

**MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
Joint Meeting of the Board of Trustees and
Advisory Committee on Retirement Matters**

May 20, 2016

On May 20, 2016, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a meeting at 9:00 a.m. at TMRS Headquarters, located at 1200 North IH 35 in Austin, Texas, with the following members present:

Board of Trustees

Jim Parrish, Chair
Bill Philibert, Vice Chair
Julie Oakley
David Landis
Jim Jeffers

Absent: Roel "Roy" Rodriguez

Advisory Committee Members

Alex Cramer, Arlington Professional Fire Fighters Association
David Riggs, Texas State Association of Fire Fighters
Greg Shipley, Combined Law Enforcement Associations of Texas
Victor Hernandez, City Councilmember, City of Lubbock
Tadd Phillips, Texas Municipal Human Resources Association
Greg Vick, Texas City Management Association
Keith Dagen, Government Finance Officers Association of Texas
J.J. Rocha, Texas Municipal League
Bryan Langley, City of Denton
David Russell, Texas Municipal Police Association
Julie Masters, Mayor, City of Dickinson
Michael Dane, City of San Angelo

Present also were:

David Gavia, Executive Director
Eric Davis, Deputy Executive Director
Christine Sweeney, General Counsel
Kristie O'Hara, Director of Human Resources
TJ Carlson, Chief Investment Officer
Rhonda Covarrubias, Director of Finance
Leslee Hardy, Director of Actuarial Services
Robert Klausner, Klausner, Kaufman, Jensen & Levinson
Debbie Munoz, Director of Member Services
Bill Wallace, Director of Communications
Dan Wattles, Director of Governmental Relations

Scott Willrich, Director of Information Resources
Jesse Pittman, Project Manager
Sandra Vice, Director of Internal Audit
Kristin Qualls, Director of Public Equity
Marc Leavitt, Director of Absolute Return
Chris Schelling, Director of Private Equity
Tom Masthay, Director of Real Assets
Jason Weiner, Director of Fixed Income
Dimitry Shishkoff, Director of Risk Management
Karen Jackson, Executive Assistant
Marcia Beard, RVK
Amy McDuffee, Aon Hewitt Investments
Brian Borton, StepStone
Keith Brainard, National Association of State Retirement Administrators
Gary Shilling, A. Gary Shilling and Company

Also in attendance:

Michelle Mellon-Werch, Assistant General Counsel
David Rodriguez, Regional Manager – City Services
Michael Schaff, Assistant General Counsel
Madison Jechow, Assistant General Counsel
Adrienne Strong, Human Resources Generalist
Pete Krnavek, Information Systems Manager
Melanie Thomas, Editor
Carol Leung, Equities Investment Analyst
Chris Tindell, Private Equity Analyst
Cindy Morse, Investment Support Analyst
Debbie Farahmandi, Investment Operations Specialist
Peter Jeske, Project Specialist
Kate Reed, Compliance Officer
Eddie Schultz, Real Estate Analyst
Martha deLivron, Absolute Return Analyst
Rachel Cleak, Alternative Analyst
German Gaymer, Fixed Income Analyst
Melissa Jerkins, Quantitative Analyst
Sherry Chapman, Investment Accountant
Candace Nolte, Assistant Finance Director
Paula Nguyen, Investments Accountant
Arielle Chou, Actuarial Analyst
Peter Jeske, Project Specialist
Bob Scott, City of Carrollton
George Kaufman, City of Garland
Cody Hill, Arlington Professional Fire Fighters
Ashley Rendon, Pension Review Board

Eloisa Mata, Pension Review Board
Kenneth Hubold, Pension Review Board

Mr. Parrish called the meeting to order and the meeting was reconvened at 9:01 a.m.

1. Public Pension Trends Presentation

Mr. Gavia introduced Mr. Keith Brainard, Research Director for the National Association State of Retirement Administrators. Mr. Brainard began with an overview of the statistics associated with public pension in the U.S. including assets, members, retirees and funding levels. He noted that 2009 to 2014 saw an unprecedented period of reform among plans. There is a heightened sensitivity to making required contributions. We are seeing new ways of looking at pension obligations and there is federal interest in increasing public pension oversight and regulation. Since 2009, nearly every state has modified public benefits, raised employee contributions or both. The states considering hybrid plans continue to grow.

Mr. Brainard discussed legal rulings. Many state pension reforms that affected current plan participants provoked lawsuits. An unprecedented number of legal rulings on public pension matters have been issued since 2010. Some states have clear and strong constitutional protections against reducing pension benefits, but bankruptcy rulings have permitted reductions in pension benefits despite strong pension legal protection in those states. Mr. Brainard discussed the fallout from the new GASB disclosures.

Mr. Brainard noted that public sector employment growth remains muted. The number of new retirees continues to grow while the number of active members has remained flat or declined. Change in salary growth has remained tepid causing contribution rates to increase. However, employer spending on public pensions have averaged approximately 3% of total government spending for the past 30 years. Investment return assumptions continue to be reduced and median annualized returns remain muted.

Mr. Brainard reviewed public pension plans in Texas. The four statewide plans account for 90% of assets and members. He noted the six large cities that are not in TMRS and the movement to take these six cities' plans out of state law and returned to local control.

In conclusion, understanding and responding to multiple pension measures remains a challenge. The possibility of federal oversight continues to be a possibility and should continue to be monitored.

The Board thanked Mr. Brainard for his time and for his presentation.

Mr. Parrish asked each of the members of the Advisory Committee to introduce themselves and the group they present.

2. Annual Economic Outlook Presentation

Dr. A. Gary Shilling was introduced by Mr. Gavia and was asked to provide an overview of the current economic conditions. He began by comparing the personal saving rate and household debt. Real Gross Domestic Product (GDP) has been running about 2%, but it is

well below the expected level of 3% to 3.5%. Dr. Shilling compared corporate profits and employee compensation as a percentage of national income. The year-over-year percentage changes in real weekly wages and household incomes have remained flat. Central banks around the globe have been involved in quantitative easing which has contributed to the increase in stock prices, but it has not filtered down to the lower end of the economy. Growth continues to decline in China.

In reviewing manufacturing, Dr. Shilling concluded that globalization is mostly over. In other words, movement of manufacturing out of the US and Western Europe has almost stopped. Oil production of OPEC has remained flat while growth in production has been outside of OPEC. There will likely be further price declines as crude oil storage capacity fills up and more oil is dumped on the market. There will likely be lower prices in other commodities.

Ms. Oakley asked for Dr. Shilling's expectation for the Federal Reserve to raise interest rates in June. The Federal Reserve has a lot of pressure to raise rates, however if the Federal Reserve does raise rates, it is likely to have little impact on the markets.

3. Consider and Act on Private Equity Manager Search Recommendation(s) (formerly #2 on the Thursday, May 19, 2016 agenda)

Mr. Schelling introduced Brian Borton with StepStone and Chris Tindell, TMRS Investment Analyst. He reviewed the Private Equity manager search timeline as well as the search process objectives. Mr. Schelling highlighted the manager search process including the number of managers reviewed at each step and indicated that this process must be flexible because of the short funding windows many managers have. He discussed the manager selection portfolio consideration which included strategy considerations, manager implementation and geographic diversification. Mr. Schelling also reviewed total portfolio construction, focusing on the "growth equity" phase. The four managers recommended for approval span the spectrum from early stage venture capital to late stage venture capital to small buy out.

Mr. Tindell highlighted the characteristics of Providence. Providence targets growth equity investments in lower middle market technology companies in North America. Updata Partners was discussed next. Updata's focus provides growth equity to software and technology service businesses in the lower middle market and is typically the first institutional capital into founder-owned companies.

Mr. Schelling discussed Mercato's characteristics. Mercato will invest in lower middle market, growth stage companies primarily located in the Mountain West region, targeting high potential companies in the Technology, Branded Consumer Products, and Digital Media sectors. Mr. Schelling then discussed Foundry Group which makes investments in early and late stage information technology, Internet and software startups.

Mr. Philibert moved that the Board approve the following investment allocations, each as proposed and in accordance with the TMRS Investment Policy Statement (IPS), with an allocation up to the amount set out below, at fees no greater than proposed in the staff

memo, each individually contingent upon favorable background checks and successful negotiation of the investment agreements:

Fund	Strategy	Allocation
Providence Strategic Growth II, L.P. (Providence)	Growth Equity	\$60 Million
Updata Partners V, L.P. (Updata)	Growth Equity	\$50 Million
Mercato Partners Growth III, L.P. (Mercato)	Growth Equity	\$40 Million
Foundry Group Next, L.P. (Foundry)	Venture Capital	\$35 Million

Mr. Philibert also moved that the Board (i) approve that such investment authorization includes authorization to (a) invest in the named investment fund or in a fund or other alternate investment vehicle formed by the investment managers, their affiliates, or companies associated with the investment manager for the purpose of investing in the named fund or the fund strategy as described in the Staff memo, and/or (b) make such investment indirectly through a parallel fund, feeder fund, or alternate investment vehicle; (ii) approve that each allocation may include the option to participate in the fund's distribution reinvestment program, if any, and may exceed the authorized commitment to the fund by the value of the distribution reinvestments, when TMRS Staff and its Private Equity consultant determine that it is economically advantageous to do so and in accordance with the TMRS IPS Private Equity guidelines; (iii) authorize the Executive Director to negotiate, execute, acknowledge, and deliver any and all contracts, agreements, and other documents or instruments on such terms and conditions as are satisfactory to the System, such satisfactory terms and conditions to be conclusively evidenced by the execution thereof by the Executive Director, and to do any and all other acts deemed by the Executive Director in his judgment to be necessary or appropriate in the best interests of TMRS to give effect to such investment authorizations, including, without limitation, proceeding with the investment even if the final fund name is different than above as long as the underlying investment is still substantially the same investment as was proposed in the staff memo; and (iv) approve that the management and incentive fees in each fund are exclusive of the capital allocation and may be paid through cash flow of the investment, capital calls, or via invoice. Ms. Oakley seconded the motion, which passed 5-0.

4. **Consider and Act on Real Estate Manager Search Recommendation(s) (formerly #3 on the Thursday, May 19, 2016 agenda)**

Mr. Masthay and Mr. Schultz presented the Real Estate manager recommendation. Mr. Schultz reviewed the search process timeline, objectives and the process that resulted in the recommendation of Kildare European Partners II, LP. He discussed portfolio construction considerations, including strategy, manager and geographic diversification. Geographic diversification is key as it lowers volatility in the portfolio by providing exposure to geographies and economies that are in different states of their economic cycle.

Kildare is an opportunistic manager whose principal strategy is accessing commercial real estate debt and equity investments through distressed assets. Kildare looks at performing,

sub-performing and non-performing loans secured directly or indirectly by commercial real estate assets which they can buy at a discount. One of the main reasons to invest is their CEO Ellis Short and his extensive background operating in the space. Ms. Oakley asked about the headline risk associated with the Mr. Short and what has been done to mitigate this risk. Mr. Masthay spoke to the overall framework for consideration including the background check process which culminated with TMRS outside counsel, Kutak Rock, providing a letter stating that it was “reasonable for the system to conclude that no material issue exists with respect to Mr. Short”. It was noted that past headline issues were in large part related to his time working at Lone Star. Mr. Schultz noted that Kildare is a smaller group and it is taking a different approach than Lone Star. Currency risk was also discussed – it was noted that the fund hedges currency risk back to US dollars.

Mr. Landis moved that the Board approve the following investment allocation, as proposed and in accordance with the TMRS Investment Policy Statement (IPS), with the allocation up to the amount set out below, at fees no greater than listed in the staff memo and contingent on favorable background checks and successful negotiation of the investment agreements.

Fund	Strategy	Allocation
Kildare European Partners II, LP (“Kildare”)	Opportunistic	\$100 Million
Total Allocation		\$100 Million

Mr. Landis also moved that the Board (i) approve that such investment authorization includes authorization to (a) invest in the named investment fund or in a fund or other alternate investment vehicle formed by the investment managers, their affiliates, or companies associated with the investment manager for the purpose of investing in the named fund or the fund strategy as described in the Staff memo, and/or (b) make such investment indirectly through a parallel fund, feeder fund, or alternate investment vehicle; (ii) approve that each allocation may include the option to participate in the fund’s distribution reinvestment program, if any, and may exceed the authorized commitment to the fund by the value of the distribution reinvestments, when TMRS Staff and its Real Estate consultant determine that it is economically advantageous to do so and in accordance with the TMRS IPS Real Estate guidelines; (iii) the Board authorize the Executive Director to negotiate, execute, acknowledge, and deliver any and all contracts, agreements, and other documents or instruments on such terms and conditions as are satisfactory to the System, such satisfactory terms and conditions to be conclusively evidenced by the execution thereof by the Executive Director, and to do any and all other acts deemed by the Executive Director in his judgment to be necessary or appropriate in the best interests of TMRS to give effect to such investment authorizations, including, without limitation, proceeding with the investment even if the final fund name is different than above as long as the underlying investment is still substantially the same investment as was proposed in the staff memo; and (iv) approve that the management and incentive fees in each fund are exclusive of the capital allocation and may

be paid through cash flow of the investment, capital calls, or via invoice. Mr. Philibert seconded the motion, which passed 5-0.

5. Consider and Act on Real Return Manager search Recommendation(s) (formerly #4 on the Thursday, May 19, 2016 agenda)

Mr. Masthay reviewed the Real Return search process timeline, the search process objectives and scoring. After final due diligence, Brookfield Infrastructure Fund III, L.P. is recommended for Board approval.

Mr. Masthay discussed the portfolio considerations. Data documenting global shortage of infrastructure financing was presented as a key consideration. Mr. Masthay presented information pertaining to risks associated with the global nature of fund exposures. It was noted that the fund offers exposure to high quality core assets that generate strong risk-adjusted returns and that TMRS' consultant Albourne rates this manager and fund highly.

Mr. Masthay then discussed portfolio construction including strategy, manager and geographic diversification. He said that the TMRS Real Return portfolio will pursue geographic diversity in the underlying portfolio assets through a measured and modest implementation. He then reviewed the candidate characteristics, stating that the fund offers exposure to high quality core assets that generate strong risk-adjusted returns. The firm executes deals globally, in countries where they have a local presence.

Mr. Masthay noted there is also a recommendation to ratify a \$350 million allocation for investment in the Real Asset Multi-Strategy of Cohen & Steers Capital Management Inc. or its affiliates (Cohen & Steers), an allocation that was originally approved by the Board on December 3, 2015.

Ms. Oakley moved that the Board approve the following allocation, as proposed and in accordance with the TMRS Investment Policy Statement (IPS), with the allocation up to the amount set out below, at fees no greater than listed in the staff memo and contingent on favorable background checks and successful negotiation of the investment agreements.

Fund	Strategy	Allocation
Brookfield Infrastructure Fund III-B, L.P. ("Brookfield")	Infrastructure	\$150 Million
Total Allocation		\$150 Million

Ms. Oakley also moved that the Board (i) approve that such investment authorization includes authorization to (a) invest in the named investment fund or in a fund or other alternate investment vehicle formed by the investment managers, their affiliates, or companies associated with the investment manager for the purpose of investing in the named fund or the fund strategy as described in the Staff memo, and/or (b) make such investment indirectly through a parallel fund, feeder fund, or alternate investment vehicle; (ii) approve

that each allocation may include the option to participate in the fund's distribution reinvestment program, if any, and may exceed the authorized commitment to the fund by the value of the distribution reinvestments, when TMRS Staff and its Real Return consultant determine that it is economically advantageous to do so and in accordance with the TMRS IPS Real Return guidelines; (iii) authorize the Executive Director to negotiate, execute, acknowledge, and deliver any and all contracts, agreements, and other documents or instruments on such terms and conditions as are satisfactory to the System, such satisfactory terms and conditions to be conclusively evidenced by the execution thereof by the Executive Director, and to do any and all other acts deemed by the Executive Director in his judgment to be necessary or appropriate in the best interests of TMRS to give effect to such investment authorizations, including, without limitation, proceeding with the investment even if the final fund name is different than above as long as the underlying investment is still substantially the same investment as was proposed in the staff memo; and (iv) approve that the management and incentive fees in each fund are exclusive of the capital allocation and may be paid through cash flow of the investment, capital calls, or via invoice.

Further, Ms. Oakley moved that the Board ratify the previous approval of the Cohen & Steers Real Assets Multi-Strategy Fund, a sub-fund of the Cohen & Steers Collective Investment Trust with the highlighted clarification:

“The Board authorizes that TMRS allocate \$350 million for investment in the Real Asset Multi-Strategy of Cohen & Steers Capital Management Inc. or its affiliates (Cohen & Steers), and if invested through a commingled investment trust structure which has a TMRS specific share class, to be at fee terms no greater than a flat fee of 55 bps and where SEI Trust Company is Trustee of the Cohen & Steers Collective Investment Trust; or, if invested through a mutual fund or other type of commingled fund structure, to be at an expense ratio no greater than 110 basis points. This recommendation is contingent upon successful negotiation of the investment agreements.” Mr. Philibert seconded the motion, which passed 5-0.

6. RVK Quarterly Investment Report (formerly #6 on the Friday, May 20, 2016 agenda)

Ms. Beard stated the first quarter started negatively, but reversed in March due to renewed optimism. By the quarter's end, global equities had sufficiently rallied to produce marginal overall gains for investors. She reviewed the total fund composite and negative cash flow is reflected in the return numbers. The allocation versus peers was reviewed noting TMRS has more exposure in fixed income, but the portfolio continues to move towards a well-diversified structure. Ms. Beard reviewed total fund performance versus benchmarks. The composite performance was discussed on a net of fees basis.

7. Chief Investment Office Management Update, Including Governance, Personnel, Manager Updates, Negative Interest Rates and Other Investment Related News or Matters (formerly #12 on the Friday, March 24, 2016 agenda)

Mr. Carlson noted that 354 meetings were taken by the team translating to approximately 100-200 hours. This does not include meetings where managers are not selected.

8. **Executive Director Update (formerly #8 on the Friday, March 24, 2016 agenda)**

Mr. Gavia introduced Kristie O'Hara and Adrienne Strong to review the Human Resources Department. Ms. O'Hara highlighted the areas of responsibility and reviewed key areas of accomplishments. This included new hires, the 2014 Compensation Study, policy manual reviews, bilingual pay program, parking cash out program, intern program and the HRIS system implementation. Ms. O'Hara discussed programs and projects on the horizon including a work flex program and succession plans.

9. **Call for Future Agenda Items**

None were noted.

Mr. Philibert made a motion to adjourn the meeting. Mr. Landis seconded, which passed 5-0. The meeting was adjourned at 12:48 p.m.



David Gavia
Executive Director



Jim Parrish
Chair, Board of Trustees