

**MINUTES OF THE**  
**NEW MEXICO EDUCATIONAL RETIREMENT BOARD**  
**INVESTMENT COMMITTEE**

July 8, 2010

**CALL TO ORDER**

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at approximately 1:30 p.m. in the Educational Retirement Board Room, 6201 Uptown Boulevard, N.E., Ste. 203, Albuquerque, New Mexico.

A quorum was not present:

**Members Present:**

Mr. Bruce Malott, Chair  
Dr. Beulah Woodfin

**Members Excused:**

Mr. H. Russell Goff  
Ms. Jan Goodwin

**Other ERB Members Present:**

Dr. Gautam Vora

**Legal Counsel Present:**

None.

**Staff Present:**

Mr. Bob Jacksha, CIO  
Ms. LeAnne Larrañaga-Ruffy, Investment Officer  
Mr. Steve Neel, Deputy CIO  
Mr. Jude Perez  
Mr. Jeff Riggs, Deputy Director

**Others Present:**

Mr. Allan Martin, NEPC  
Mr. Bill Monagle, NEPC

[Lacking a quorum, the Committee proceeded with non-action items on the Agenda.]

## **PRIVATE EQUITY PROGRAM QUARTERLY UPDATE: Bill Monagle**

NEPC consultant Bill Monagle commented that the ERB's Private Equity program is a relatively new program (June 2006) and overall is out of the J-curve with an annualized IRR of 1.46%. He said the ERB committed \$692.7 million to this program and has funded \$266 million, with \$16.8 million received in distributions to date.

Mr. Malott asked if NEPC is concerned that any of the ERB's private equity managers might be holding onto cash while simply collecting fees. He said he recently read an article about the disjointed nature of the markets where private equity managers were holding back on making investments and that some entities were asking for money back to reduce their commitments.

Mr. Monagle responded that NEPC has no concerns with that. He said there was a concern initially with Lexington Capital VII, but today's *Wall Street Journal* reports that Citigroup is about to sell a portfolio of roughly \$1 billion of private equity investments to Lexington. He said NEPC had been in ongoing discussions with Lexington around NEPC's concerns that Lexington hadn't yet made an investment, but it is a delicate balance between encouraging them to make investments while also encouraging them to make the right investments.

Mr. Monagle said that, overall, the exposure is primarily in the Mega Buyout space, where the ERB has no exposure. He said NEPC has also tilted the portfolio to Distressed, Secondaries and Mezzanine. He noted that the return for the Distressed managers in the quarter was 9.56% and for the year was 85.12%. He said Buyouts and Secondaries also generated positive returns for the quarter at 3.04% and 2.23% respectively and for the trailing one-year period at 20.15% and 18.10%. He added that Mezzanine is doing as expected, generating 3.52% for the quarter and a 5.51% IRR since 2006; and while this may not seem like much, it far outpaces the S&P 500.

Mr. Monagle stated that, for 2010, the following commitments are planned:

- \$100 million to Distressed;
- \$45 million to Secondaries;
- \$40 million to Mezzanine; and
- \$40 million to Buyouts.

Mr. Monagle said NEPC plans to bring managers back to the Investment Committee for approval in the next two to three months.

Mr. Malott asked Mr. Neel to discuss the status of the Aldus Equity/Erasmus Co-Investment Fund.

Mr. Neel responded that the ERB is in the process of getting the assets transitioned from the General Partners to a separate runoff fund. He said ERB General Counsel Chris Schatzman did write to Aldus, asking for their cooperation, and received no response. He said the ERB is now going directly to the portfolio companies to get the certificates changed into the ERB's name, and anticipates no problem in getting that done.

Mr. Jacksha commented that there will be some legal issues expected around what rights they have to fees, participation, profits, etc.

Dr. Vora asked Mr. Monagle if NEPC is looking at other categories in the Private Equity space and Mr. Monagle responded that they are looking at managers in the Secondary Direct space, but are also focusing on Distressed. He said real estate debt coming due between now and 2014 is \$1.4 trillion, of which \$870 billion is underwater, and on top of this are leveraged loans coming due as well as high yield coming due—so the wall of debt is there.

Mr. Monagle said NEPC is also looking at Mezzanine because of the number of banks that have already failed along with an estimated 700 banks still having problems. He said NEPC is looking at people who will do mid-market type lending as well as project based financing in the energy area, e.g., pipelines.

Mr. Monagle clarified for Dr. Vora that, while NEPC does look at the emerging manager niche, right now they are looking at people with experience; so if they can produce a 10-15 year track record from a previous entity, NEPC is very happy to work with them.

Mr. Martin added that NEPC is working with ERB staff on other credit opportunities that may not be structured as Private Equity, for example, Direct Lending. He said there are a lot of smaller companies that need to finance their growth and can't borrow from banks because banks aren't lending. He said CIT and GE Capital are getting out of the business or curtailing the business, so there are a number of opportunities in that space, where loans would be directed through a manager to those kinds of companies. He said they are generally priced at LIBOR + 6 to LIBOR +12, and the return comes in the coupon.

### **MAY FLASH REPORT**

Mr. Jacksha reported that May was a difficult month in the markets, with a –4.20% return, slightly better than the benchmark and significantly better than the S&P, which was down almost 8%.

Mr. Jacksha referred to the Domestic Equity portfolio return and said he was inclined to go to indexing in the Large Cap area based on the longer-term performance of the managers.

Dr. Woodfin noted that Mr. Jacksha had emailed Board members regarding a query he had received about the ERB's exposure to BP and the fact that one of the managers had sold BP. She asked where the ERB's current exposure is.

Mr. Jacksha responded that Brandywine was the Domestic manager that had some in ADR, but sold it. He said the other exposure was with Alliance Bernstein in the EAFE portfolio. He said BP is not an S&P 500 company so is not traded in the index.

Mr. Jacksha stated that he would schedule a presentation and review of the Infrastructure program at the August meeting.

Mr. Malott asked how the two Lone Star Real Estate Funds are doing, and Mr. Jacksha responded that they have gotten off to a slow start— they are trying to raise \$5 billion for each of the two funds and have raised about \$2 billion total.

### **OTHER INVESTMENT REPORTS**

Mr. Jacksha stated that one of the funds being considered for a Mezzanine investment is Newstone; however, Newstone was one of the funds that paid a third party marketer. He asked for guidance from the Committee.

Mr. Malott commented that the ERB is a fiduciary and so has the duty to look at any opportunity that might benefit the Fund, and Newstone has performed well for the ERB. He added that he would have a lot of questions to ask them before considering another investment, however.

Dr. Woodfin asked if Newstone has been involved in any kind of government or legal proceedings as a result of the third party issue, and Mr. Jacksha responded that they were questioned by the authorities along with all of the other funds that were involved; however, he was not aware of them being targeted in any inquiry or being sued by anyone. He said staff could explore that further.

Mr. Jacksha said he attended Newstone's annual meeting and talked to some of the partners at length. He stated that his feeling is that Newstone felt they were engaging in a legitimate placement agent hiring, and were surprised by what was going on in New Mexico. He stated that Newstone is not using any placement agents for the ERB, SIC or any other New Mexico entity in this next funding round.

Mr. Neel commented that this issue will come up again over the next few months as a number of other funds the ERB has invested in come back to the market.

Responding to Dr. Vora, Mr. Jacksha stated that he has no problem with the legitimate use of a placement agent provided it is fully disclosed. He said the problem in the past was that there was no disclosure. He added that, when a placement agent appears to have done no work, he does not call that a legitimate placement agent relationship.

Mr. Martin commented that, when someone is running an entity and wants to bring in new business, they should be free to decide between either hiring a fulltime employee to do that or else outsourcing that to a third party. He said the outsourcing option is more sensible for entities who are not continuously in the market, such as entities in real estate or private equity, who have a fundraising period and then move on. He said 60% of buyout private equity funds employ placement agents.

Mr. Jacksha stated that, if there is fair disclosure and a legitimate contractual relationship, the ERB doesn't have a problem with that—and the placement agent policy that the Board adopted reflects that.

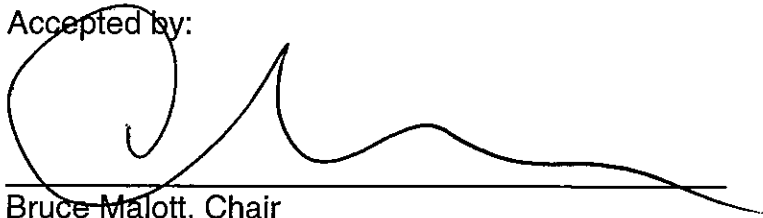
Mr. Jacksha described how ERB staff calculates returns as reflected in the Flash Reports. He said some returns, such as PIMCO's, have manager fees built in.

Mr. Martin noted that EnnisKnupp recommended preparing reports showing net and gross of manager fees. He said the industry standard has been gross of fees, so that one can compare the performance of Manager A against Manager B and not be adjusting for fees. He said NEPC will be doing both for the ERB.

## **ADJOURN**

Its business completed, the Investment Committee adjourned the meeting at approximately 2:15 p.m.

Accepted by:



Bruce Malott, Chair

