



STATE OF OREGON
OFFICE OF THE STATE TREASURER
350 WINTER STREET NE, SUITE 100
SALEM, OREGON 97301-3896

OREGON INVESTMENT COUNCIL
JANUARY 23, 2013
MEETING MINUTES

Members Present: Paul Cleary, Harry Demorest, Katy Durant, Keith Larson, Dick Solomon, Ted Wheeler

Staff Present: Darren Bond, Tony Breault, Karl Cheng, Jay Fewel, Sam Green, Andy Hayes, John Hershey, Julie Jackson, Mary Krehbiel, Perrin Lim, Tom Lofton, Mike Mueller, Tom Rinehart, Michael Selvaggio, James Sinks, John Skjervem, Michael Viteri, Byron Williams

Consultants Present: David Fann and Kenn Lee (TorreyCove); John Meier (SIS); Alan Emkin and Mike Moy (PCA)

Legal Counsel Present: Dee Carlson, Oregon Department of Justice
Deena Bothello, Oregon Department of Justice

The OIC meeting was called to order at 9:00am by Keith Larson, Chair.

I. 9:00 a.m.: Review and Approval of Minutes

MOTION: Treasurer Wheeler moved approval of the December 5, 2012 meeting minutes. Ms. Durant seconded the motion. The minutes were approved by a vote of 5/0.

John Skjervem, CIO updated council members on committee actions taken since the last OIC meeting:

Private Equity Committee:

December 13, 2012 CDH Fund V, LP \$75 million commitment approval

II. 9:01 a.m.: Riverside Capital Appreciation Fund VI, L.P. - OPERF Private Equity Portfolio

Staff recommended a \$75 million commitment to Riverside Capital Appreciation Fund VI, L.P., subject to staff working with Department of Justice personnel in support of successful legal document negotiations.

Riverside was formed in 1988 by Bela Szigethy to focus on the SMM space, as Mr. Szigethy identified what he believed to be an abundance of attractive but under-pursued investment opportunities. Five years later, Stewart Kohl joined Riverside as Co-CEO. Mr. Kohl and Mr. Szigethy worked together at Citibank Venture Capital, prior to Riverside, and were personal friends dating back to their time together as students at Oberlin College

The Fund has a target size of \$1.0 billion, with a hard cap set at \$1.5 billion, and will seek to invest in 20 - 30 Small Middle Market (SMM) opportunities, with a generalist, rather than sector-specific focus. While Riverside employs a generalist approach, their history shows success in the consumer discretionary, industrial and health care industries. Riverside, as a firm, invests across the globe in multiple different funds.

The Fund will invest primarily in companies that are established leaders within their markets, or that have the potential to become such market leaders. This criterion typically involves demonstrating a sustainable competitive advantage and/or market share leadership. A fundamental element of Riverside's strategy is to find small companies through proprietary sources, rather than an auction process, which leads to relatively lower EBITDA purchase multiples.

Once changes to increase a company's revenue and EBITDA as well as efforts to institutionalize its business model have been successfully implemented, Riverside's most common exit strategy is a sale to either a strategic or financial buyer. Evidence of Riverside's ability to exit portfolio companies profitably can be found in OPERF's prior Riverside Capital Appreciation Fund (RCAF) investing experience. Specifically, OPERF has invested in three prior RCAF funds, with commitments totaling \$225 million (see below).

As of December 31, 2012, Riverside has called roughly \$199 million of OPERF capital and returned roughly \$220 million with significant value remaining.

There was a brief question and answer period following the presentation.

MOTION: Ms. Durant moved approval of the staff recommendation. Treasurer Wheeler seconded the motion. The motion was passed by a vote of 5/0.

III. 9:55 a.m.: Public Equity Mandate/Manager Recommendations

Staff recommended a) funding DFA's proposed Micro Cap Value strategy with both an initial commitment of \$150 million and an option to increase OPERF's allocation to this strategy by an additional \$150 million subject to CIO approval, and b) amending OIC policy 04-05-01 accordingly. Bob Deere, Investment Director with Dimensional Fund Advisors made the presentation.

OIC Policy 04-05-01 addresses the strategic role of Public Equities within OPERF. One objective of OIC Policy 04-05-01 is to achieve a portfolio return of 75 basis points or more above the MSCI All Country World Investable Market Index (ACWI IMI). In an effort to enhance return, one of the strategies specified in OIC policy is a strategic overweight to U.S. Small Cap targeted at 100 percent relative to the Russell 3000 Index (with an upward bound range of 140 percent). This overweight to U.S. Small Cap is supported by widely recognized academic studies which show that the smaller cap equities provide greater expected returns relative to larger cap equities.

Staff originally identified the need for Micro Cap Value (MCV) exposure in 2010. At that time, staff and SIS independently screened the pool of candidates to create a "shortlist," of potential managers based on a variety of qualitative and quantitative factors. MCV is a capacity constrained asset sub-class, and SIS and staff found that many favorable asset managers in this space were hard closed and no longer accepting additional assets. As a result, staff postponed bringing any recommendations for MCV to the OIC.

Although DFA manages over \$25 billion in U.S. Small and Micro Cap strategies, the absence of a Micro Cap Value track record in the eVestment Alliance database became evident when staff began evaluating the MCV space. Staff contacted DFA whose representatives confirmed that the firm did not have a Micro Cap Value product. Given the firm's history in investing Small Cap and Value stocks, staff asked DFA to consider creating a customized MCV mandate for OPERF. After internal research on their end, DFA responded affirmatively and enthusiastically and presented staff and SIS with a proposed MCV strategy

portfolio. Staff and SIS reviewed the proposed portfolio and worked collaboratively with DFA on minor structural changes so that the proposed MCV portfolio would better complement OPERF's existing Micro Cap Growth exposure.

Given the long relationship OIC has enjoyed with DFA and the multiple mandates OIC has funded with the firm, DFA proposed a management fee that is significantly less than the average active management fee in the MCV space. DFA also agreed to reserve an additional \$150 million of the firm's MCV capacity should staff (with CIO approval) decide to increase the OPERF allocation to this strategy.

There was a brief question and answer period following the presentation.

MOTION: Mr. Solomon moved approval of the staff recommendation. Treasurer Wheeler seconded the motion. The motion was passed by a vote of 5/0.

IV. 10:47 a.m.: OST/OIC Investment Beliefs Project: Introduction

Allan Emkin of PCA introduced the OST/OIC Investment Beliefs Project. He presented background for both the project in general as well as his firm's role in particular, and provided a timeline and projected list of project milestones.

The genesis for this project was the realization that a broader, more structured framework would be useful as we (staff, OIC members and consultants) assess our existing set of policies and procedures relative to new investment ideas and strategies. In addition, we thought this framework could help us develop a better, collective understanding of how such policies and procedures may be impacted by the organizational changes contemplated in SB120 as well as changes we should consider should some or all of that legislation become effective. The important work associated with the recently initiated asset/liability study also provides a timely and critical set of project inputs.

Mr. Skjervem agreed to work with the Board and PCA to set a feasible timeline for this project.

V. 11:07 a.m.: OIC Consultant Discussion and Recommendation

Staff proposed contract extensions for Strategic Investment Solutions and PCA (Emkin) through December 31, 2013, given both firms' current work in connection with the OPERS asset-liability study and OST/OIC Investment Beliefs project. A new general consultancy RFP process will be initiated by staff once the asset-liability study and Investment Beliefs project have been completed.

Staff also recommended an update to the real estate consultant search focusing on the firms previously selected as finalists in 2011 with the expectation that said search would be concluded for OIC action prior to June 30, 2013.

MOTION: Mr. Solomon moved approval of the staff recommendation. Treasurer Wheeler seconded the motion. The motion was passed by a vote of 5/0.

VI. 11:10 a.m.: OIC Investment Funds and Operational Review Report

Darren Bond, Deputy State Treasurer and Byron William, Sr. Internal Auditor made the presentation. Oregon Revised Statute 293.776 requires the OIC to audit the OST investment program at least once every four years. To satisfy this requirement, the OIC directed Internal Audit Services to perform an operational review of the investment division and its practices and compare the division and its practices to an appropriately-sized and selected institutional peer group.

Internal Audit Services completed a review of OST operations and OIC oversight for the year ended December 31, 2011. This audit was conducted in conformance with Generally Accepted Government Auditing Standards and the International Standards for the Professional Practice of Internal Auditing.

Those standards require that auditors plan and perform audits to obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions based on audit objectives.

The board thanked Byron and his staff for a well-executed audit.

VII. 11:20 a.m.: Annual Placement Agent Report

Mr. Skjervem reported that in accordance with OST Policy 5.03.01, Conflict of Interest and Code of Conduct, OST shall disclose at least annually all investment recommendations to the OIC in which a Placement Agent used by an investment firm had any contact with Treasury investment staff. Staff shall present to the OIC an annual summary of such contacts, which will also be made available to the public on the Treasury website.

Summary for Calendar Year 2012

<u>Partnership</u>	<u>OPERF Commitment</u>	<u>Placement Agent</u>
Reservoir Strategic Partners Fund, LP	\$50 million	Credit-Suisse Aqueduct Capital Group
RK Mine Finance Fund II, LP	\$75 million	Eaton Partners
Stonepeak Infrastructure Fund, LP	\$100 million	First Avenue Partners
GGV Capital IV, LP	\$50 million	UBS Private Funds Group
A&M Capital Partners, LP	\$100 million	Barclays

Mr. Skjervem noted further that placement agents are retained by funds' general partners, and OST staff does not rely on such agents for either access or analysis.

VIII. 11:23 a.m.: Asset Allocations and NAV Updates

Mr. Skjervem reviewed the Asset Allocations and NAV's for the period ending December 31, 2012.

IX. 11:26 a.m.: Calendar – Future Agenda Items

Mr. Skjervem highlighted future agenda topics.

X. 11:29 a.m.: Other Business

No other business was discussed.

11:45 a.m.: Public Comments

A number of people made public comments regarding the planned closing of a Sealy mattress plant in North Portland.

- Barbara Dudley of the Working Families Party read a letter from Representative and Speaker of the Oregon House Tina Kotek who represents North Portland District 44 where the Sealy mattress plant is located.
- Barbara Dudley went on to make her own comments about investment beliefs in general and the circumstances associated with the North Portland Sealy mattress plant in particular.

- Ron Rodgers, U.S. Steel workers staff representative, expressed concern for his local membership. He specifically discussed the concessions his members had made, and shared the frustration he and his constituents felt regarding the planned Sealy mattress plant closing.
- Bob Tackett, Executive Secretary/Treasurer of the Northwest Oregon Labor Council as well as President of Local 330 reiterated many of Mr. Rodgers's remarks and thanked those who had worked in support of his members' efforts.
- Tom Leedham, Secretary/Treasurer of Teamsters Local 206 since 1987, discussed the economic impact the plant's closure would have on the North Portland area.
- Darrin Willingham, North Portland Sealy mattress plant employee for the past 22 years, described how the plant's closure will personally affect his and other employees' families.
- Gene Blackburn, Teamsters warehouse representative, read a letter from Vincent Asero, a North Portland Sealy mattress plant employee who could not attend the meeting. The letter described how the plant closure would affect Mr. Asero's retirement plans.
- Rob Sisk, President of SEIU Local 503, requested that the OIC support Treasurer Wheeler's recent public request to initiate good faith negotiations among KKR, local Sealy management, labor, community, business and political leaders in an effort to find a solution that would keep the North Portland Sealy mattress plant open.
- Scott Reeves, a North Portland Sealy mattress plant employee for the past 29 years, expressed sentiments similar to those who had testified before him.
- Steve Hughes, Oregon Working Families Party representative delivered to the OIC a petition that had been signed by many members of his organization.

Mr. Larson summarized the issues addressed in the meeting's public comments section.

The meeting adjourned at 12:18 pm.

Respectfully submitted,

A handwritten signature in cursive script that reads "Julie Jackson".

Julie Jackson
Executive Support Specialist