



Teachers' Retirement System of the State of Illinois

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MINUTES

Meeting of the Investment Committee October 25, 2012

A meeting of the Investment Committee of the Illinois Teachers' Retirement System was held on October 25, 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 8:32 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, Sonia Walwyn Molly Phalen, and Chris Koch. Absent: Enrique Vasquez

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; Dakin Sanert, Sr. Investment Analyst; Tom Gray, General Counsel; Cynthia Fain, Sr. Assistant General Counsel; Stacy Smith, Director of Internal Audit; Dave Urbanek, Director of Communications; Tammy Green, Asst. to Executive Director; Sue Billington, Executive Assistant; Sally Haskins, Callan Associates (Real Estate Consultant); Becky Gratsinger, John McLaughlin, and Jonathon Kowolik, RV Kuhns (Investment Consultant); Mike Krems, Christian Ulloa, and Kara King, TorreyCove (Private Equity Consultant); Patrick Donohue, State Street (Custodian), and Pat O'Hara, Cavanagh & O'Hara (Fiduciary Counsel).

Visitors present: Christine Williamson, Pensions & Investments; Janet Kilgus, IEA-R; Dennis Murfin, IRTA Rep.; Shirley Dodds, IRTA Rep.; Jason Parks, Loop Capital Markets; Andrew Perkins and Tom LaHood, Senate GOP.

APPROVAL OF MINUTES

A draft of the August 22-23, 2012 minutes of the Investment Committee meeting was sent to the committee for review. On a motion by Bob Lyons, seconded by Janice Reedus, the minutes were approved, as amended.

OLD BUSINESS

Investment Manager Chart

Stan Rupnik, Chief Investment Officer, provided an organizational chart of TRS's investment managers as of June 30, 2012 and a chart with preliminary public market values for 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 RFP responses for real estate co-investment advisor services, general investment consulting, and an investment performance reporting system. Recommendations are anticipated in December.

The RFPs for real estate appraisal services and for a private equity secondary advisor were posted on the TRS website with submission deadline dates of October 12 and November 13, 2012.

NEW BUSINESS

Silver Lake Management – Private Equity

Representatives of Silver Lake Management Company provided an investment opportunity in the firm's private equity fund, Silver Lake Partners 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 Cinda Klickna, seconded by Sonia Walwyn, that the committee

recommend to the Board to commit up to \$150 million to Silver Lake Partners IV, L.P. with 85% allocated to the main TRS trust fund and 15% to the POB account. The motion passed by unanimous voice vote.

STAFF/CONSULTANT PRESENTATIONS

Investment Performance Review – June 30, 2012

RV Kuhns provided an overview of the final June 30, 2012 fiscal year end investment performance report noting a positive 0.76 percent rate of return during FY 12. Total assets: \$36.3 billion. Documentation is on file. Stan Rupnik provided preliminary data of the investment performance for the quarter ended September 30, 2012 noting for the 12-month period ending on September 30, the rate of return was 16.4 percent. The June 30, 2012 total fund return, gross of fees:

- 1 year: 1.3%
- 3 year: 12.7%
- 5 year: 1.2%
- 10 year: 6.9%

RECESS

The meeting recessed at 10:10 a.m. and reconvened at 10:25 a.m.

Real Estate Performance – June 30, 2012

Callan Associates provided an overview of the real estate performance for the quarter ended June 30, 2012. Documentation is on file. Total fund return:

- Quarter: 2.6%
- 1 year: 10.6%
- 3 year: 7.7%
- 5 year: (1.5%)
- 10 year: 7.8%

Private Equity Performance Review – June 30, 2012

TorreyCove Capital Partners provided an overview of the investment performance within the private equity asset class for fiscal year 2012. Documentation is on file.

- 1 year: 5.7%
- 3 year: 16.2%
- 5 year: 6.7%
- 10 year: 11.5%

RECESS

The meeting recessed at 12:00 p.m. and reconvened at 1:00 p.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 June 30, 2012. Assets under management for WMBE-owned investments were \$4.78 billion, representing 13.17% of the total TRS portfolio. Documentation is on file.

Staff proposed that the brokerage utilization goals for fiscal year 2013 remain at 15.0% for fixed income while increasing the goal for international equity to 12.0%, up by 1.0% , and increasing the goal for domestic equity to 16.0%, up by 1.0%. Additionally, staff recommended the goal for assets under management be set at 15.0% of the total fund, up by .50% from the prior fiscal year. A motion was made by Bob Lyons, seconded by Sonia Walwyn, that the committee recommend to the Board to approve the W/MBE FY 2013 goals, as presented. The motion passed by a unanimous voice vote.

Domestic Equity Asset Class

Bill Thomas, Investment Officer, reported on the recent activity within the domestic equity asset class. Staff requested ratification for the termination of the Denali Advisors large cap value mandate due to poor performance, decline of firm assets, and lack of conviction in the investment process. A motion was made by Mike Busby, seconded by Marcia Campbell, that the committee recommend to the Board to ratify the termination of Denali's

large cap value mandate and approve an offsetting 2.0% target allocation increase to the S&P 500 index fund. The motion passed by a unanimous voice vote.

Staff requested ratification of three items related to the domestic equity large cap growth portfolio. 1) The termination of Turner Investment Partners current 5.0% domestic equity mandate due to poor performance and lack of conviction in the investment process; 2) Award a mandate to J.P. Morgan's large cap growth product; and 3) the resulting transfer of assets from Turner Investment Partners to J.P. Morgan and cash flow accounts. Staff also requested approval to reallocate Turner's 5% target mandate to J.P. Morgan (establishing a 3% mandate) and for a 2% increase to the Rhumblin S&P 500 target mandate (this increase was in addition to the request related to the Denali approval). A motion was made by Bob Lyons, seconded by Janice Reedus, that the committee recommend to the Board to adopt the ratifications and approvals noted above. The motion passed by a voice vote. Trustee Busby abstained from voting.

Staff requested ratification of fee revisions for three domestic equity mandates: Boston Company SMID Value, Frontier Small Growth, and J.P. Morgan's 130/30 portfolio. A motion was made by Marcia Campbell, seconded by Jan Cleveland, that the committee recommend to the Board to ratify the fee revisions, as presented. The motion passed by a unanimous voice vote.

International Equity Asset Class

Chuck Handy, Investment Officer, reported on the recent activity within the international equity asset class. Staff requested ratification for the termination of Brandes Investment Partners' current 10.0% international equity large cap value mandate due to poor performance and lack of conviction in the investment process. In addition, staff requested to ratify the hire of LSV Asset Management's international equity large cap value product with initial funding of approximately 5.0% with remaining assets to be managed by State Street Global Markets on an interim basis. A motion was made by Sharon Leggett, seconded by Bob Lyons, that the committee recommend to the Board to ratify the termination of Brandes Investment Partners large cap value mandate, ratify hire of LSV's large cap value product, and ratify an interim investment management assignment to the

State Street Optimized MSCI EAFE value index portfolio. The motion passed by a unanimous voice vote.

Staff requested ratification for the termination of Putnam Investments' current 3.0% international small cap mandate due to poor performance and lack of conviction in the investment process and the hire of Mondrian Investment Partners' small cap product. A motion was made by Marcia Campbell, seconded by Janice Reedus, that the committee recommend to the Board to ratify the termination of Putnam Investments' small cap mandate and the hire of Mondrian Investment Partners' small cap product. The motion passed by a unanimous voice vote.

Fixed Income and Real Return Reports and Annual Reviews

Scottie Bevill, Sr. Investment Officer, reported on the recent activity within the fixed income and real return portfolios. A report was submitted on the recently completed investment manager annual reviews along with a summary of recommendations.

Fixed Income:

- Reduce Dolan McEniry Capital Management's target from 7.5% to 5.0%
- Increase MacKay Shields' target from 10.0% to 13.5%
- Reduce Loomis Sayles' target from 14.0% to 13.0%
- Reduce Prudential's target from 10.0% to 9.0% as an offset to a proposed increase to the Special Situations target from 5.0% to 6.0%

Real Return:

- Maintain New Century Advisors target and PIMCO's target. Adjust the allocation range around the global inflation linked composite target of 24% to +/-10% (from current range of +/-5%)
- Maintain PIMCO Global Multi-Asset Strategy (GMAS) at current target, with elimination of the GMAS POB account. Proceeds from the GMAS POB account will be rebalanced into GMAS main trust fund account or rebalanced into other real return accounts as appropriate.

A motion was made by Sharon Leggett, seconded by Cinda Klickna, that the committee recommend to the Board to approve staff's recommendations

within the fixed income asset class and real return asset class, as presented. The motion passed by a unanimous voice vote.

LM Capital

Staff and LM Capital have agreed that any incentive fee earned will be paid annually rather than quarterly. The fee revision is effective January 1, 2013. A motion was made by Cinda Klickna, seconded by Bob Lyons, that the committee recommend to the Board to approve the revision to LM Capital's fee structure, as presented. The motion passed by a unanimous voice vote.

RECESS

The meeting recessed at 3:02 p.m. and reconvened at 3:20 p.m.

NEW BUSINESS

AQR Capital Management – Fixed Income

Representatives of AQR Capital Management presented an investment opportunity in the firm's Balanced Reinsurance Fund. Their presentation booklet is on file. Staff provided an overview of the due diligence that was conducted. A motion was made by Bob Lyons, seconded by Jan Cleveland, that the committee recommend to the Board to commit \$40 million to the AQR Risk Balanced Reinsurance Fund, Ltd. in the 2013 REIN vehicle. The funding source will be TRS assets in AQR real return mandates. The motion passed by a unanimous voice vote.

Watch List

Stan Rupnik provided an update of the investment managers currently on the watch list for the quarter ended September 30, 2012. The existing managers remain on watch due to performance reasons: Boston Company SMIDV (domestic equity), Frontier Capital Management (domestic equity), and Levin Capital Management (domestic equity). The following managers were recommended for termination due to performance reasons: Brandes Investment Partners (international equity), Turner Investment Partners (domestic equity), Denali Advisors (domestic equity), and Putnam Investments (international equity). A motion was made by Cinda Klickna, seconded by Marcia Campbell, that the committee recommend to the Board

to accept the watch list, as presented. The motion passed by a unanimous voice vote.

Private Equity Asset Class

Staff reported on the amendments proposed within the private equity program. Staff and TorreyCove voted on 45 amendments within the private equity program from January 1, 2011 through August 31, 2012.

Private Equity Co-investment Advisor Consultant RFP

Staff issued an RFP in January 2012 for private equity co-investment advisor services but the responses were not deemed satisfactory. Staff requested the reissuance of a formal request-for-proposal. A motion was made by Cinda Klickna, seconded by Molly Phalen, that the committee recommend to the Board to authorize a RFP for a private equity co-investment advisor. The motion passed by a unanimous voice vote.

K2 Advisors, LLC

Staff reported that Franklin Templeton Institutional, LLC has purchased a majority of the equity of K2 Advisors, LLC. Since this transaction represents a change in control, K2 Advisors requested the System's consent to allow them to continue providing services to K2 Bluegill Fund following the sale to Franklin Templeton Institutional. A motion was made by Bob Lyons, seconded by Mike Busby, that the committee recommend to the Board to allow K2 Advisors to provide advisory services to K2 Bluegill Fund following the sale to Franklin Templeton Institutional. The motion passed by a unanimous voice vote.

Annual Reports

Deron Bertolo, Director of Investment Operations, presented the standard year-end reports for fiscal year 2012. The reports included proxies, broker activity, commission recapture, security lending, bankruptcy and securities litigation, and the annual performance reviews documenting the quality of service provided by consultants and custodian.

Securities Lending RFP

In February 2012, the Board authorized a search for providers of securities lending services. Staff provided an overview of the search process and an analysis of the finalist candidates. A motion was made by Sonia Walwyn, seconded by Chris Koch, that the committee recommend to the Board to select Citi to be the System’s securities lending provider, subject to successful contract negotiations. The motion passed by a unanimous voice vote.

ADJOURNMENT

There being no further business to come before the Investment Committee, a motion was made by Molly Phalen, seconded by Jan Cleveland, to adjourn the meeting at 5:20 p.m.

Richard W. Ingram, Executive Director

Approved _____