



NEW MEXICO STATE INVESTMENT COUNCIL



INVESTMENTS & PENSIONS OVERSIGHT COMMITTEE

ALTERNATIVE INVESTMENTS COSTS & BENEFITS

REPRESENTATIVE JIM TRUJILLO, CHAIR
SEPTEMBER 9, 2014

STATE INVESTMENT OFFICER STEVE MOISE
DEPUTY SIO VINCE SMITH



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SIC Overview



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- **Total assets under management:**
 - Record high close for fiscal year: **\$19,814,031,173**
 - FY 14 total assets investment returns: **15.9%**
- **Fund distributions for FY15:**
 - LGPF: \$596.0 million
 - STPF: \$182.7 million
 - Total: \$778.7 million
- **Projected FY16 total distributions: \$845 million**
- **Fund growth = greater benefits**



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Alternative Assets: Introduction



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- **Traditional 60/40 portfolio vs. modern asset allocation**
 - Diversification benefits
 - Reduction in volatility
- **Public vs. Private assets**
 - Valuations
 - Costs (fees)
 - Passive vs. active management
- **Pension vs. endowment models**
 - Endowments capitalize on liquidity premium
 - Pension liabilities & related allocation restrictions



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Types of Alternative Assets



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- **Private equity**
 - Buyout, distressed, growth equity, venture capital
- **Real estate**
 - Core, tactical, opportunistic; open/closed funds, joint ventures
- **Hedge funds (absolute return)**
 - Fund of funds; long-short & other equity-based strategies
- **Opportunistic credit**
 - Distressed debt strategies
- **Real assets**
 - Timber, infrastructure, farmland, energy



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Asset Allocation



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Land Grant Permanent Fund Asset Allocation

- Shifting away from equity risk
- Focus on income-producing strategies

Investment Strategy	Current	New	Difference
Domestic Equity	31%	28%	-300 bps
Foreign Equity	15%	13%	-200 bps
Fixed Income	16%	18%	200 bps
Absolute Return	8%	7%	-100 bps
Real Estate	10%	10%	0 bps
Real Return	10%	12%	200 bps
Private Equity	10%	12%	200 bps
NM Private Equity	0%	0%	0 bps

Severance Tax Permanent Fund Asset Allocation

- 2007: equity-like risk 85% of portfolio
- Today: approximately 53%

Investment Strategy	Current	Proposed	Difference
Domestic Equity	31%	22%	-900 bps
Foreign Equity	15%	18%	300 bps
Fixed Income	16%	18%	200 bps
Absolute Return	8%	7%	-100 bps
Real Estate	10%	10%	0 bps
Real Return	10%	12%	200 bps
Private Equity	10%	8%	-200 bps
NM Private Equity	5%	5%	0 bps



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Alternative Portfolio: Yale

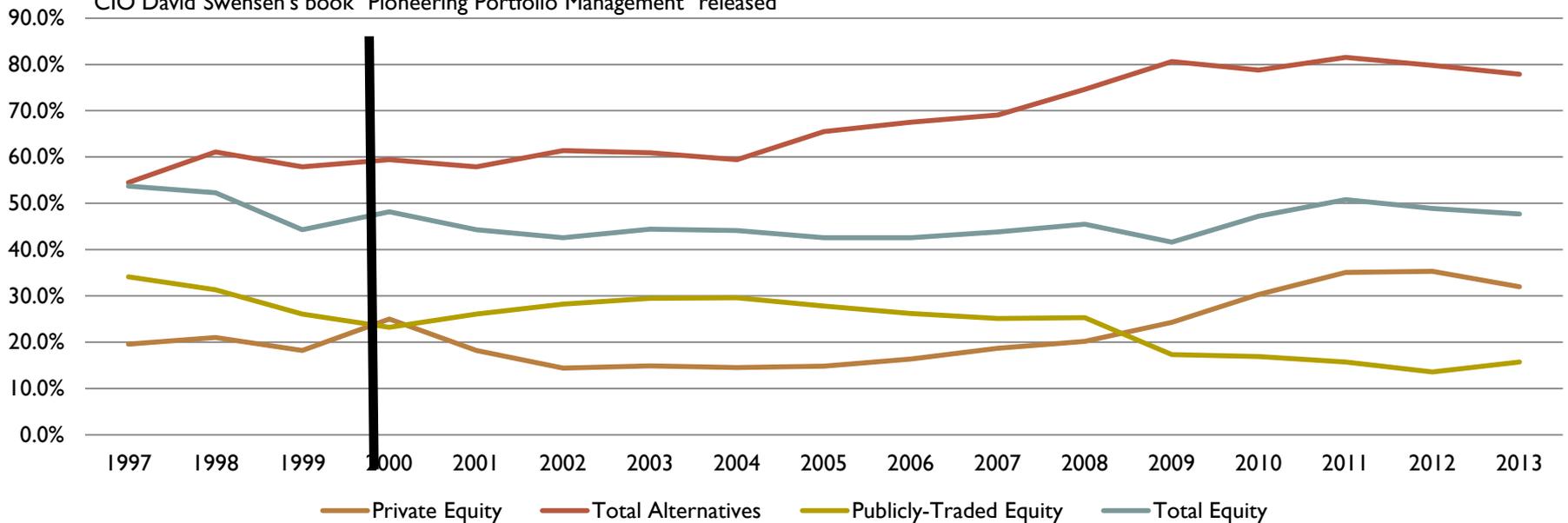


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- Up to 80% alternative assets
- Consistent total equity exposure near 50%

Yale University Endowment Asset Allocation

CIO David Swensen's book "Pioneering Portfolio Management" released





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Costs & Benefits



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Calendar Year 2013 SIC Direct Costs

- Includes passive/index managers combined
- Active management more expensive
- Average: 0.22%

Investment Strategy	Annual Cost (basis points)
Domestic Equity	24
International Equity	20
Fixed Income	20

Calendar Year 2013 SIC Embedded Costs

- Fees vary by strategy
- Passive management not an option
- Expectation \$2 or \$3 in excess returns for each \$1 paid in fees
- Average: 1.12%

Investment Strategy	Annual Cost (basis points)
Private Equity	90
Real Estate	81
Real Return	89
Hedge Funds	203
Credit/Structured debt	141



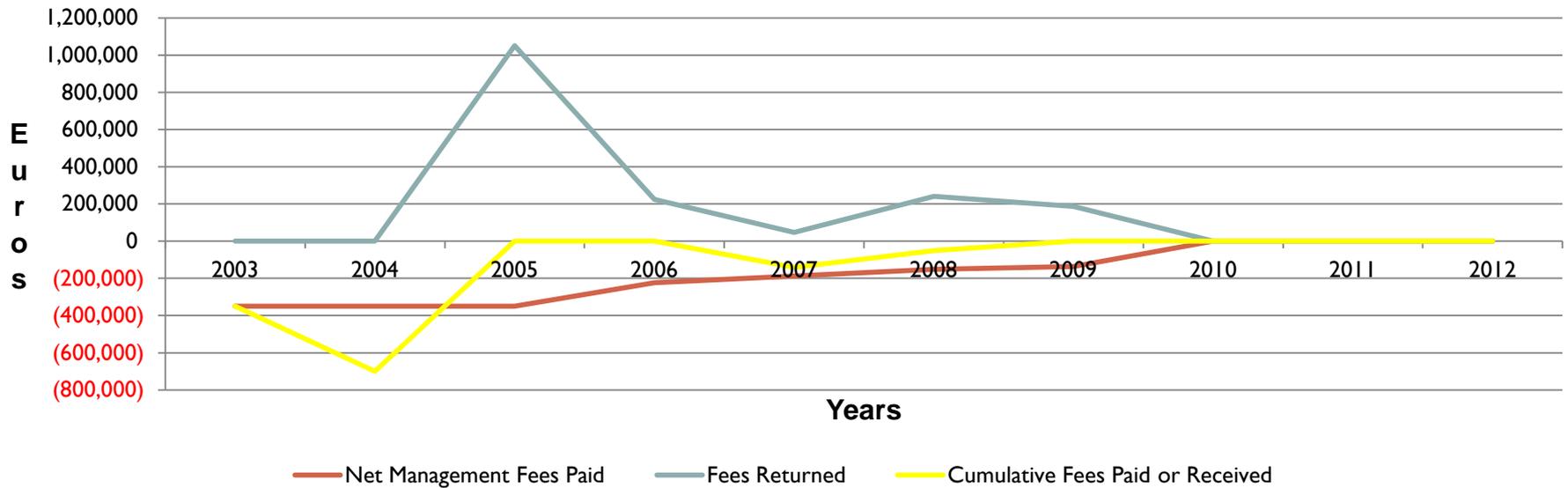
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Private Equity Fees



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- Case study: Nordic Capital Fund V return waterfall:
 - Manager pays back SIC:
 - ✦ Capital invested, fees & expenses, 8% preferred return, then 80/20 split





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Severance Tax Fund Returns



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- **Impact of Economically Targeted Investments on returns**
 - LFC: up to 1% opportunity cost/year (\$40 million)
 - Today, less impact, fewer ETIs deployed, change of focus
 - ✦ No new film loans since 2008
 - ✦ SBIC: no new venture investments, no additional losses
 - ✦ NM Private Equity Program: seeking market rates of return





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Closing thoughts



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- **Alternative investments**
 - A powerful tool in the Council's duty to construct a diversified portfolio
 - Fees negotiated to market rates or lower
 - Costs overseen by the Council
 - Asset allocation study completed by SIC staff & advisors, updated every three years, reviewed often
- **ETIs**
 - Council taking a very conservative approach
 - Focus today is on making investments in NM, "assuming all else is equal"