MR. RICH: We are out there right now.
10 We will know by tomorrow's evening.

11 MS. COLLINS: The City wants to send out
12 the final letter with everybody's signature.
13 The intent is to have each fund represented
14 individually on the letter. So just has more
15 impact as five funds instead of the New York
16 City funds.

17 MR. ADLER: And I think the letter is
18 supposed to go out tomorrow evening, and to
19 summarize again, the letter is urging the SEC
20 to maintain the strongest fiduciary
21 protections for investors in private equity
22 funds. So do we need a motion to sign onto it
23 or just see if there is consent?

24 MS. BUDZIK: I think consensus is fine.

25 MR. ADLER: So do we have consensus?

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2 And obviously I know the Comptroller's Office,
3 but is there consensus to allow the Teachers'
4 Retirement System to sign onto this letter?
5 MR. KAZANSKY: Yes.
6 MS. PENNY: Yes.
7 MR. ADLER: Okay. Great. So with that,
8 I think that concludes our business for the
9 public agenda. So we have some executive
10 session business. Is there a motion to exit
11 public session and enter executive session?
12 MS. PENNY: There is. I move pursuant
13 to Public Officers Law Section 105 to go into
14 executive session for discussions on specific
15 investment matters.
16 MR. ADLER: Is there a second?
17 MS. VICKERS: Second.
18 MR. ADLER: Any discussion? All in
19 favor of the motion to exit public session and
20 enter executive session, please say aye. Aye.
21 MS. VICKERS: Aye.
22 MS. PENNY: Aye.
23 MR. BROWN: Aye.
24 MR. KAZANSKY: Aye.
25 MR. ADLER: I believe it's unanimous.

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2 So let's go into executive session.

3 (Whereupon, the meeting went into Executive Session.)

4 MR. ADLER: Anybody have anything else

5 for executive session? So a motion to exit

6 executive session and return to public session

7 would be in order.

8 MR. BROWN: So moved.

9 MR. ADLER: Thank you, Mr. Brown. Is

10 there a second?

11 MS. PENNY: Second.

12 MR. ADLER: Thank you, Ms. Penny. Any

13 discussion? All in favor of the motion to

14 exit executive and enter public session,

15 please say aye. Aye.

16 MS. VICKERS: Aye.

17 MS. PENNY: Aye.

18 MR. BROWN: Aye.

19 MR. KAZANSKY: Aye.

20 MR. ADLER: Resounding. Any opposed?

21 And okay, any abstentions? Motion carries.

22 Okay. We are back in public session.

23 Susan, would you please report out of

24 executive session?

25 MS. STANG: Certainly. In executive

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2 session, there was a presentation and
3 discussion of a sector of the US equity market
4 and a subsector of the US equity market.
5 MR. ADLER: Great. Thank you. That
6 concludes our business for today. Is there a
7 motion to adjourn?
8 MR. KAZANSKY: So moved.
9 MR. ADLER: Thank you, Mr. Kazansky. Is
10 there a second?
11 MS. VICKERS: Second.
12 MR. ADLER: Thank you, Ms. Vickers. Is
13 there any discussion?
14 All in favor of the motion to adjourn,
15 please say aye. Aye.
16 MS. VICKERS: Aye.
17 MS. PENNY: Aye.
18 MR. BROWN: Aye.
19 MR. KAZANSKY: Aye.
20 MR. ADLER: All opposed, please say nay.
21 Any abstentions? Motion carries. Meeting is
22 adjourned.
23 (Time noted: 12:25 p.m.)
24
25

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2 C E R T I F I C A T E

3 STATE OF NEW YORK)

4 : ss.

5 COUNTY OF QUEENS)

6

7 I, YAFFA KAPLAN, a Notary Public

8 within and for the State of New York, do

9 hereby certify that the foregoing record of

10 proceedings is a full and correct

11 transcript of the stenographic notes taken

12 by me therein.

13 IN WITNESS WHEREOF, I have hereunto

14 set my hand this 18th day of February,

15 2019.

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17 ______________________

18 YAFFA KAPLAN

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