

SC House Executive Subcommittee of the Legislative Oversight Committee

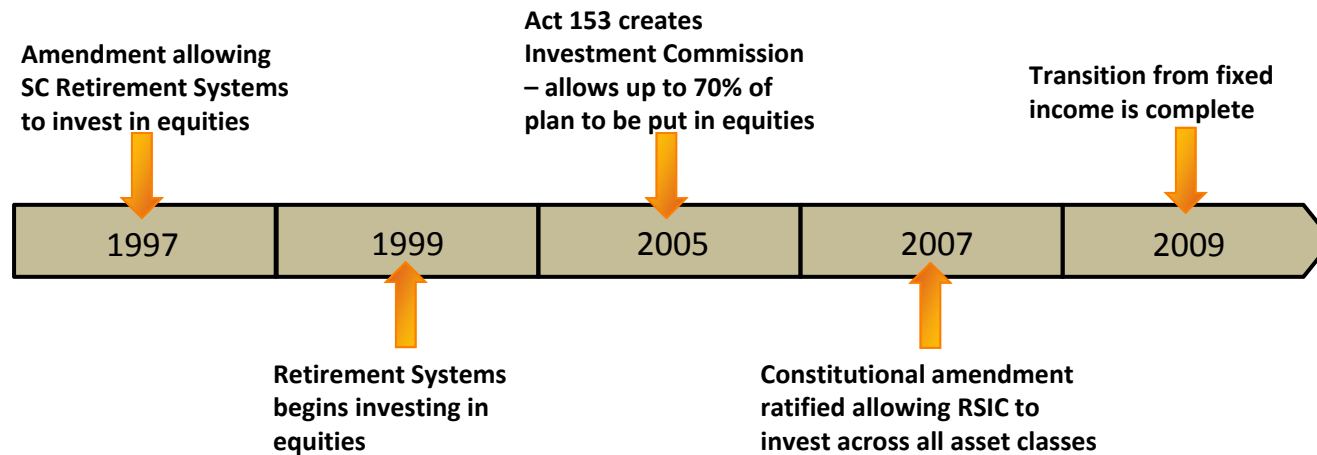
Michael Hitchcock, Chief Executive Officer
Geoff Berg, Acting Chief Investment Officer
July 12, 2016

Investment Background

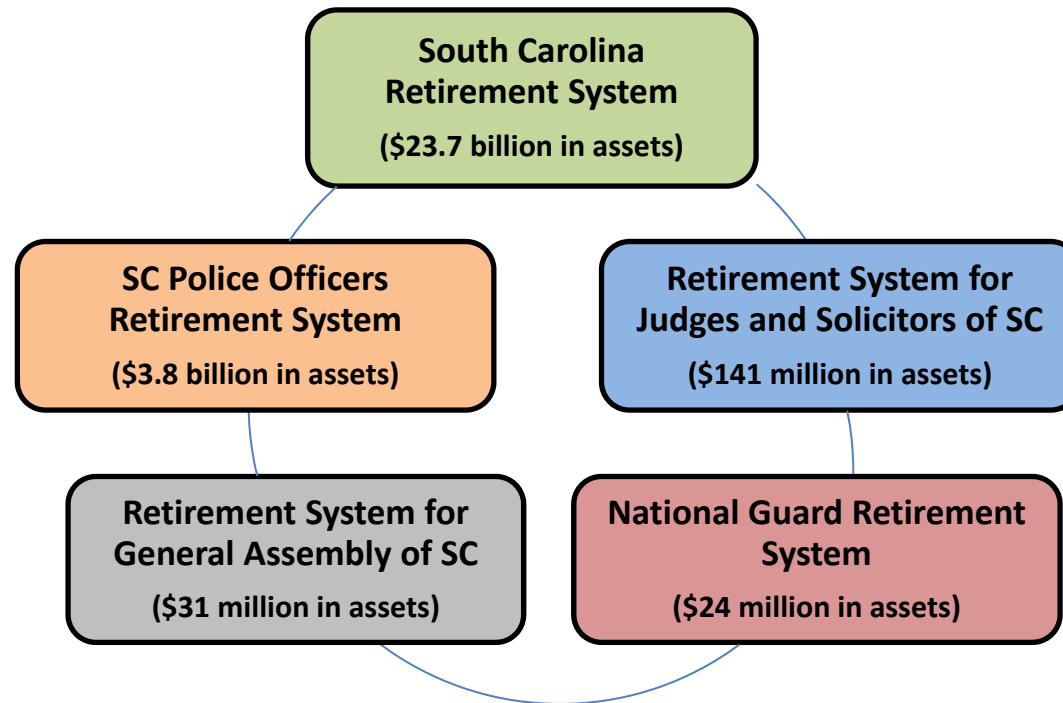
- Although the Retirement Systems Investment Portfolio existed since 1945, the assets of the Retirement System were historically invested in domestic fixed income investments only until 1997.
- The Investment Panel was created in the late 90's to advise the Budget and Control Board on the domestic equity portfolio, which was limited to 40%.
- Effective October 1, 2005, the State Retirement System Preservation and Investment Reform Act established the Investment Commission.



History up to Commission



Purpose & Duties



- The assets of the five defined-benefit plans are held collectively in a group trust referred to as the “South Carolina Retirement Systems Group Trust” or “Systems”.
- RSIC is responsible for investing and managing assets held in trust for the five systems.
- As of March 2016, Systems totaled approximately \$27.7 billion in assets.



Who Do We Work For?

OVER 500,000

Plan Participants and Beneficiaries

About 1 in every 9 South Carolinians



Why do We Exist?

We exist to help provide a secure future for our beneficiaries.

*“Beneficiaries First:
Their Future. Our Mission.”*



The Commission

The RSIC is a seven member commission:

- **Rebecca Gunnlaugsson, PhD**, Chair (Appointed by: Comptroller General Richard Eckstrom)
- **Ron Wilder, PhD**, Vice Chair (Retiree Representative to the Commission)
- **Reynolds Williams, J.D., CFP** (Appointed by: Senate Finance Committee Chairman, Hugh Leatherman)
- **Peggy Boykin, CPA** (Ex-Officio as PEBA Executive Director)
- **Allen R. Gillespie, CFA** (Appointed by: Ways and Means Committee Chairman Brian White)
- **Edward N. Giobbe, MBA** (Appointed by: Governor Nikki Haley)
- **Curtis M. Loftis, Jr.** (State Treasurer)



RSIC Staff Qualifications

RSIC staff and Commission includes:

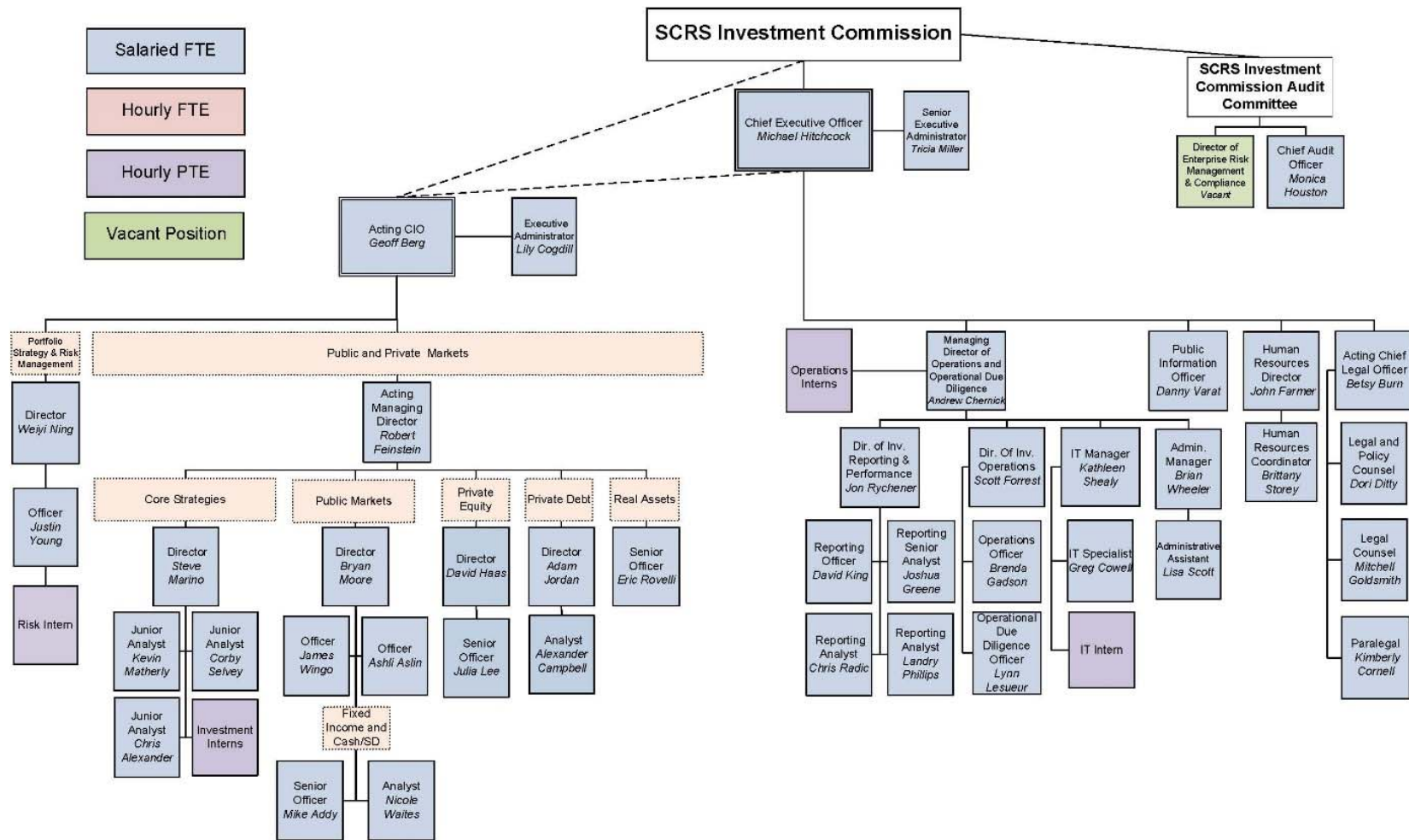
- Seven Juris Doctors
- Three Certified Public Accountants
- Nine Chartered Financial Analysts
- Nineteen Masters Degrees
- Three PhDs
- Five Chartered Alternative Investment Analysts
- Three Claritas Investment Certification

Chartered Financial Analyst (CFA) is a professional credential that measures the competence and integrity of financial analysts.

- Required to pass 3 exams.
- A minimum of 4 years of investment/financial experience and a bachelor's degree.
- One of the most respected designations in finance and considered the gold standard in the field of investment analysis.



RSIC Organizational Chart



Aon Hewitt Background – Consultant

- Aon is RSIC's investment consulting firm.
- Aon is a fiduciary.
- Aon has \$4.3 trillion in assets under advisement worldwide.
- Aon has over thirty years of experience working with public funds.

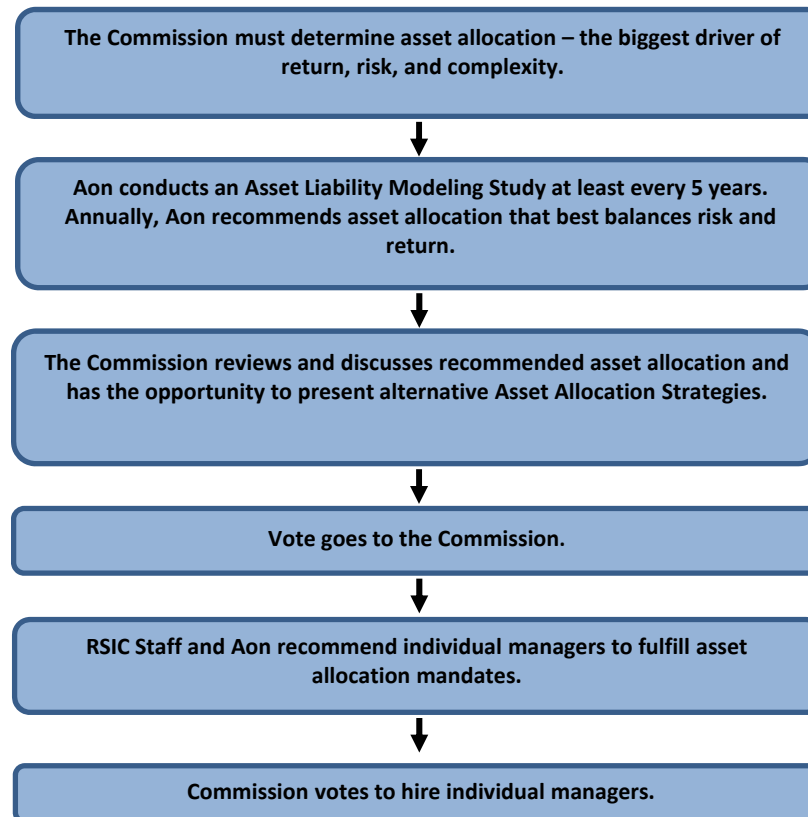
What Can We Invest In?

Includes, but not limited to, the following:

- (1) bonds of this State, other states of the United States, the United States, or any political subdivisions or agencies thereof;
- (2) banks and savings and loan institutions;
- (3) top-rated commercial paper;
- (4) funds of funds;
- (5) foreign certificates of deposit;
- (6) short-term debt;
- (7) investment trust securities;
- (8) real estate securities;
- (9) foreign fixed-income obligations;
- (10) futures and options regulated by the United States Securities and Exchange Commission;
- (11) private equity;
- (12) domestic and foreign group trusts;
- (13) investment vehicles of Federal Deposit Insurance Corporation approved institutions;
- (14) bonds of foreign countries designated industrialized by the International Monetary Fund;
- (15) collateralized mortgage obligations;
- (16) World Bank bonds;
- (17) debt of the United States or Canadian corporations;
- (18) equipment trust debt;
- (19)(a) purchase money mortgages received for real estate;
 - (b) real property;
 - (c) exchange traded funds;
 - (d) American Depository Receipts;
- (20) real estate investment trusts; and
- (21) investments allowed pursuant to Section 11-9-660 and equity investments as allowed pursuant to Section 16, Article X of the Constitution of this State.



Asset Allocation Process



Asset Allocation

Equity	47%
Conservative Fixed Income	12%
Diversified Credit	18%
Opportunistic	12%
Real Assets	11%

Section 9-16-335 Assumed Rate of Return

Effective July 1, 2012, the assumed annual rate of return on retirement system investments is:

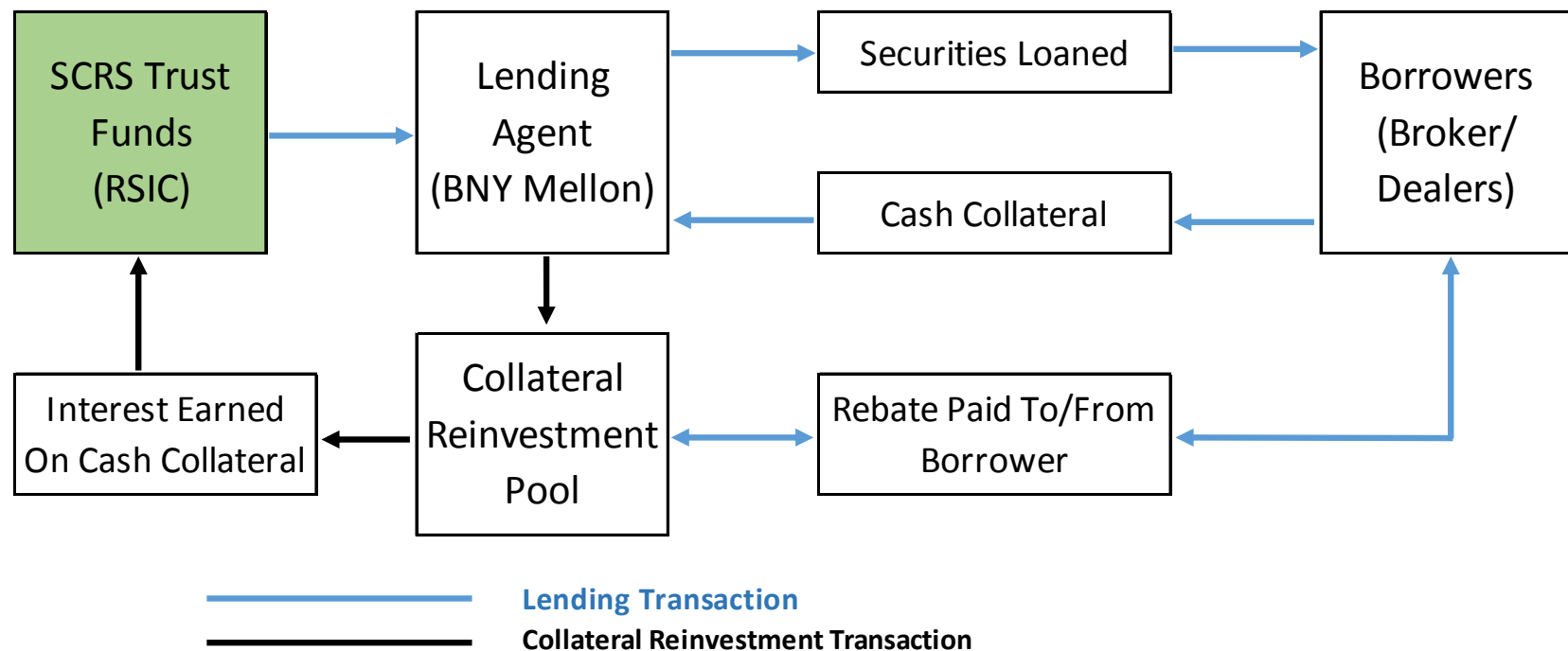
7.5%



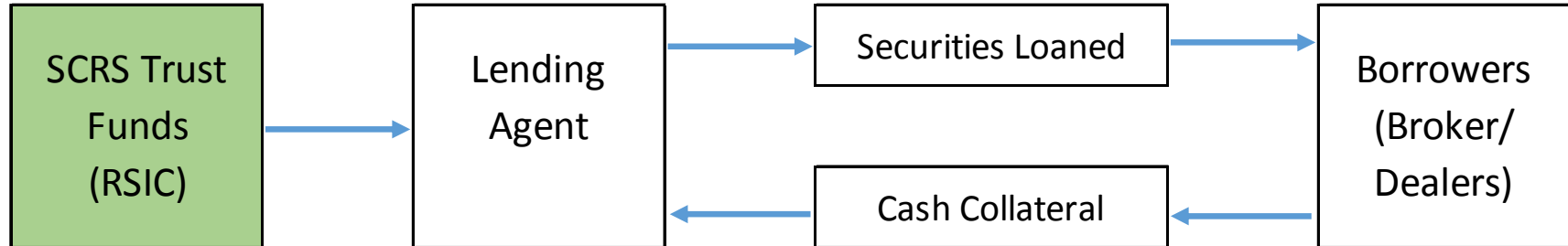
Understanding Securities Lending



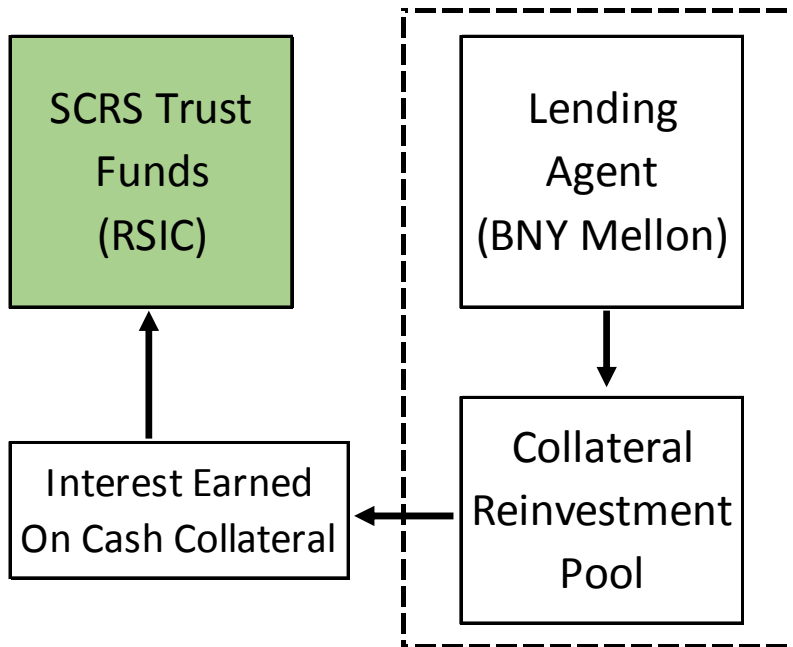
Securities Lending



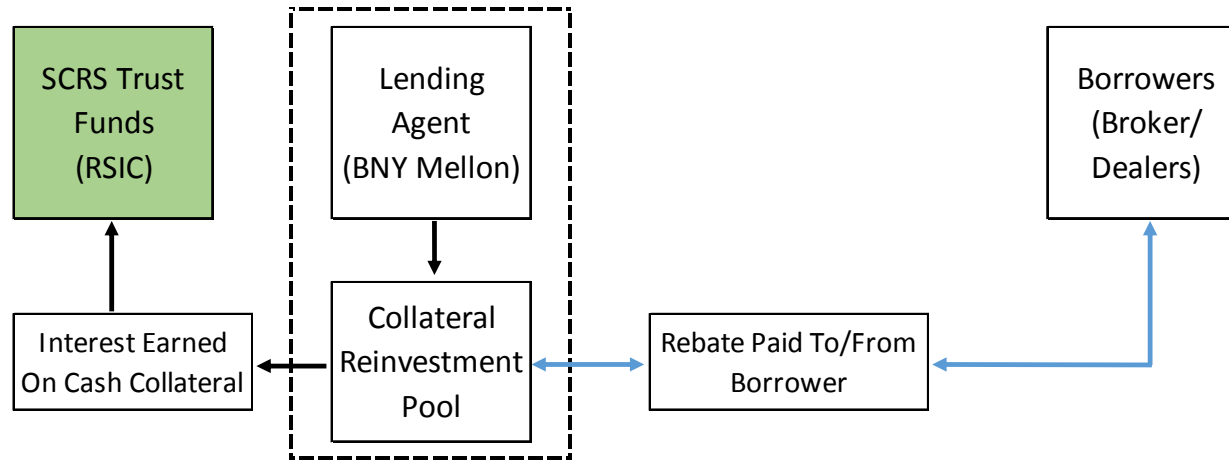
The Lending Transaction



Collateral Reinvestment Transaction



Collateral Reinvestment Transaction



Securities Lending Risks

Risk	Description
Borrower Risk	Borrower becomes insolvent and is unable to return securities to the lender
Collateral Risk	Value of collateral falls below the replacement cost of the lent securities
Intraday Settlement Risk	Securities being lent are delivered to the borrower before collateral is received
Operational Risk	Late recall of securities, failure to claim dividends, etc.
Legal Risk	Lender's legal agreement does not provide full protection against borrower default or for Cash Collateral Risk
Cash Collateral Risk	Lender suffers loss on the re-investment of the cash collateral

Source: International Securities Lending Association (www.isla.co.uk)

Key Events

- Lending Agent invested in Lehman Brothers and asset-backed securities (backed by mortgages), resulting in losses
 - FYE 2009 CAFR showed losses of \$223 million (*unrealized*)
 - Actual realized losses totaled \$165 million (September 2012)
- RSIC funded \$75 million loss in order to remove the asset-backed securities from the collateral reinvestment pool (“CRP”)
- The STO filed suit against the Lending Agent (2011)
- The STO settlement included a cash payment of \$20 million for the Trust fund (May 2013)

Removal of ABS Securities From CRP

- Asset-backed securities removed from the pool
 - RSIC hired external firm to manage these distressed securities
 - Removing securities from the CRP required funding the losses attributed to these securities (\$75 million)
 - As of 2013 analysis, outcome had improved \$28 million vs. taking no action

Conclusion

Questions?





BENEFICIARIES FIRST:
THEIR FUTURE, OUR MISSION.

