



Teachers' Retirement System of the State of Illinois

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Richard W. Ingram, Executive Director

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MINUTES

Meeting of the Investment Committee December 10-11, 2012

A meeting of the Investment Committee of the Illinois Teachers' Retirement System was held on December 10, 2012 at the Springfield office of the Illinois Teachers' Retirement System 2815 West Washington Street. Cynthia O'Neill, Chair, called the meeting to order at 9:03 a.m. A quorum was present.

Roll Call attendance was taken with the following trustees present: Cynthia O'Neill (Chair), Mike Busby (Vice Chair), Marcia Campbell, Jan Cleveland, Cinda Klickna, Sharon Leggett, Bob Lyons, Janice Reedus, Enrique Vasquez, Sonia Walwyn (arrived 9:20 a.m.), and Molly Phalen. Absent: Chris Koch

Others present: Dick Ingram, Executive Director; Stan Rupnik, Chief Investment Officer; Greg Turk, Director of Investments; Deron Bertolo, Director of Investment Operations; Scottie Bevill, Sr. Investment Officer; Zak Doehla, Sr. Investment Officer; Ken Musick, Investment Officer; Kenyatta Matheny, Investment Officer; Tim Hays, Sr. Investment Officer; Dakin Sanert, Sr. Investment Analyst; Bill Thomas, Investment Officer; Chuck Handy, Investment Officer; Tom Gray, General Counsel; Cynthia Fain, Sr. Assistant General Counsel; Stacy Smith, Director of Internal Audit; Tassi Maton, Sr. Internal Auditor, Christina Baker, Internal Auditor; Gina Larkin, Director of Human Resources; Jana Bergschneider, Director of Administration; Kathleen Farney, Director of Research; Sally Sherman, Director of Member Services; Rich Frankenfeld, Director of Outreach; Dave Urbanek, Director of Communications; Tammy Green, Asst. to Executive Director; Sue Billington, Executive Assistant; Pat O'Hara, Cavanagh & O'Hara (Fiduciary Counsel); Jamie Shen, Callan Associates (Real Estate Consultant); Becky Gratsinger, John McLaughlin, and Marcia Beard, RV Kuhns (Investment Consultant).

Visitors present: Christine Williamson, Pensions & Investments; Janet Kilgus, IEA-R; Dennis Murfin, IRTA Rep.; Shirley Dodds, IRTA Rep.; Jason Parks, Loop Capital Markets; Jim Baker, UNITE HERE.

APPROVAL OF MINUTES

A draft of the October 25, 2012 minutes of the Investment Committee meeting was sent to the committee for review. On a motion by Sharon Leggett, seconded by Janice Reedus, the minutes were approved, as printed.

OLD BUSINESS

Investment Manager Chart

Stan Rupnik, Chief Investment Officer, provided an organizational chart of TRS's investment managers as of September 30, 2012. Allocations are shown for the main TRS trust fund, the POB account and on a total TRS basis. Documentation is on file.

Cash Withdrawal

Mr. Rupnik discussed the recent cash withdrawals necessary to fund the System's cash requirements. Documentation is on file.

RFP Updates

Staff is reviewing submissions from candidates for real estate co-investment advisor services, a private equity secondary advisor, a private equity co-investment advisor, and an investment performance reporting system. Recommendations are anticipated in February.

STAFF/CONSULTANT PRESENTATIONS

Investment Performance Review – September 30, 2012

RV Kuhns provided an update of the investment performance for the quarter ending September 30, 2012 and provided a preliminary update through October. Total assets: \$37.5 billion. Documentation is on file. In addition, RVK discussed the impact that the fiscal cliff will have on TRS.

The total fund return, gross of fees:

- 1 year: 16.43%
- 3 year: 10.51%
- 5 year: 1.69%
- 10 year: 8.23%

RECESS

The meeting recessed at 9:50 a.m. and reconvened at 10:00 a.m.

W/MBE Utilization Report

Kenyatta Matheny provided data on the participation of minority and female-owned brokers/dealers and investment managers within the TRS investment portfolio through September 30, 2012. Assets under management for WMBE-owned investments were \$4.88 billion, representing 13.04% of the total TRS portfolio. Documentation is on file.

The Senate Committee on Pensions and Investments will conduct annual hearings in Chicago on December 12, 2012. The System will host its annual Opportunity Forum in Springfield on March 21, 2013.

Investment Policy Revisions

Staff proposed revisions to the TRS Investment Policy reflecting the recent change in the System's assumed rate of return. A motion was made by Molly Phalen, seconded by Marcia Campbell, that the committee recommend to the Board to accept revisions to the investment policy, Sections III, XIII, XXV (Investment Philosophy, Performance Benchmarks, and POB Proceeds). The motion passed by a unanimous voice vote.

NEW BUSINESS

Sky Investment Council – Emerging Manager Program

The committee interviewed Sky Investment Council to fill an allocation within the System's Emerging Manager Program. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted. A motion was made by Molly Phalen, seconded by Jan Cleveland, that the committee recommend to the Board to select Sky's

international equity large cap product for a \$25 million assignment within the EMP. The motion passed by a unanimous voice vote.

Herndon Capital Management – Emerging Manager Program

The committee interviewed Herndon Capital Management for graduation from the System's Emerging Manager Program to full mandate within the domestic equity portfolio. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted and noted improved fee terms were negotiated. A motion was made by Bob Lyons, seconded by Cinda Klickna, that the committee recommend to the Board to approve graduation of Herndon Capital Management's large cap core product from the EMP to a 2.0% mandate within the domestic equity portfolio. The allocation will be offset by a reduction of the Rhumblin S&P 500 target from 28.0% to 26.0% and managed to the Russell 1000 index. The motion passed by a unanimous voice vote.

Lombardia Capital Management – Termination

RV Kuhns and Staff recommended the termination of Lombardia's large cap value assignment within the System's Emerging Manager Program due to poor performance. A motion was made by Mike Busby, seconded by Cinda Klickna, that the committee recommend to the Board to terminate Lombardia's large cap value assignment within the EMP. The motion passed by a unanimous voice vote.

STAFF/CONSULTANT PRESENTATIONS

Quarterly Compliance Summary

Staff reviews alerts triggered by the State Street compliance system to determine if there are any discrepancies. Deron Bertolo, Director of Investment Operations, provided a summary of the quarterly compliance for the quarter ended September 30, 2012. TRS is in compliance with Public Acts 95-0616 and 95-0521. Documentation is on file.

RECESS

The meeting recessed at 12:15 p.m. and reconvened at 1:05 p.m.

International Equity Asset Class Annual Review

Greg Turk, Director of Investments, reported on the recent activity within the international equity asset class. A report was submitted on the recently completed investment manager annual reviews along with a summary of recommendations. Staff proposed the following changes in investment mandates:

- Increase emerging manager Strategic Global Advisors international equity all-cap core mandate by \$25 million. Source of funds will be the Rhumblin S&P 500 Emerging Manager account.
- Authorize a search for an emerging market equity manager.

A motion was made by Mike Busby, seconded by Sharon Leggett, that the committee recommend to the Board to approve staff's recommendations within the domestic equity asset class, as presented. The motion passed by a unanimous voice vote.

RECESS

The meeting recessed at 2:10 p.m. and reconvened at 2:15 p.m.

NEW BUSINESS

Gaw Capital Partners – Real Estate

Representatives of Gaw Capital Partners presented an investment opportunity in the firm's real estate fund, Gateway Real Estate Fund IV, Limited Partnership. Their presentation booklet is on file. Staff provided an overview of the due diligence that was conducted. A motion was made by Mike Busby, seconded by Sharon Leggett, that the committee recommend to the Board to commit \$50 million to Gateway Real Estate Fund IV, L.P. to invest in the Asia-Pacific region. The motion passed by a unanimous voice vote.

General Investment Consultant

The current contract with RV Kuhns expires on December 31, 2012. The committee interviewed NEPC and RV Kuhns & Associates as finalists to provide the System with general investment consulting services. Staff

provided an overview of the search process and due diligence that was conducted. Their presentation booklets are on file. A motion was made by Cinda Klickna, seconded by Marcia Campbell, that the committee recommend to the Board to hire RV Kuhns to serve as the System's investment consultant for a period of five years, subject to successful completion of contract negotiations. The motion passed by a unanimous voice vote. Staff will present its future goals to RV Kuhns.

RECESS

The meeting recessed at 6:05 p.m. and reconvened the following day at 8:35 p.m.

MBK Partners

Via videoconference, representatives of MBK Partners presented an investment opportunity in the firm's private equity fund, MBK Partners Fund, III, Limited Partnership. Their presentation booklet is on file. Staff provided an overview of the due diligence that was conducted. Following discussion, a motion was made by Molly Phalen, seconded by Jan Cleveland, that the committee recommend to the Board to commit \$125 million (85% main fund, 15% POB account) to MBK Partners Fund III, L.P. to investments in North Asia. The motion passed by a unanimous voice vote.

RECESS

The meeting recessed at 9:42 a.m. and reconvened at 10:00 a.m.

STAFF/CONSULTANT PRESENTATIONS

Co-Investment

Staff requested ratification of a co-investment opportunity with Natural Gas Partners in an equity capital raise for Mosaic Energy to fund capital expenditures for Mosaic's drilling program and making asset acquisitions. A motion was made by Cinda Klickna, seconded by Jan Cleveland, that the committee recommend to the Board to ratify the Mosaic energy co-investment opportunity with Natural Gas Partners. The motion passed by a unanimous voice vote.

Domestic Equity Asset Class Annual Review

Greg Turk reported on the recent activity within the domestic equity asset class. A report was submitted on the recently completed investment manager annual reviews along with a summary of recommendations. Staff proposed the following changes in investment mandates:

- Increase Boston Partners 130/30 large cap value from 6.0% to 7.0%
- Increase OakBrook large cap enhanced index from 2.0% to 3.0%
- Increase Lombardia small cap value from 2.0% to 3.0%
- Decrease Levin large cap core active from 6.0% to 5.0%
- Decrease Boston Company SMID cap value from 3.0% to 2.0%
- Decrease Rhumblin S&P 500 index allocation from 26.0% to 25.0%
(this target decrease is in addition to the Herndon recommendation)

A motion was made by Marcia Campbell, seconded by Cinda Klickna, that the committee recommend to the Board to approve staff's recommendations within the domestic equity asset class, as presented. The motion passed by a unanimous voice vote.

Real Estate Appraisal Services

Staff issued an RFP in September 2012 for real estate appraisal services resulting in bids from six firms. Staff provided an overview of the due diligence that was conducted. Based on evaluation, staff recommended the selection of Butler Burgher Group, Joseph J. Blake, and U.S. Realty Consultants for asset assignments. BBG would receive 61 appraisal assignments, Blake 35 assignments, and USRC will be retained as a potential service provider and awarded assignments on an as-needed basis. The contract period for all firms is three years. A motion was made by Enrique Vasquez, seconded by Cinda Klickna, that the committee recommend to the Board to engage Butler Burgher Group and Joseph J. Blake for appraisal services at a total cost of \$415,650 for TRS's existing assets. In addition, retain US Realty Consultants as a potential service provider for individual assignments, as needed. The motion passed by voice vote. Trustee Walwyn abstained from voting.

ADJOURNMENT

There being no further business to come before the Investment Committee, a motion was made by Molly Phalen, seconded by Marcia Campbell, to adjourn the meeting at 11:20 a.m.

Richard W. Ingram, Executive Director

Approved _____