

MINUTES OF THE INVESTMENT COMMITTEE OF THE  
BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM  
OF THE STATE OF HAWAII

AUGUST 22, 2022

CITY FINANCIAL TOWER  
201 MERCHANT STREET, SUITE 1200  
HONOLULU, HAWAII 96813

Committee Member	Dr. Catherine Chan, Chair
Trustees present:	Mr. Lance Mizumoto, Vice Chair
(via teleconference)	Dr. Genevieve Ley
	Mr. Emmit Kane
Visiting Trustees	Mr. Vincent Barfield
present:	
(via teleconference)	
Attorneys present:	Mr. Ivan Torigoe, Deputy Attorney General
(via teleconference)	
Staff present:	Mr. Thomas Williams, Executive Director
(City Financial Tower)	Ms. Kanoe Margol, Deputy Executive Director
	Mr. Howard Hodel, Acting Chief Investment Officer
	Mr. Anthony Goo, Acting Deputy Chief Investment Officer
	Mr. Aaron Au, Investment Officer – Illiquid Markets
	Mr. David Okamoto, Investment Officer – Credit
	Mr. Ian Wetzel, Investment Officer – Real Assets
	Mr. Andrew Chen, Investment Specialist
	Ms. Gerri Konishi, Member Home Loan Assistant
	Ms. Lori Kim, Secretary
	Ms. Kehau Kanae, Secretary
	Ms. Diana Gomes, Secretary
Guest present:	Mr. Colin Bebee, Meketa Investment Group, Inc.
(via teleconference)	Ms. Mika Malone, Meketa Investment Group, Inc.
	Mr. Chae Hong, Aon
	Ms. Natalie Fitch, Hamilton Lane Advisors, LLC
	Mr. Paul Yett, Hamilton Land Advisors, LLC
	Mr. Jens Foehrenbach, FRM
	Mr. Zachary Olsen, Parametric
	Mr. Daniel Ryan, Parametric
	Mr. Alex Zweber, Parametric
Public present:	Ms. Kim Huynh
(via teleconference)	Ms. Lindsay Saienni

CALL TO ORDER

A quorum being present (Chair Chan, Vice Chair Mizumoto, Trustees Kane and Ley), Chair Chan called the Investment Committee meeting to order at 9:00 a.m. and requested Board members to identify themselves and confirm that no other individuals are present in the room. Committee members present confirmed. Chair Chan read the following

statement, “Motion to hold the meeting allowing Trustees and members of the public to participate by interactive conference technology, pursuant to HRS § 92-3.7, with at least one meeting location open to the public that has audiovisual connection.” On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley and unanimously carried, the Investment Committee meeting continued.

## PUBLIC COMMENT PERIOD NEW BUSINESS

Chair Chan called for public comment. There was no public comment.

- REQUEST FOR PROPOSALS (RFP)  
FOR GENERAL CONSULTANT,  
PRIVATE EQUITY  
CONSULTANT AND REAL  
ASSET CONSULTANT

Executive Director Thomas Williams referred to the memo in the meeting packet and requested the Investment Committee to approve the RFP process and timeline being proposed for the Evaluation Committee. Three consultant contracts will expire in 2023; Private Equity in March with the General Consultant as well as Real Asset in June. Investment Staff and the Executive Director will be involved in five of the six phases listed and create a finalist list of two to three candidates for the Board’s consideration. The Board will interview the finalists, make a decision, and award the contract. The process is consistent with the past procurement done for these contracts.

On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley and unanimously carried, the Investment Committee approved the revisions to the ERS Investment Policy as presented.

## PRESENTATIONS

- FRM – DIVERSIFYING  
STRATEGIES ANNUAL REVIEW  
FOR PERIOD ENDING JUNE 30,  
2022

Mr. Jens Foehrenbach of FRM presented the Diversifying Strategies Annual Review. The following is a summary of the presentation:

- The portfolio performed positively during a volatile year.
- The Diversifying Strategies portfolio is comprised of two components:
  - Liquid Diversifying and Liquid Defensive.
  - Illiquid Diversifying.
- Liquid Diversifying Strategies net annual performance was 11.2% vs the benchmark of 2.83%.
- Systematic Trend Following (STF) was the largest contributor to performance, while Alternative Return Capture (ARC) and Defensive Return Capture (DRC) also contributed positively. Outperformance vs the benchmark was driven by Systematic Trend Following (STF) and Alternative Return Capture (ARC).
- ERS added \$1.27 billion of capital primarily to fund Alternative Return Capture (ARC), Defensive Return Capture (DRC), and Relative Value/Arbitrage (RV/A) components.
- Seven new accounts/strategies were added to the class during the year. No managers were fully redeemed.
- The Crisis Risk Committee convened once during the fiscal year.
- ERS Staff and FRM handled all nine guideline breaches satisfactorily within reasonable timescales.

Mr. Jens Foehrenbach of FRM gave the quarterly review. The following is a summary of the presentation:

Diversifying Strategies – Liquid Defensive & Liquid Diversifying:

- DS-LD 2<sup>nd</sup> Quarter net performance was 7.59% and gross performance was 8.14%.
- Crisis risk status turned amber in April and May.
- The DS-LD's exposures were long equities, short fixed income, long commodities, long U.S. dollar and long credit.
- Systematic Trend Following, Alternative Return Capture and Defensive Return Capture all experienced positive performance during the quarter.
- Total Liquid Diversifying and Defensive strategies NAV at quarter end was \$5.6 billion.

Diversifying Strategies – Illiquid Diversifying:

- Four capital calls were processed totaling \$117.3 million.
- As of the end of the quarter, total paid-in capital is \$923 million with a total commitment of \$1.2 billion.

Mr. Jens Foehrenbach concluded by stating that due to the complexity of the ERS Diversifying Strategies portfolio, 26 individuals within FRM work on it.

Mr. Colin Bebee of Meketa Investment Group gave the semi-annual review. The following is a summary of the presentation:

- MEKETA INVESTMENT GROUP, INC. – SEMI-ANNUAL REVIEW FOR PERIOD ENDING JUNE 30, 2022

- A large portion of ERS' investment assets rely upon continued economic growth and success.
- Crisis Risk Offset (CRO) was originally designed to help offset the most material market declines.
- Current Diversifying Strategic Class Components:
  - Liquid Defensive
  - Liquid Diversifying
  - Illiquid Diversifying
- In the past six months, Liquid Defensive increased by 5% and Liquid Diversifying and Illiquid Diversifying increased by 2% and 3%.
- In FY 2022, Diversifying Strategies grew from \$5.3 billion and 19 managers to \$6.5 billion and 27 managers.
- ERS staff have executed on the policy plan that was presented in January 2020 as a result of the 2019 Asset-Liability Study.
- The Diversifying Strategies has performed inline with expectations across all periods.
- ERS Staff have been transitioning the portfolio to the new Diversifying Strategies structure. The components of CRO still make up the majority of the Diversifying Strategies class, with other strategies being added to improve the resiliency of the class. Despite an increase of new managers and strategies, the original CRO concepts remain intact.

Mr. Colin Bebee of Meketa Investment Group gave the June 30, 2022 quarterly review of the entire ERS portfolio. The following is a summary of the presentation:

- MEKETA INVESTMENT GROUP, INC. – PERFORMANCE REPORT FOR PERIOD ENDING JUNE 30, 2022

- ERS' total portfolio generated a -1.6% quarterly return, a decrease of \$417 million in the Quarter, ending the period at \$22.0 billion.

- ERS' total portfolio outperformed the Policy Benchmark during the time period. Private Growth and Real Assets were overweight while Public Growth and Diversifying Strategies were underweight.
- In comparison to peers, ERS' total portfolio performance is in the top percentile for the quarter, year-to-date and 1-year trailing periods. The total portfolio performed in-line with expectations given the market environment.
- On a risk-adjusted basis, ERS' total portfolio outperformed the Median Public Fund by an even greater percentage across all time periods than the unadjusted outperformance.
- Impacts of high inflation will be important moving ahead, with volatility probably staying high.

Mr. Chae Hong of Aon gave the annual review. The following is a summary of the presentation:

- AON – REAL ASSETS ANNUAL REVIEW FOR PERIOD ENDING MARCH 31, 2022

- Recent infrastructure, agriculture and real estate commitments should help the portfolio continue toward its target allocation.
- The real estate portfolio is performing well overall by outperforming the NFI-ODCE Index on a net of fee basis.
- The real estate portfolio has generated an 8.7% net IRR and 1.5x net equity multiple since inception.
- The timber portfolio has generated an 8.1% net IRR and 2.6x net equity multiple since inception.
- The infrastructure portfolio has generated a 16.2% net IRR and 1.5x net equity multiple since inception.
- ERS portfolio has slightly under performed for the last quarter but outperformed since inception.
- New commitments were made during Q1 2022 and subsequent to quarter end:
  - \$220 million to a U.S. Diversified Real Estate Fund.
  - \$50 million U.S. Value-Add Fund.
  - \$50 million Asia Opportunistic Fund.
  - \$50 million U.S. Value-Add Fund.
  - \$50 million U.S. Opportunistic Fund.

Ms. Natalie Fitch and Mr. Paul Yett of Hamilton Lane presented the Private Equity Program Update. The following is a summary of the presentation:

- HAMILTON LANE ADVISORS, LLC – PRIVATE EQUITY QUARTERLY REVIEW FOR PERIOD ENDING MARCH 31, 2022

- Quarter 1 gain of \$63.8 million.
- ERS portfolio outperformed its public benchmark by 669 bps since inception.
- One year net IRR of 30.83% is outperforming the public benchmark by 2,409 bps.
- ERS portfolio sustained strong performance with a one-year IRR of 30.83%.
- PE allocation of 18.1% is above the 13.5% target as of 3/31/2022 but within the allocation range of 5.0 to 25.0%.
- Allocation is up 400 bps from 3/31/2021 and 57 bps from the prior quarter due to the strong performance driving the increase in PE allocation with quarterly net value changes >\$200 million in 2Q20 through 4Q21.

- ERS portfolio outperformed the public market benchmark (MSCI ACWI IMI +200 bps) for all periods.
- Contributions were down by 26% and distributions were down by 32%.
- Foundation managers continue to represent most of the portfolio value and outperformed the total portfolio by 374 bps.
- ERS closed on \$415 million across 11 investments and is on track to achieve the approved pacing plan of \$550-\$650 million by 2022-year end.

Mr. Zachary Olsen, Mr. Daniel Ryan and Mr. Alex Zweber of Parametric presented the Overlay Solutions Performance Review. The following is a summary of the presentation:

- PARAMETRIC – OVERLAY SOLUTIONS PERFORMANCE REVIEW FOR PERIOD ENDING JUNE 30, 2022

- Parametric assists institutional investors to essentially eliminate cash drag through a securitization overlay utilizing:
  - Established investment capabilities.
  - Transparency and repeatability.
  - Staff partnership.
- Cash provides liquidity for:
  - Benefit payments.
  - Capital calls.
  - Operating cash flow.
  - Funding obligations.
- Average cash exposure securitized was over 98% while maintaining zero portfolio leverage.
- The net overlay return of -\$57.3 million in FY 2022 reduced the net return to \$111.5 million since inception in May 2019.
- Portfolio tracking worked well in securitizing cash efficiently.
- During manager transitions, overlay bridged exposure gaps.
- Overlay exposures are used to securitize cash exposure into capital market exposure resulting in increased expected returns, reduced transaction costs, and increased liquidity.
- A tail risk event refers to a sharp selloff in the equity market.
- ERS is planning to add Parametric's Tail Risk Strategy the overlay; it
  - Utilizes an annual premium budget so the maximum hedge cost is a known and fixed amount.
  - Allocates half of the annual premium budget to each of the two sub-strategies.
  - Monetizes profits using a rules-based methodology.
  - Integrates seamlessly with the existing ERS overlay program.

- MEKETA INVESTMENT GROUP, INC. – 2022-2023 ASSET-LIABILITY STUDY

Mr. Colin Bebee of Meketa Investment Group presented the asset-liability study introduction. The following is a summary of the presentation:

- Last Asset-Liability Study was completed in 2019.
- Strategic Allocation is the foundation for long-term portfolio structure.
- Three steps to the Asset-Liability process:
  - 1) Determine how the financial condition of the ERS might vary based on outcomes of the ERS' investment portfolio.

- 2) Set a consensus definition and view of the risk the ERS should assume.
  - 3) Once the risk tolerance is established, select an appropriate long-term investment strategy.
- 2022-2023 Asset-Liability priorities:
    - Clarify sensitivities to various types of plan risks.
    - Examine 2022-2023 capital market assumptions.
    - Optimize the investment portfolios as part of a total system.
  - Modeling Principles:
    - Trustees' perspectives on risks and implementation.
    - Financial position of system must be considered.
    - Analyze and understand portfolios that are "near optimal."
    - Examine short-, medium- and long-term outcomes for the best decision-making process.
  - Timeline:
    - November 2022-Review Trustee Survey results.
    - February 2023-Asset class assumptions & defining key risks.
    - Spring 2023-Presentation of initial model output.
    - Spring/Summer 2023-Final model & target portfolio selection.

#### SUMMARY OF AUGUST 2022 INVESTMENT OFFICE ACTIVITIES:

- MARKET OVERVIEW
- CURRENT STATUS OF  
ACTIVITIES OF THE  
INVESTMENT OFFICE

Acting Chief Investment Officer Howard Hodel and Acting Deputy Chief Investment Officer Anthony Goo presented an update on the market. Acting DCIO Goo covered the market information for the year to date.

Acting DCIO Goo reported that inflation continued to climb during the May-July period and despite the low unemployment rate, recessionary fears abounded as the Federal Reserve raised the fed funds rate 75 bps in both June and July following a 50 bp increase in May. The fed funds rate-range is 2.25%-2.50%, with the market anticipating an increase to 3.25%-3.50% by year end. Volatility remained elevated across global equities and bonds as global growth concerns mounted alongside ongoing inflation risks. Global equities suffered a sharp 16% selloff during the second quarter, closing H1-2022 down 20%. In July, Global equities staged a recovery rally of 7% despite economic data continuing to deteriorate. Real US GDP declined for the second consecutive quarter, marking what is by some definitions a technical recession. The clearest catalyst for the rally in July was the decline in longer term interest rates. For the period, growth stocks outperformed value and US outperformed non-US markets.

Falling yields and spreads supported fixed income assets. High yield spreads declined sharply, supported by risk-on sentiment and elevated spreads. The yields on the 2-year and 10-year Treasury notes dropped 3 bps and 31 bps respectively and inverted by 22 bps during July as the market weighed the next rate move by the Federal Reserve in September.

#### Acting CIO Report

Acting CIO Hodel stated that the last couple of months was a very busy time for the Investment Office during this transition period.

Acting CIO Hodel reported that the team is looking at the portfolio's future. The U.S. economy and several other economies are teetering between recession and a soft landing which makes it difficult to determine where capital markets are going to end up. Three important groups - the very resilient consumer, the hawkish central banks around the world, and governments exercising expansionary fiscal and more protectionist trade policies, will drive capital markets. Currently, we are experiencing one of the worst productivity shocks in post-war history with a 40-year high in inflation and 50-year lows in unemployment.

The Federal Reserve and several other/Central Banks are in a rate hike cycle, and at the same time increasing money supply while government debt is rising. All three of these are going to weigh on productivity and future earnings for corporations. Globally we are seeing the end of three very positive long-term global growth and productivity factors – globalization, global peace, and the rapid expansion of the Indo-China economies. There are also numerous global macro risks including Europe's dependence on Russian energy, global supply chain issues, China's struggles with its zero Covid policy and deflating housing markets, among others that could threaten the near-term outlook for risk assets. Currently, the ERS portfolio is over allocated to growth risk, especially in private markets. Staff is allocating more capital to defensive and diversifying strategies to balance the risks in the portfolio and maintain the current exposure to higher quality equity and credit.

[End of CIO Report]

Acting DCIO Goo stated that an active manager reported three separate overdrafts during the May-July period. The overdrawn amounts were Euro Dollar 123.14 and Danish Krone 81.47. The overdrafts were due to negative interest being applied to credit balances and regulatory fees on failed trades. Overdraft amounts plus fees have been credited back to the account.

IO Okamoto reported that two new credit managers were approved by the Internal Executive Investment Committee (IEIC) in July and are in the process of on-boarding. Staff conducted on-site due diligence meetings with managers in early August.

IO Wetzel mentioned that commitment pacing is on track. CY 2022 pacing plan for total real assets commitments is a \$650 million target with total commitments of \$420 million have been approved for CY 2022. The CY 2023 strategic/pacing plan was approved at the July ERS Investment Summit for total real assets target of \$550 million.

IO Au reported that Hamilton Lane (HL) covered most of the information in their presentation. ERS has over \$1 billion in potential investment opportunities with high-conviction managers but is limited to invest within its previously approved range of \$550 to \$650 million. Staff and its consultant, Hamilton Lane, believe it is critical for ERS to establish new relationships and maintain existing relationships with such managers, or else risk losing our ability to invest in the next round of fundraising. Private Equity allocation was, therefore, increased to \$775

million from \$650 million. The commitment is still within the overall 25% allocation to Private Equity. Meketa supports the increase.

Acting CIO Howard Hodel reported the return of the \$6 billion Diversifying Strategies (“DS”) liquid portfolio was strongly positive during a risk-off environment with lower stock prices, higher interest rates, higher commodity prices, elevated volatility in virtually all markets, and the highest inflation levels in 40 years from May through July of 2022. The DS liquid portfolio’s annualized ex-ante volatility remained at about 7%, while ex-post volatility remained at about 8%.

Crisis Risk Indicators turned from green to amber for three business days at the end of April and beginning of May as the VIX and Dollar indicators exceeded their limits. On May 2, 2022, ERS staff transferred \$55 million of profits from Defensive managers to the Overlay account and to a Diversifying account to take advantage of market opportunities. A systematic rebalance was triggered in mid-June and as a result ERS staff transferred \$490 million of profits from trend, defensive and macro managers to fund other strategies and expenses, bringing the manager allocations back within their ranges.

Acting CIO Hodel continued that in Illiquid Diversifying, ERS added \$25 million of capital to Pillar Enso and \$10 million of capital to Nephila Ulu for June 1 and July 1 subscriptions, respectively, to complete full funding of the two strategies.

In addition, the cash securitization overlay has been running since late May 2019 and has produced positive results to date; cash securitization averaging between \$400-\$700 million.

Acting CIO Hodel reported that in May-August, the Internal Executive Investment Committee (IEIC) approved staff recommendation for:

- up to \$220 million for a multi-strategy manager in Liquid Diversifying-Relative Value/Arbitrage in July.
- an \$80 million allocation increase to an Illiquid Diversifying–Idiosyncratic Return Capture manager in June.
- up to \$50 million in a Real Assets–Non-Core Core Real Estate (Value-Add) fund in June.
- up to \$50 million in a Real Assets–Non-Core Core Real Estate (Opportunistic) fund in June.
- a \$150 million commitment and a \$200 million commitment in the Global Credit portfolio in July.
- a \$35 million commitment and a \$200 million commitment in the Private Growth portfolio in June and July, respectively.
- a \$1 million/year premium spend budget for a hedging strategy in the Overlay in July.

IS Chen reported that the VIX averaged 25% (closing between 21.3% and 27.5%) for the month. The current level is above the average level of 20.1% over the past five years. Daily tracking of the ERS portfolio performance during July indicated an annualized volatility of 3.5% well below the average annualized volatility of 9.5% over the past three



years. Staff is continuing to monitor potential, significant macro risks in each of the three major economic regions of the world, any of which could trigger another market correction.

Staff continues to provide records/documents requested via Uniform Information Practices Act (“UIPA”) with the assistance of the Attorney General’s office.

Investment Specialist Chen continued with the 2nd Quarter 2022 Risk Report. The following is a summary of the presentation:

- Growth risk dominates, ERS realized risk is muted, active risk and other risks remain high.
- ERS portfolio is tilted toward the U.S. dollar and U.S. equity markets.
- International growth-oriented assets are tilted toward developed markets (10.3%).
- Portfolio risk levels are appropriate and consistent with policy & market conditions.
- Diversifying Strategies (DS) class dampened portfolio volatility from 20.8% to 8.4% during the quarter.
- Growth risk accounted for 85.6% of the projected portfolio risk.
- Portfolio beta to MSCI ACWI IMI is approximately 0.4.
- Sharpe Ratio, Information Ratio and annual excess returns over the rolling 1-year were 1.95, 1.06, and 2.39% respectively.
- Equity volatility, as measured by the VIX, averaged 27.4% for the quarter, well above the 5-year historical average of 19.9%.

ENTER EXECUTIVE SESSION

EXECUTIVE SESSION

EXECUTIVE SESSION, PURSUANT TO HRS § 88-27.5(A)(1), AND HRS § 92-5(A)(4), TO CONDUCT DISCUSSIONS AND DELIBERATIONS RELATING TO, AND IF APPROPRIATE, TO MAKE A DECISION ON INVESTMENTS OR PROSPECTIVE INVESTMENTS BY THE SYSTEM THAT REQUIRE THE CONSIDERATION OF INFORMATION OR RECORDS THAT ARE EXEMPT FROM DISCLOSURE UNDER HRS CHAPTER 92F, INCLUDING INFORMATION AND RECORDS THAT ARE PROPRIETARY INFORMATION OR CONFIDENTIAL BUSINESS INFORMATION, AND TO CONSULT WITH THE BOARD’S ATTORNEYS ON QUESTIONS AND ISSUES PERTAINING TO THE BOARD’S POWERS, DUTIES, PRIVILEGES, IMMUNITIES, AND LIABILITIES

[Before entering Executive Session, Chair Chan read the names of all authorized participants. All unauthorized participants were asked to leave the meeting.]

On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley, and unanimously carried, the Investment Committee entered Executive Session at 11:58 a.m.

[At the beginning of Executive Session, Chair Chan asked each participant individually to confirm no unauthorized person is present or able to hear them at their remote locations or via another audio or audiovisual connection. All responded they were by themselves.]

WITH RESPECT TO UPDATES ON  
STATUS OR ISSUES RELATED TO  
CONFIDENTIAL ERS INVESTMENT  
PORTFOLIO UPDATES REGARDING  
CHANGES IN (1) ORGANIZATIONAL  
CHANGE FOR DIVERSIFYING  
STRATEGIES MANAGERS, (2)  
MANAGER PIPELINES FOR EACH  
STRATEGIC CLASS.

APPROVAL OF EXECUTIVE  
SESSION MINUTES – MAY 25, 2022

On a motion made by Trustee Ley, seconded by Vice Chair Mizumoto, and unanimously carried, the Investment Committee approved the Executive Session minutes of May 25, 2022 meeting as presented.

EXIT EXECUTIVE SESSION

On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley, and unanimously carried, the Investment Committee exited Executive Session at 12:14 p.m.

APPROVAL OF MINUTES – MAY 25,  
2022

On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley and unanimously carried, the Investment Committee approved the minutes of the May 25, 2022 meeting as presented.

ADJOURNMENT

On a motion made by Vice Chair Mizumoto, seconded by Trustee Ley, and unanimously carried, Chair Chan adjourned the meeting at 12:15 p.m.

**REDACTED  
SIGNATURE**

Howard Hodel  
Acting Chief Investment Officer  
HH/dlg