Minutes are intended to note (a) the date, time and place of the meeting; (b) those members of the public body who were present and those who were absent; and (c) the substance of all matters proposed, discussed and/or action was taken on. Minutes are not intended to be a verbatim report of a meeting. An audiotape recording of the meeting is available for inspection by any member of the public interested in a verbatim report of the meeting. These minutes are not final until approved by the Board of Regents at the September 2016 meeting.

BOARD OF REGENTS and its
INVESTMENT COMMITTEE
NEVADA SYSTEM OF HIGHER EDUCATION
Sierra Building, Room 108
Truckee Meadows Community College
7000 Dandini Boulevard, Reno
Thursday, June 9, 2016

Members Present:	Mr. Kevin C. Melcher, Chair Mr. Robert M. Davidson, Vice Chair Mr. Cedric Crear Dr. Jason Geddes Mr. Trevor Hayes
Other Regents Present:	Mr. Michael B. Wixom
Others Present:	Mr. Vic Redding, Vice Chancellor for Finance Mr. Nicholas Vaskov, System Counsel and Director of Real Estate Planning Mr. Jamie Hullman, Senior Director of Finance Dr. Mark A. Curtis, President, GBC Dr. Len Jessup, President, UNLV Mr. Chester Burton, President, WNC Mr. David Breiner, Cambridge Associates Mr. Jeff Mansukhani, Cambridge Associates Mr. Lindsay VanVoorhis, Cambridge Associates Ms. Wendy Walker, Cambridge Associates Mr. Matt Beardsley, Russell Investments Ms. Cara McGinnis, Russell Investments Mr. Paul Olschwanger, Russell Investments Ms. Lisa Schneider, Russell Investments Mr. Russell Campbell, Your Second Opinion

There were no faculty senate chairs or student body presidents in attendance.

For others present, please see the attendance roster on file in the Board office.

Chair Kevin C. Melcher called the meeting to order at 3:30 p.m. with all members present except Vice Chair Davidson.

1. <u>Information Only-Public Comment</u> – None

2. <u>Approved- Minutes</u> – The Committee recommended approval of the minutes from the March 4, 2016, meeting *(Ref. INV-2 on file in the Board office).*

Regent Geddes moved approval of the minutes from the March 4, 2016, meeting. Regent Crear seconded. Motion carried. Vice Chair Davidson was absent.

3. <u>Information Only-Transfer of Assets from GBC Foundation Endowment Pool to the System Endowment Pool</u> – Staff provided an update of progress made towards moving the GBC Foundation Endowment accounts into the System Administration Endowment Pool.

Mr. Jamie Hullman, Senior Director of Finance, said at the March 2016 Board meeting the Board approved the transfer of GBC Endowment assets into the System Administration Endowment Pool. He stated it is required that any NSHE foundation having prior year assets greater than $6.0 million must have an annual audit performed. The cost of the audit can be quite expensive for such a small Endowment Pool so the goal is to move the assets, or as many assets as possible, into the System Endowment Pool by June 30, 2016. Mr. Hullman has asked Cambridge Associates to provide the Committee with the investment allocation recommendation of the funds to be transferred from the GBC Pool into the System Pool. He will travel to GBC to conduct a review of the calculations and data to be sure all the necessary documents are available for each of the Endowment accounts.

Mr. Hullman continued that he and the Vice Chancellor for Finance, Vic Redding, met with a representative of the WNC Foundation to discuss the benefits of moving the WNC small Endowment Fund into the System Administration Endowment Pool. He will continue efforts to communicate with the WNC Foundation and other small institution foundations regarding the advantages of moving funds.

Vice Chair Davidson entered the meeting.

4. <u>Approved-Pooled Endowment and Operating Funds; Operating Pool Reserve</u> – The Committee recommended approval for:
Rebalancing and distribution: *(continued)*

- Operating Fund:
  - i) Add $10.0 million to Vanguard Inflation-Protected Securities, sourced from PIMCO All Asset All Authority Fund.
- Endowment Fund:
  - i) A $2.2 million quarterly distribution from the portfolio to campuses for the quarter ending June 30, 2016, funded from Cash;
  - ii) $0.3 million annual System administration fee, funded from Cash;

4. Approved-Pooled Endowment and Operating Funds; Operating Pool Reserve – *(continued)*

Rebalancing and distribution: *(continued)*

- Endowment Fund: *(continued)*
  iii) Upon receipt of the expected $5.8 million inflow from Great Basin College in June, deploy the funds to rebalance the portfolio toward policy targets as follows:
    1. $1.0 million addition to Vanguard Institutional Index;
    2. $0.5 million addition to DFA EM Value;
    3. $1.0 million addition to PIMCO Total Return;
    4. $1.0 million addition to Wells Capital Montgomery Fixed Income; and
    5. Balance (approximately $2.3 million) to Cash.

Ms. Wendy Walker, Cambridge Associates, reported the Endowment Fund returned 0.6 percent in the quarter shortly after the markets troughed in mid-February. As a preview of second quarter results, the Endowment returned an additional 3.0 percent for the second quarter through June 8, 2016. The strongest performer for the first quarter was Public Real Assets which rebounded 5.8 percent in the Endowment portfolio, and for the second quarter it rebounded an additional 16.0 percent through June 8, 2016. The biggest laggard in the quarter was Marketable Alternatives which returned a negative 4.8 percent, lagging the benchmark by 2 percentage points. She said the Marketable Alternatives are hedge fund-to-funds which will presumably be revisited should the Committee elect to move to an outsourced chief investment officer (OCIO) model.

Ms. Walker said over the long-term trailing one year period the Endowment returned negative 4.6 percent, underperforming the policy index by 150 basis points. The primary detractor has been in the Public Real Assets area, which is now rebounding and has been the strongest contributor on the calendar year-to-date. Over the very long-term, the Endowment has returned 9.9 percent annualized since inception, adjusting for inflation that equals 7.2 percent in real terms, which is well ahead of the financial objective to support the payout to campuses and offering growth in principal.

Ms. Walker said the Operating Fund for the first quarter posted a return of 1.3 percent, beating the policy index by 50 basis points. She stated for the second quarter through June 8, 2016, the estimate is for an additional 1.5 percent return. She indicated Opportunistic Assets and TIPS were the two strongest performing asset classes during the first quarter, posting 5.6 percent and 4.6 percent returns respectively. She said the Opportunistic Assets rose another 4.1 percent while TIPS was relatively flat through the second quarter through June 8, 2016. The laggard from an absolute basis was Global ex U.S. Equity that returned a relatively more muted 0.7 percent, but it did outperform its benchmark by 3.7 percentage points. Ms. Walker continued that similar to the Endowment over the trailing one-year period, the Operating Fund returned negative 0.8 trailing its

4. Approved-Pooled Endowment and Operating Funds; Operating Pool Reserve – *(continued)*

policy benchmark. The largest detractor was Opportunistic Assets which has not returned nearly 10.0 percent for the calendar year-to-date. She added that Cambridge is pleased to see the rebound of the out-of-favor asset classes.

Ms. Walker said the manager updates for the Endowment are on page 5 of the report *(on file in the Board office)*. She reported that Commonfund Capital, Inc., had a senior level departure from its venture team – it is a concern – and it would be unlikely that Cambridge would recommend this fund-family given the magnitude of recent losses. However, Commonfund has a large roster of relationships so Cambridge does not see any reason to take action with respect to the Endowment's current investments.

Ms. Walker stated the other portfolio manager changes are at Capital Group Emerging Markets Growth Fund which is having turnover at its portfolio manager level. Capital has also gone through an extended period of disappointing performance. Cambridge does not believe the impending portfolio manager turnover is a reason for immediate action but this manager, in particular, would be subject to a review and hard look if and when the Endowment is moved into an OCIO model, but no need for action today given that pending change.

Ms. Walker pointed out the rebalancing recommendation serves primarily to fund the $2.2 million distribution to campuses plus $0.3 million distribution to the System as an administration fee. The recommendation is for those to be paid out of current Cash and then, upon receipt of the inflow from Great Basin College, the recommendation is a $1.0 million addition to Vanguard Institutional Index, a $0.5 million addition to DFA, a $1.0 million addition to PIMCO Total Return and $1.0 million to Wells Cap Montgomery Fixed Income. She noted these moves serve to rebalance the portfolio closer to policy targets with the exception of Emerging Markets, which is designed to modestly increase the slight overweight on valuation grounds. The balance of approximately $2.3 million would be moved to Cash, but subject to the amount being transferred from Great Basin College.

Ms. Walker said for the Operating Fund rebalancing, the recommendation is adding $10.0 million to Vanguard Inflation-Protected Securities sourced from PIMCO All Asset All Authority which is similar to the move approved at the March 2016 meeting, as Context TIPS has been underweight the policy target for several years, it has been a highly successful tactical positioning since the underweight was incepted. TIPS has, in that time, returned negative 0.6 percent annualized while the overall Operating Fund has returned 2.9 percent annualized, so this underweight has captured a 3.5 percent performance differential. Cambridge feels TIPS is overvalued relative to historical yields but are increasingly attractive relative to nominal treasuries and, right now, the 10 year break-even yields are approximately 1.7 percent but it would be prudent to moderate the underweight slightly and the $10.0 million addition would bring the

4. Approved-Pooled Endowment and Operating Funds; Operating Pool Reserve – *(continued)*

position size up to 10.2 percent of the Operating Fund versus a 12.0 percent policy target, so it is still a reasonably meaningful underweight – just more moderate.

Regent Crear moved approval for:
Rebalancing and distribution:

- Operating Fund:
  - i) Add $10.0 million to Vanguard Inflation-Protected Securities, sourced from PIMCO All Asset All Authority Fund.

Regent Geddes seconded. Motion carried.

Regent Crear moved approval for:
Rebalancing and distribution:

- Endowment Fund:
  - i) A $2.2 million quarterly distribution from the portfolio to campuses for the quarter ending June 30, 2016, funded from Cash;
  - ii) $0.3 million annual System administration fee, funded from Cash;
  - iii) Upon receipt of the expected $5.8 million inflow from Great Basin College in June, deploy the funds to rebalance the portfolio toward policy targets as follows:
    1. $1.0 million addition to Vanguard Institutional Index;
    2. $0.5 million addition to DFA EM Value;
    3. $1.0 million addition to PIMCO Total Return;
    4. $1.0 million addition to Wells Capital Montgomery Fixed Income; and
    5. Balance (approximately $2.3 million) to Cash.

Regent Geddes seconded. Motion carried.

4. Approved-Pooled Endowment and Operating Funds; Operating Pool Reserve – *(continued)*

Mr. Hullman reported the estimated value of the Operating Pool Reserve as of the close of business on June 8, 2016, was approximately $25.0 million, which is an increase of $18.6 million since the last report in March 2016. He said approximately $3.5 million of income was distributed to the campuses.

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – The Committee recommended approval to direct staff to enter into contract negotiations with Cambridge Associates and Russell Investments for OCIO services for the Endowment Pool in consultation with the Investment Committee Chair and review by the Vice Chancellor for Legal Affairs. Staff should bring both contracts or, if successful with only one firm, a single contract for approval at the September 2016 meeting.

The Committee recommended approval for staff to work with campus business officers in evaluating the long-term portion of the Operating Pool and provide a recommendation at the September 2016 meeting.

Vice Chancellor Redding said this item is finally coming to fruition. He discussed the process after the Committee approved the circulation of the Request for Proposal (RFP) on December 17, 2015, to the present.

Mr. Jeff Mansukhani, Mr. Lindsay VanVoorhis, Ms. Wendy Walker and Mr. David Breiner represented Cambridge Associates. Mr. Mansukhani said it has been an honor to work with NSHE over the last 32 years. The Cambridge Associates' team gave its presentation *(on file in the Board office).* After Cambridge Associates completed their presentation, Chair Melcher asked the Committee for questions.

Regent Crear asked the difference between what Cambridge does for the System now and what it would do as an OCIO. Ms. Walker explained right now Cambridge serves the System on an advisory basis by bringing in recommendations, but it is up to the Committee to vote on each recommendation. She said the process is constrained because of the unique governance circumstances for the System. The meetings are quarterly, but if anything happens requiring a decision outside of the scheduled meetings then a special meeting has to be called. Ms. Walker said as an OCIO she would coordinate the entire portfolio, the asset allocation and marketable investments; Mr. Breiner would take over the marketable alternatives; and Mr. VanVoorhis the private investments portion. The difference is, as an OCIO, Cambridge Associates would be delegated authority to make investments and transactions at any point and report back to the Committee on compliance with the strategic asset allocation.

Vice Chair Davidson asked if Cambridge would manage 100 percent of the portfolio as the OCIO or is there discretion in managing the portfolio. Ms.

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – *(continued)*

Walker said there are various arrangements with clients – some are managed 100 percent and some on a carve-out basis where portions of the portfolio are managed. Vice Chair Davidson thought the public equities sector is fairly common for large investors to use some stock index funds which have a very low cost to carry compared to hiring a manager to do the same thing. Vice Chair Davidson stated it is difficult for a manger to beat those indexes with their fees. He thought the System might want to take advantage of the stock index funds. Ms. Walker said for discretionary clients there is usually a portion of their public equities in index funds because it is an efficient way to rebalance quickly. The index exposures are a part of their mandate because of actively managing the allocations to those indices – it is not that Cambridge is not advising the part of the portfolio that is invested in index funds. Vice Chair Davidson thought it made sense because the response time is quicker.

Mr. Paul Olschwanger, Ms. Lisa Schneider, Mr. Matt Beardsley and Ms. Cara McGinnis represented Russell Investments. Mr. Olschwanger thanked the Committee for inviting Russell Investments to make a presentation *(on file in the Board office).*

Regent Geddes, referring to page 20 of the presentation, asked if the timeframe was the same for the 1 year, 3 years and 5 years of the System's Endowment as of December 31, 2015. Ms. Olschwanger said the timeframe was the same.

Regent Crear wondered how much time would be put into the process for the System. Mr. Beardsley said he has 10 clients, so the System will receive a full share of his time which is available every day. He said there will be a lot of time spent on the front end, which means trips to visit staff, and after that on a quarterly basis but more often if it is requested.

Regent Crear asked for an explanation of the fee schedule and annual fees. He thought it seemed like Russell was investing in only Russell funds. Mr. Beardsley said for the assets the System sets aside for Russell to manage directly (he is aware of the private equity vehicles which may be illiquid), Russell would not take those over immediately because there could be a long horizon before becoming liquid. The remainder of the portfolio that are able to be transitioned and moved to a Russell solution would happen right away so the portfolio would consist of just those items.

Ms. Schneider said page 33 showed a quote for a Russell fund – Russell does not actually manage the money, it is done by third party managers. She went to page 13 where the managers were listed under the Growth bar. The fees being quoted include all of the OCIO services and those underlying manager fees. The assets are pooled together for pricing purposes, which are comingled, multi-manager pools made up of separate account managers. The portfolio will be customized for the System. Ms. Schneider stated with the hedge fund strategies, the System

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – *(continued)*

will own them directly – it is not a hedge fund-of-funds – there will be a separate account portfolio for Russell to buy those directly for its clients.

Ms. Schneider thought it should be viewed as the underlying cost of the manager, something like the cost of goods sold.

Vice Chancellor Redding asked about corporate structure/corporate governance and specifically how to avoid a conflict of interest within that structure. Ms. Schneider said Russell completely separates the consulting group from the OCIO group. She stated from a manager standpoint, there is one manager research team across the globe that ranks all managers. The information can be used by the consultants that are serving consulting clients or by the OCIO team and the portfolio managers that are building client portfolios. Ms. Schneider remarked, interestingly, when it comes to capacity constrained managers, there are asset classes for which Russell does not provide manager research to the consulting client because Russell reserves capacity with those managers for the OCIO clients.

Vice Chair Davidson questioned if the OCIO is an all or nothing, and if there are certain cases where things should be pulled out. Vice Chancellor Redding said areas will be pulled out and recommended the Operating Pool be put aside for now. He said when the pieces were being put together, particularly with the Operating Pool, it is not an excellent fit with the OCIO model as currently structured and it could be done better. Vice Chancellor Redding suggested taking the summer to look at the Operating Pool structure and bring back a specific recommendation to the September 2016 meeting. He stated for today's purposes the discussion is the Endowment only.

Vice Chancellor Redding brought up the question about what the Board does after an OCIO contract. He stated the Board is still the governing body and making the important decisions about the spending rate and strategic asset allocation even to the point of going into manager selection as appropriate. The Board should consider some triggers on long-term private equity placements that would obligate the Board well beyond the term of an OCIO contract.

Vice Chancellor Redding felt the fit is just as important as the performance each firm can bring and either firm would be a fine fit for the System. He believed the Endowment is of the size to be allocated to either firm and not pay a material penalty. He recommended taking time over the summer to negotiate with both firms.

Regent Crear asked about the benefit of hiring two firms. Vice Chancellor Redding thought there were benefits and tradeoffs. The tradeoff would be more work for System staff, the OCIOs and, to a certain degree, the Committee as

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – *(continued)*

performance is monitored for accountability. He said there was more work to go through the negotiation process because there are legacy managers which cannot be exited in a timely manner, especially because of significant penalties, so there would have to be an allocation of those between the firms. Vice Chancellor

Redding said the positives are two highly qualified bidders. The more than $220 million Endowment could be viewed as two $110 million Endowments. He considered another benefit based on successful negotiations with both firms would be all eggs not being in one basket, particularly because handing off this type of operational control is new, and it would be a way to monitor the performance of both firms relative to each other and the constraints of market environments.

Chair Melcher wondered, if both firms were hired there would have to be governance decisions relative to asset allocation, and would the Committee's recommendations come from both companies. Vice Chancellor Redding stated there would be decisions informed by two recommendations. The spending rate and asset allocation would be done annually with information from both consultants. He continued the performance reporting would be from both firms.

Chair Melcher asked about funds being pulled from the Operating Pool to invest in the Endowment. Vice Chancellor Redding said there are three components to the Operating Pool and it is time to formalize what the goals of those three sub-pools are and what the parameters would be. He stated it could be there are other alternatives for the long and even intermediate portion of the Operating Pool. Chair Melcher said there is a possibility to make more money through the Operating Pool by investing it in the Endowment. Vice Chancellor Redding thought an analysis would have to be conducted to make that determination.

Regent Crear wondered what fees Russell and Cambridge would charge for services. Vice Chancellor Redding requested that be the motion – to negotiate with both firms. He pointed out the Committee would probably like to see returns net of fees and it is difficult to take each firm's fees side-by-side to see the best value, of which fees is a portion.

Chair Melcher made a suggested motion "to direct staff to enter into contract negotiations with both firms for OCIO services for the Endowment Pool in consultation with the Chair and review by the Vice Chancellor for Legal Affairs. Staff should bring both contracts or, if successful with only one firm, a single contract for approval to the September 2016 meeting."

Regent Crear asked, based on the submitted proposals, how much it will cost to hire Russell and how much it will cost to hire Cambridge. Ms. Schneider responded that Russell's fee is $1.15 million.

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – *(continued)*

Mr. Russell Campbell, Your Second Opinion, said he has been working with staff on these issues. The most contentious part of the process is figuring out what the fees are. The basic problem is there are two excellent OCIO vendors with very different business models. The most important point is both ending up at the same place. Mr. Campbell continued the Russell Investments model is a pooled model where you pay the fee for a packaged good – it says specifically what the price is. Mr. Campbell continued with the Cambridge model, there will be separate fees depending on what is purchased.

Regent Crear, referring to page 43 of the Cambridge report, noted the lowest fee is $2.07 million and the highest is $2.9 million. He felt there is a big difference in fees between the firms. Ms. Walker said Cambridge is a different model that does not offer any pooled vehicles or any funds Cambridge manages and charges fees for. She stated Cambridge provides clients access to manager relationships that the client owns.

Ms. Walker said Cambridge's fees are transparent and simple – the System will pay only 30 basis points flat, approximately $663,000 to Cambridge, then each manager the System invests in charges their own investment manager fees. Cambridge is accountable to find investment managers that will deliver excess returns after accounting for their fees. Ms. Walker pointed out that Cambridge has delivered, over the long run, significant value above the fees.

Regent Geddes understood the motion was for staff to negotiate for the best terms with both firms on the actual points and return to the Committee in September 2016 with the best recommendation to either go with one firm or split it between the two firms.

Vice Chair Davidson recommended approval to direct staff to enter into contract negotiations with Cambridge Associates and Russell Investments for OCIO services for the Endowment Pool in consultation with the Investment Committee Chair and review by the Vice Chancellor for Legal Affairs. Staff should bring both contracts or, if successful with only one firm, a single contract for approval at the September 2016 meeting. Regent Geddes seconded. Motion carried.

5. Approved-Outsourced Chief Investment Officer Selection (OCIO) – *(continued)*

Regent Geddes recommended approval for staff to work with campus business officers in evaluating the long-term portion of the Operating Pool and provide a recommendation at the September 2016 meeting. Regent Crear seconded. Motion carried.

6. New Business – None.

7. Information Only-Public Comment – None.

The meeting adjourned at 5:37 p.m.

Prepared by:	Nancy Stone Special Assistant & Coordinator to the Board of Regents
Submitted for approval by:	Dean J. Gould Chief of Staff and Special Counsel to the Board of Regents