S·U·R·S

STATE UNIVERSITIES RETIREMENT SYSTEM

September 2020

Fiscal Year 2021
Investment Plan

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S·U·R·S
STATE UNIVERSITIES RETIREMENT SYSTEM

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Investment Department

August 28, 2020

Board of Trustees
State Universities Retirement System
1901 Fox Drive
Champaign, IL 61820

RE: ***Fiscal Year 2021 Investment Plan***

Dear Board of Trustees:

The Investment Staff is pleased to provide the SURS Investment Plan for Fiscal Year 2021. This document was developed in order to formalize the strategic plans for the investment portfolio for the coming year and provide transparency of the planning process. The Investment Plan for Fiscal Year 2021 marks the tenth year of the formal plan for the SURS investment program.

The Investment Plan reviews the results of Fiscal Year 2020 and defines the strategy for Fiscal Year 2021 in accordance with the Board-approved asset-liability study and Investment Policy. Since financial markets are dynamic, revisions to the plan may be required and will be communicated to the Board in a timely manner.

The SURS portfolio returned 2.64% during Fiscal Year 2020, net of fees, exceeding the policy portfolio return of 2.00%. The Total Fund's outperformance relative to the policy portfolio for Fiscal 2020 was due to a number of factors, including:

- Strong relative performance by the aggregate global equity portfolio;
- Strong absolute and relative performance by the Inflation Sensitive class due to a legacy commodities allocation;
- Strong relative performance by the option strategies sub-class of the Stabilized Growth portfolio; and
- Outperformance by the newly implemented Crisis Risk Offset class, which was funded during the fiscal year.

The positive relative performance was especially noteworthy, given the significant restructuring in nearly every class during the fiscal year.

From a long-term perspective, the SURS portfolio has performed well, earning an 7.9% annualized rate of return over the past 30 years, exceeding the 7.6% policy portfolio return. This return is also in line with the 8.0% average assumed rate of return in effect over the last 30 years and the current 6.75% assumed rate of return.

When compared to a universe of other large public funds, the SURS return ranks in the top quartile for the one-, three- and ten-year periods and the second quartile for the five-year period. Asset allocation is the primary determinant of a fund's ranking in a peer universe.

As of June 30, 2020, the defined benefit plan is valued at approximately $19.4 billion while the Self-Managed Plan (SMP) is valued at approximately $3.0 billion (including forfeiture and disability reserve assets).

Much of the activity completed during Fiscal Year 2020 was tied to implementation of the new functional-based portfolio structure approved in September 2018. The new portfolio structure is designed to produce improvement in long-term expected returns with significantly improved volatility and downside risk measures, with a much tighter range of projected return paths. Key projects completed include the following:

- Continued implementation of Non-Traditional Growth allocations;
- Restructuring of Traditional Growth portfolio, including completion of a search for global equity managers;
- Creation and structuring of Stabilized Growth portfolio, including creation of a credit portfolio, initiation of a private credit specialty consultant/advisor search, and continued commitment to the core real assets portfolio;
- Selection of two firms to replace SURS' manager of emerging managers partner, who closed its doors during FY 2020;
- Restructuring of Inflation Sensitive class, eliminating the commodities allocation and shifting to 100% TIPS;
- Restructuring of the Principal Protection class;
- Completion of searches and implementation of mandates in the Crisis Risk Offset class;
- Completion of searches for recordkeeper and custom investment solution providers for the SMP/Retirement Savings Plan and the new supplemental deferred compensation plan; and
- Education on a number of topics relevant to the investment portfolio, including, but not limited to, defined contribution plan considerations, private equity portfolio construction and asset allocation.

Numerous projects are planned for Fiscal Year 2021, including, but not limited to, the following:

- Initiation of an asset allocation study;
- Completion of the private debt specialty consultant / advisor search;
- Continued implementation of Non-Traditional Growth allocations;
- Continued review of opportunities to include firms owned by minorities, females and persons with a disability in the investment program;
- Launch of redesigned SURS Retirement Savings Plan and supplemental deferred compensation plan.

The Manager Diversity Program (MDP), which focuses on investment management firms owned by minorities, females, and persons with a disability (MFDB), continues to be a high priority. As of June 30, 2020, the MDP is valued at approximately $4.1 billion. In total, assets under management with MFDB firms are approximately $7.2 billion or 36.7% of the Total Fund. SURS recently hosted its second annual Diverse Manager Week. Investment managers in strategies across the portfolio were invited to present to staff, the corresponding consultant (either general or specialty), and our manager of emerging manager partners. In total, 30 diverse owned firms participated in meetings during that week.

The Investment Plan for Fiscal Year 2021 contains additional details on Fiscal Year 2020 accomplishments and strategic initiatives for Fiscal Year 2021. The investment team is focused on successfully completing the projects planned and prudently positioning the portfolio for the future. A long-term focus is of utmost importance. I look forward to discussing the ***Fiscal Year 2021 Investment Plan*** at future meetings.

Sincerely,

Douglas C. Wesley

Douglas C. Wesley, CFA
Chief Investment Officer

cc: Martin Noven, Executive Director

FY 2021 Investment Plan
Table of Contents

Page

I. Purpose

The Investment Plan reviews the results of Fiscal Year 2020 and defines the strategy for Fiscal Year 2021 in accordance with the Board-approved asset-liability study and Investment Policy[1]. **This Plan is intended to be a living document. Since financial markets are dynamic, revisions to the plan may be required during the year. In the event of changing circumstances or opportunities during the year, items will be discussed with the Board as necessary.**

II. Overview

Background

The State Universities Retirement System (SURS) is the administrator of a cost-sharing, multiple employer public employee retirement system. SURS membership includes employees of the public universities and other affiliated organizations. Currently, SURS membership totals more than 230,000 active, inactive and retired participants. SURS maintains both a defined benefit and a defined contribution plan, known as the SURS Self-Managed Plan (SMP). As of June 30, 2020, the defined benefit plan is valued at approximately $19.4 billion while the SMP is valued at approximately $3.0 billion (including forfeiture and disability reserve assets). The investment portfolio is broadly diversified across several functional classes.

Fiscal Year 2020 Performance Review

Favorable economic conditions continued during the first seven months of Fiscal Year 2020, until the global pandemic brought the economy to a near halt. Financial markets plummeted in response during the month of March but quickly rebounded in the 2Q 2020 quarter. Economic volatility remains heightened, however. The SURS investment portfolio returned 2.64%, net of fees, during Fiscal Year 2020, exceeding the policy portfolio return of 2.00% by 64 basis points. The table below illustrates the performance of the overall SURS investment portfolio relative to the policy portfolio, as of June 30, 2020.

Investment Performance*
As of June 30, 2020

	1 Year	3 Years	5 Years	10 Years	20 Years	25 Years	30 Years
SURS	2.6%	5.6%	5.8%	8.5%	5.6%	7.7%	7.9%
Policy Portfolio	2.0%	5.5%	5.8%	8.5%	5.6%	7.5%	7.6%

*Net of investment management fees

The Total Fund's outperformance relative to the policy portfolio for Fiscal 2020 was due to a number of factors, including:

[1] The SURS Investment Policies can be found at http://surs.org/investment-policies.

- Strong relative performance by the aggregate global equity portfolio. Worthy of mention is the outstanding performance by T.Rowe Price during the year (+22.76% vs. 2.11% benchmark return);
- Strong absolute and relative performance by the Inflation Sensitive class due to a legacy commodities allocation. This portfolio segment is currently comprised of a passive TIPS portfolio.
- Strong relative performance by the option strategies sub-class of the Stabilized Growth portfolio.
- Outperformance by the newly implemented Crisis Risk Offset class, which was funded during the fiscal year.

The positive relative performance was especially noteworthy, given the significant restructuring in nearly every class during the fiscal year.

At the aggregate level, the Traditional Growth, Non-Traditional Growth, Inflation Sensitive and Crisis Risk Offset portfolios exceeded their performance benchmarks for the year ending June 30, 2020. The Stabilized Growth and Principal Protection classes slightly lagged their benchmarks for the period.

Of the private, illiquid asset classes, the non-core infrastructure portfolio provided the strongest absolute return, +7.8%. The private equity asset class provided the strongest relative return, exceeding the benchmark for the one-year period by 917 basis points.

Performance of each of the broad asset classes during FY 2020 is shown in the table that follows.

SURS FY 2020 Asset Class Returns
(Net of Fees)

Asset Class	FY 2020 Return
Broad Growth	
Traditional Growth	
US Equity	4.15%
Dow Jones US Total Stock Market	6.41%
Excess	-2.26%
Non-US Equity	-5.05%
MSCI ACWI Ex-US	-4.82%
Excess	-0.23%
Global Equity	8.45%
MSCI ACWI	1.33%
Excess	7.12%
Stabilized Growth	
Option Strategies	1.32%
Performance Benchmark	-6.24%
Excess	7.56%
Stabilized Real Assets*	1.22%
NCREIF ODCE	3.93%
Excess	-2.71%
Credit Fixed Income**	-0.81%
Performance Benchmark	0.10%
Excess	-0.91%

Asset Class	FY 2020 Return
Non-Traditional Growth*	
Non-Core Real Estate	-0.62%
NCREIF ODCE + 1.5%	5.48%
Excess	-6.10%
Non-Core Infrastructure	7.84%
CPI-U + 5.0%	6.61%
Excess	1.23%
Private Equity	0.59%
ACWI IMI + 2% / Blend	-8.58%
Excess	9.17%
Inflation Sensitive	7.39%
Performance Benchmark	6.83%
Excess	0.56%
Principal Protection	6.46%
Performance Benchmark	7.46%
Excess	-1.00%
Crisis Risk Offset**	3.07%
Performance Benchmark	2.98%
Excess	0.09%

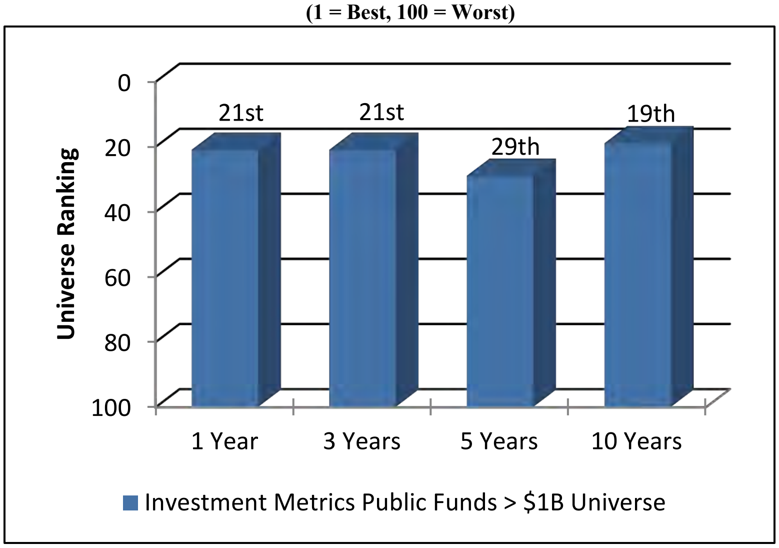
*Returns shown for Stabilized Real Assets and Non-Traditional Growth classes are Internal Rates of Return (IRR).
**Credit Fixed Income and Crisis Risk Offset classes have less than one year of performance history. Returns shown are inception-to-date.

From a long-term perspective, the SURS portfolio has performed well, earning an 7.9% annualized rate of return over the past 30 years, exceeding the 7.6% policy portfolio return. This return is also in line with the 8.0% average assumed rate of return in effect over the last 30 years and the current 6.75% assumed rate of return[2]. In inflation-adjusted terms, the Total Fund returned 5.7% over this time period, exceeding the actuarial real assumed rate target of 4.5% (6.75% less the 2.25% assumed rate of price inflation).

[2] On March 9, 2018, the SURS Board of Trustees approved lowering the System's assumed rate of investment return to 6.75% from 7.25%. The rate was effective as of July 1, 2018.

When compared to a universe of other large public funds, the SURS return ranks in the top quartile for the one-, three- and ten-year periods and the second quartile for the five-year period. Asset allocation is the primary determinant of a fund's ranking in a peer universe.

SURS Total Fund vs. Public Funds > $1 Billion
Periods Ending 6/30/20
(1 = Best, 100 = Worst)



III. Asset Allocation Framework

The purpose of the asset allocation policy is to establish an Investment Policy framework for SURS with a high likelihood, in the Board's judgment, of realizing SURS' investment objective. This is a critical step as the continued sustained growth of SURS assets is a necessary component to achieving long-term sustainability.

The AL study, most recently completed in September 2018, organizes SURS' assets within a functional framework rather than the descriptive-oriented asset-based framework. In this approach, assets are grouped by similar risk profiles, rather than asset class name. At the highest level, assets are classified as either growth-oriented or diversifying strategies, as shown in the following table.

	Functional Asset Class	Allocation as of 6/30/20	Long-Term Goal Allocation
Growth-oriented	Non-Traditional Growth	11%	15%
	Traditional Growth	44%	25%
	Stabilized Growth	24%	26%
Diversifying	Inflation Sensitive	5%	6%
	Principal Protection	8%	8%
	Crisis Risk Offset	6%	20%
	Cash	1%	0%

*Totals may not add due to rounding.

Growth-oriented strategies include risk-taking assets or strategies that produce high total returns relative to other asset classes. Success in this category is often linked to economic success or failure. The three strategic components within this group are shown and described below.

Role	Group	Description
Growth	Non-Traditional Growth	Provide growth in excess of Traditional Growth through exposure to investments driven by exposure to the equity risk and illiquidity risk premiums (i.e. Private Equity and Non-Core Real Assets)
	Traditional Growth	Provide growth in line with traditional public equity markets (i.e. US Equity, Non-US Equity and Global Equity)
	Stabilized Growth	Provide growth through strategies that are exposed to market beta, exhibiting expected returns similar to Traditional Growth but with lower volatility (i.e. Credit fixed income, options strategies, and Core Real Assets)

Diversifying strategies provide two forms of diversification via anchor strategies and offset strategies. Anchor strategies are characterized by low volatility and high liquidity. Offset strategies, in contrast, tend to be higher volatility strategies that have zero-to-negative correlation to public equity markets. These strategies, described in the table below, are designed to perform well in the event of a prolonged equity market downturn.

Role	Group	Description
Diversifying	Inflation Sensitive	Serves a mixed role as part anchor (i.e. TIPS) and part offset (i.e. Commodities) depending on the market environment. Designed to help protect the portfolio during periods of high inflation.
	Principal Protection	Provide an anchor to the portfolio by exhibiting low volatility with minimal exposure to equity risk. Designed to provide consistent, stable returns during most market environments and preserve principal during periods where growth investments are experiencing significant drawdowns (i.e. Core Fixed Income).
	Crisis Risk Offset	Provide an offset to growth risk through liquid exposures to risk premiums expected to exhibit offsetting behavior to growth investments during periods of significant drawdown (i.e. Long Duration Treasury, Systematic Trend Following, Alternative Risk Premia)

IV. Fiscal Year 2020 Accomplishments

Much of the activity completed during Fiscal Year 2020 was tied to implementation of the new functional-based portfolio structure approved in September 2018. The new portfolio structure is designed to produce improvement in long-term expected returns with significantly improved volatility and downside risk measures, with a much tighter range of projected return paths, compared to the previous allocations. Key projects completed include the following:

Growth-Oriented Strategies

- **Continued Implementation of Non-Traditional Growth Allocations** – The Non-Traditional Growth portfolio consists of the private equity and non-core real assets portfolios.

    - **Private Equity** – The board selected TorreyCove Capital Partners (now Aksia TorreyCove) in June 2019 as discretionary private equity advisor to SURS. This selection marked a shift in the model used by SURS to access the private equity asset class, moving away from a fund-of-funds approach to a less costly, more efficient method of directly accessing fund investments. This direct approach allows SURS greater control over portfolio strategy and allows for larger, more meaningful GP allocations. Aksia TorreyCove's contract was completed in September 2019. Since that time, Aksia TorreyCove completed a strategic plan and pacing model for the private equity portfolio and began making commitments on SURS behalf. Aksia TorreyCove has made 13 commitments through June 30, 2020, totaling nearly $480 million, in line with expectations. Importantly, 35% of the commitments have been made to diverse firms.

    - **Non-Core Real Assets** - In December 2019, Callan, SURS specialty real assets consultant, presented a real assets strategic plan, including an updated pacing plan. During FY 2020, the Board approved the following commitments to non-core real estate funds in accordance with the pacing plan.

        - Cabot Industrial Value Fund VI ($50 million)
        - Crow Holdings Realty Partners IX ($50 million) – an existing manager
        - Longpoint Realty Fund II ($50 million) – a diverse firm

- **Restructuring of Traditional Growth Portfolio**

    - **Equities** - In September 2019, the Board approved a new structure for the Traditional Growth portfolio with the goal to reduce exposure to fund the Crisis Risk Offset class, capture the global equity risk premium and increase reliance on passive/structured-active strategies. A search for global equity managers was concluded in June 2020. Four experienced, highly qualified firms were selected to fulfill the mandate. All four firms are diverse-owned. As part of the global equity search, a manager of emerging managers was also selected to replace Progress (further discussion to follow below). The transition, completed in July 2020, reduced the Traditional Growth allocation from 52% to 40%. The assets from the reduction were used to fund Principal Protection, Inflation Sensitive, Credit and CRO portfolios, as discussed below.

- **REITS –** As part of the Traditional Growth restructure, the REITs allocation was eliminated and used to fund diversifying strategies in December 2019.

- **Creation and Structuring of Stabilized Growth Portfolio**

  - **Credit Portfolio** – The credit portfolio resides within the Stabilized Growth Class and its restructuring was approved by the Board in June 2019. The changes, completed in September 2019, included streamlining of the manager lineup from eight mandates to five, implementation of more focused manager guidelines and the adoption of a custom credit-centric benchmark for the overall portfolio.

    During the June 2020 board meeting, staff and consultant recommended an allocation to PIMCO's DiSCO III fund, a complementary add-on to their existing credit account. This private investment targets investments in the dislocated public credit markets. Given the functional framework adopted by the Board, staff is able to temporarily overweight the credit allocation at the expense of core real estate.

  - **Private Credit Specialty Consultant / Advisor Search –** As the makeover of the investment portfolio continues, staff requested in June 2020 to issue an RFP for a private credit consultant/advisor to assist in the buildout of a new segment of the overall credit portfolio. The consultant would provide a high level of control on private credit portfolio construction, pacing and evaluation. In addition, the use of a specialty consultant could increase opportunities to directly access the diverse private credit marketplace and would provide flexibility in the procurement process of securing direct private credit fund commitments. The search is scheduled to conclude in September 2020.

  - **Replacement of Manager of Emerging Managers Partner** - The announced closing of Progress Investment Management (Progress) in December 2019 created an urgent need to replace an important partner. Progress previously served as manager of two emerging managers portfolios for SURS (equity and credit). Action was taken to find replacement managers for both mandates in a timely manner. As stated previously, a replacement for the equity mandate was completed as part of the global equity search that was already in process. Xponance was retained to fulfill the equity mandate. For the credit mandate, Staff issued and completed a Request for Proposal (RFP) process that resulted in the Board's retention of Bivium to manage the global credit allocation. The transition to Bivium was completed in March 2020.

  - **Continued Commitment to Core Real Assets Portfolio** - SURS committed an additional $100 million to Prologis US Targeted Logistics Fund during FY 2020.

Diversifying Strategies

- **Restructuring of Inflation Sensitive Class** – The new blueprint for the inflation sensitive class is 100% TIPS, with no exposure to commodities. Elimination of the small commodities allocation should help to streamline the overall portfolio while marginally enhancing its overall return-risk profile. The total target allocation to the TIPS portfolio went from 4.0% to 6.0% with assets coming from the liquidation of the commodities account and part of the assets from the liquidation of the REIT portfolio. This was completed in December 2019.

- **Restructuring of Principal Protection Class** - The Principal Protection class restructuring, approved in June 2019, was completed in September 2019. Changes included a shift to a purely active approach in the class, adoption of an appropriate benchmark suited to the new structure, and a decrease in the number of managers from five to four with larger allocations to each manager. All four remaining firms are diverse-owned.

- **Crisis Risk Offset (CRO) Searches** – The CRO class includes long duration, trend-following and alternative risk premia strategies. The breakdown between the three classes is approximately 35% long duration, 35% trend-following, and 30% alternative risk premia. The initial funding of 5% to the CRO class was completed in December 2019. Subsequent allocation, with funding from the equity restructuring, resulted in a 10% weighting in July 2020. Although the long-term policy target for the CRO class is 20%, the CRO allocation will not be increased further until completion of a new asset allocation study, slated for FY 2021. For additional information, see Section III (Fiscal Year 2021 Strategic Initiatives).

    - **Long Treasuries** - After the completion of a Request for Information process, the Long Treasuries mandate was allocated to Rhumbline, an existing passive manager, in December 2019, with an initial allocation of 1.75% of the SURS portfolio. Rhumbline is diverse-owned.

    - **Alternative Risk Premia & Systematic Trend-Following Strategies** – The search for alternative risk premia and systematic trend-following investment managers was completed and funded to 5% in December 2019. Four systematic trend-following managers and three alternative risk premia managers were retained with two of those firms being diverse-owned.

Defined Contribution Plans

- **Defined Contribution Plan Provider Search** – In September 2019, after a comprehensive search process, the board approved Voya as the new recordkeeper and Alliance Bernstein as the income solution provider for SURS defined contribution plans. In January 2020, the board approved Principal Financial Group as an annuity provider for the DC plans and the initial investment line-up for the new plans. New plan documents were also approved for both DC plans. The updated Retirement Savings Plan (RSP) was set for implementation on June 1. Unfortunately, implementation has been delayed to September 1, 2020, as a result of the global pandemic. The new supplemental Deferred Compensation Plan is also scheduled for implementation on September 1.

A significant re-write of the DC investment policy was approved in January 2020.

Policies, Investment Beliefs & Trustee Education

- **Investment Policy Revision** – The Investment Policy statement was updated multiple times during FY 2020 as the asset allocation implementation progressed.

- **Procurement Policy Revision** – The Procurement Policy was updated twice in FY 2020, in September 2019 and June 2020.
    - The September amendment allows staff to issue RFPs for mandates included in the strategic allocation without Board approval. The Board still retains decision making authority for hiring managers.
    - The June amendment was recommended to allow SURS to take advantage of "Opportunistic" investments, such as occurred during the COVID-19 pandemic.

- **Review of SURS Investment Beliefs** – In January 2020, the Board reviewed SURS Investment Beliefs and reaffirmed the existing beliefs while adopting a new belief that integrates Environmental, Social and Governance into SURS investment decision-making and monitoring of proxy voting activities.

- **Trustee Education –** Education was provided to Trustees on a number of relevant topics, during FY 2020, including:
    - Defined contribution plan considerations
    - Private equity portfolio construction
    - SURS Investment Beliefs
    - Private Credit
    - Asset Allocation and the Stabilized Growth class
    - Calendar Year 2020 Capital Market Assumptions

Diversity & Inclusion

- **Diverse Manager Week** – SURS hosted its second annual Diverse Manager Week during the week of August 3, 2020. SURS investment staff conducted one-hour meetings with 30 firms across different asset classes. SURS' consultant/advisor partners also participated, with representatives from Meketa, Callan, Aksia TorreyCove, The Bivium Group and Xponance.

- **Commitment to Diversity** – SURS continues to be strongly committed to diversity throughout the investment program. In total, 26 firms owned by minorities, females, or persons with a disability (MFDB) directly manage a total of $7.2 billion, or 36.7% of the Total Fund, as of June 30, 2020. SURS employs a multi-strategy approach designed to maximize opportunities for qualified firms.
    - The Manager Diversity Program (MDP) is a SURS-sponsored initiative designed to identify and provide opportunities to highly successful MFDB investment management firms. Managers in the MDP contract directly with SURS. As of June 30, the MDP totals $4.1 billion and includes 23 minority- or female-owned investment managers across 25 strategies.
        - Increase in MDP assets of approximately $493 million during Fiscal Year 2020.

- Second, SURS retained two firms during FY 2020 to construct manager of emerging managers programs. As mentioned previously, these firms serve to replace the services formerly provided by Progress Investment Management. The Bivium Group was hired to construct a credit portfolio, and Xponance, formerly FIS Group, was selected to construct a global equity portfolio. These collaborations allow SURS to extend its reach into the minority manager universe. As of June 30, the Bivium program includes five minority- or female-owned investment managers (with six mandates) and has total assets of $352 million. The Xponance portfolio includes six minority- or female-owned investment managers and has total assets of $223 million, as of June 30, 2020.

- It is important to note that SURS' commitment to diversity extends beyond the bounds of the MDP and the Manager of Emerging Managers Programs. In addition to the firms previously mentioned, SURS contracts with one other MFDB firm, bringing the total number of MFDB firms in direct partnership with SURS to 26. As mentioned previously, assets managed for SURS by these 26 firms are approximately $7.2 billion, or 36.7% of the Total Fund, as of June 30, 2020.
    - Increase in total assets with diverse firms of approximately $1.2 billion during Fiscal Year 2020.

V. Fiscal Year 2021 Strategic Initiatives

Each year Staff and the General Investment Consultant (Meketa Investment Group) undertake initiatives to assist the Board with the goal of achieving more effective and cost-efficient implementation of investment strategies and positively contribute to the health of the System. The initiatives outlined below are often related and long term in nature.

Strategic Allocation Study

Given the significant economic impact from the ongoing global pandemic and the resulting change in the portfolio's risk/return profile, it is now prudent to revisit the policy allocation structure of the SURS asset portfolio. The most recent asset-liability study concluded in September 2018. Completion of a new study toward the end of Fiscal Year 2021 could readjust the policy allocation at the shorter end of the typical 3-5 year review cycle.

Private Debt Specialty Consultant / Advisor Search

As mentioned previously, a search for a private debt consultant / advisor was initiated in June 2020 and is scheduled to conclude in September 2020. A private credit consultant / advisor would assist in the buildout of a new segment of the overall credit portfolio. Upon selection, the consultant / advisor would assist in the development of a long-term strategic plan and pacing model for the private credit portfolio.

Continued Implementation of Non-Traditional Growth Allocation

- **Real Assets** - Real assets, which includes real estate, infrastructure, farmland, and timberland, is a component of the Broad Growth strategic class of the asset allocation model. The long-term policy target for real assets is 10% of the total portfolio (6% in Stabilized Growth/core assets and 4% in Non-Traditional Growth /non-core assets). SURS Real Assets portfolio currently includes real estate and infrastructure. Commitments to farmland will be considered during FY 2021. Staff will continue to work with Callan, specialty consultant for the real assets portfolio, to implement the strategic plan and pacing model for the coming year. The pacing plan ensures SURS annually deploys capital at a level which allows attainment of the strategic plan over time.

- **Private Equity** – The long-term policy target for private equity is 11% of the total portfolio. As mentioned previously, the Board selected TorreyCove Capital Partners (now Aksia TorreyCove) in June 2019 as discretionary private equity advisor to SURS. In the coming year, Aksia TorreyCove will continue implementation of the pacing model, which will result in the private equity portfolio gradually increasing to the target level over next several years. In total, commitments of $415 million to $470 million are planned for FY 2021.

Implementation of Defined Contribution Plans

Fiscal Year 2021 will bring meaningful change to the SURS defined contribution plans. First, the SMP has been redesigned and will be launched September 1, 2020. The revamped plan will be renamed the SURS Retirement Savings Plan (RSP). Enhancements will include a new default investment option, a new simplified best-in-class fund lineup, new planning and education tools and a new recordkeeper. Finally, SURS will launch a new supplemental defined contribution plan during FY 2021. See Section VIII or the SURS.org website for additional information.

Investment Policy Review

The Investment Policy was last reviewed and approved by the Board at the January 2020 Investment Committee meeting. Additional review will be conducted and potential revisions to the Policy will be considered during FY 2021. It is also likely that fiduciary counsel will provide a periodic review of the IPS during the coming year.

Procurement Policy Revision

A review of the Investment Procurement Policy will occur during FY 2021. The Investment Procurement Policy provides procedural guidance for the search and selection for SURS investment managers and/or fund investments.

Diversity Initiatives

SURS will continue to review opportunities in the investment program to consider the utilization of minorities, females and persons with a disability. Investment managers of diversity are always encouraged to participate in the search process if an applicable strategy/mandate is identified. SURS recently hosted its second annual Diverse Manager Week. Investment managers in strategies across the portfolio were invited to present to staff and the corresponding consultant (either general or specialty). In total, 30 diverse owned firms participated in meetings during the week.

Investment Manager Oversight, Due Diligence, and Risk Management

A critical duty of the investment team and Meketa is to monitor the numerous investment managers under contract with SURS. Each manager plays a role in the success of the overall program and extensive resources are utilized to ensure strategies are functioning as desired and in accordance with guidelines. Risk management monitoring of the program continues to expand and evolve with the implementation of BlackRock's Aladdin, a risk analytics tool. Once fully implemented, it will provide a comprehensive view of SURS portfolio and zero in on exposure across every portfolio and functional classes. It will also allow staff to monitor risk factors and run stress tests across various scenarios. In addition to the new risk system, staff will be implementing a new software program designed to more efficiently manage documents and provide analytics for the expanding private markets portfolio.

Investment Management Fees

SURS pays close attention to the level of investment management fees paid to its external investment managers. Fees are negotiated with investment managers prior to the commencement of the relationship with SURS and may be subsequently renegotiated, if appropriate, especially in instances where an investment manager receives an additional allocation(s). Fees vary significantly among investment managers, with the services of private markets managers, such as those in real assets and private equity being generally higher than those of public market managers.

During Fiscal Year 2020, staff negotiated more favorable fee arrangements with ten new and existing investment service providers. In aggregate, these fee negotiations are expected to result in approximately $1.4 million in fee savings. It should also be noted that significant fee savings are expected in FY 2020 and beyond from the recent transition in the private equity portfolio. SURS is moving away from the higher cost, fund-of-funds approach towards a more direct approach, which is expected to save millions over the coming years.

In total, SURS paid approximately $63.9 million or approximately 33 basis points in investment management fees and administrative expenses for Fiscal Year 2020. Total investment management fees for Fiscal Year 2021 are projected to increase by $6.4 million from fiscal year 2020 budgeted fees and include fees paid directly from alternative asset funds. This increase is due to the continued growth of the real assets portfolio and continued reallocation of assets from public equities into diversifying strategies.

VI. Environmental, Social & Governance (ESG) Issues

SURS continues to place a high priority on ESG issues. Illinois Public Act 101-0473, effective January 1, 2020, requires that SURS Investment Policy include material, relevant, and decision-useful sustainability factors to be considered by the Board, within the bounds of financial and fiduciary prudence, in evaluating investment decisions. Such factors must include, but are not limited to: (1) corporate governance and leadership factors; (2) environmental factors; (3) social capital factors; (4) human capital factors; and (5) business model and innovation factors, as provided under the Illinois Sustainable Investing Act. Revisions to the Investment Policy were made during FY 2020 to comply with this new statute. In addition, a related item has been added to the SURS Board of Trustees' Investment Beliefs.

Proxy voting is one important component of the System's corporate governance responsibilities. Additional actions pertaining to corporate governance include membership in the Council for Institutional Investors (CII), a nonprofit organization of more than 135 pension funds, foundations, and endowments with combined assets of approximately $4 trillion. CII's advocacy statement is to "educate its members, policymakers and the public about the value of corporate governance, shareowner rights and related investment issues." CII also advocates on member's behalf "for effective corporate governance and strong shareowners rights."

On October 19, 2017, SURS became a signatory to the Investor Stewardship Group (ISG), joining more than 70 U.S. and international investors with combined assets in excess of $32 trillion. The ISG establishes a framework comprised of a set of stewardship principles for institutional investors and corporate governance principles for U.S. listed companies.

VII. Manager Diversity Program

Overview

The Manager Diversity Program (MDP) is a SURS-sponsored initiative designed to identify and provide opportunities to highly successful investment management firms owned by minorities, females, and persons with a disability.

Key items of note:

- Developed in 2004 to identify and retain MFDB firms
- Managers contract directly with SURS
- Market Value of $4.1 billion, as of June 30, 2020

Asset Class	Number of MFDB Managers	Market Value* as of June 30, 2020	Commitment Amount (Private Equity & Real Assets Only)
Traditional Growth			
U.S. Equity	5	$1,103 million	N/A
Non-U.S. Equity	3	$865 million	N/A
Non-Traditional Growth			
Private Equity	5	$190 million	$305 million
Non-Core Real Assets	3	$105 million	$265 million
Stabilized Growth			
Options	1	$284 million	N/A
Principal Protection	4	$1,402 million	N/A
Crisis Risk Offset			
Systematic Trend	1	$67 million	N/A
Alternative Risk Premia	1	$83 million	N/A
Total	23**	$4,100 million	

*Totals may not add due to rounding

**23 firms and 25 strategies due to 2 strategies with 1 private equity investment manager and 2 strategies with 1 real assets manager

Performance Objectives

The performance objective of the MDP is to seek annualized investment returns, net of investment management fees, in excess of the market goal for 1, 3, 5, and 10 year periods. While individual investment managers may underperform in any given year, the diversification within the program should limit the underperformance at the program level.

Fiscal Year 2020 Performance Review

The MDP returned 0.4% for the fiscal year 2020, lagging the benchmark return of 2.0%. The private equity allocation provided the highest return, with an IRR of 10.0%. Within the private equity portfolio, Fairview Lincoln Fund I and Muller & Monroe Emerging Private Equity Fund of Funds provided strong returns. Non-US Equity returned the lowest at -7.8%, hampered by Ativo underperformance. In IRR terms, the Real Assets portfolio returned 4.2%, led by the Franklin Templeton MDP RE 2015 fund which returned 10.2%. Fixed Income also provided a positive return of 6.3%. The core fixed income managers were converted into Principal Protection mandates over the course of the year.

Investment Performance*
As of June 30, 2020

	1 Year	3 Years	5 Years	Since Inception
SURS MDP	0.4%	4.2%	4.8%	5.7%
Benchmark	2.0%	5.4%	5.5%	5.9%

*Net of investment management fees

Fiscal Year 2020 MDP Accomplishments

As of June 30, 2020, the MDP is valued at approximately $4.1 billion. A summary of MDP activities follows.

- SURS added two MFDB-owned firms to the Crisis Risk Offset category, Longtail Alpha and ARP Investments.
- SURS made direct private equity allocations via our discretionary private equity advisor, Aksia TorreyCove. Commitments were made to the following funds during FY 2020, although not all had drawn capital by June 30, 2020:
  - Clearlake Capital Partners VI ($30 million)
  - OceanSound Partners Fund ($25 million)
  - Reverence Capital Partners Opportunities Fund III ($50 million)
  - Stellex Capital Partners II ($25 million)
  - One Rock Capital Partners III ($35 million)
- SURS made direct real assets allocations via our real assets consultant, Callan. Longpoint Realty Fund II received a commitment of $50 million.
- SURS hosted the 2nd Annual SURS Diverse Manager Week event

SURS' commitment to diversity extends beyond the bounds of the MDP. In addition to the 23 firms utilized in the MDP, SURS contracts with three additional MFDB firms, bringing the total number of MFDB firms in partnership with SURS to 26. In the most recent Investment Policy, SURS has implemented guidelines for a graduation program for firms in the manager of emerging managers program to receive direct allocations from SURS.

Assets managed for SURS by these 26 firms are approaching $7.2 billion, or 36.7% of the Total Fund, as of June 30, 2020.

Fiscal Year 2021 MDP Initiatives

Plans for the MDP in FY 2021 include the following:

- Expand industry outreach efforts
- Host the 3rd Annual SURS Diverse Manager Week event
- Continue diligent monitoring of the overall program, manager structure, and risk parameters within the program
- Provide a thorough review of the MDP to the Board at the March 2021 Board meeting
- Identify potential opportunities to increase funding for existing qualified investment managers
- Continued interaction with system consultant, Meketa, via more frequent discussions regarding MFDB investment managers

VIII. Defined Contribution Plans

Overview

The Self-Managed Plan (SMP) is a defined contribution option available to SURS members. The SMP has grown steadily since the plan's inception in April 1998. Highlights of the plan include:

- Approximately $3.0 billion in assets as of June 30, 2020
- SMP forfeiture assets were $12.3 million as of June 30, 2020
- Disability reserve assets were $119.5 million as of June 30, 2020
- One Lead Administrator
  - Fidelity Investments
- Two Service Providers
  - Fidelity Investments ($1.8 billion in assets)
  - TIAA ($1.1 billion in assets)
- 29 investment options as of June 30, 2020
  - Includes series of lifecycle funds in both TIAA and Fidelity lineups
- Over 22,000 Participants currently invested
  - 14,257 active participants
  - 8,390 inactive participants

August / September 2020 Transition to Retirement Savings Plan

The SMP will be transitioning to a new administrator and recordkeeper, Voya Financial. In addition, the plan will be renamed the SURS Retirement Savings Plan (RSP). The RSP will feature a new lineup of investment options, including a customized target-date portfolio, the SURS Lifetime Income Strategy (LIS), as the default investment option. The timeline for this transition is currently planned as follows:

- August 14, 2020: Blackout period begins, and accounts start to transition to Voya
- September 1, 2020: SURS Retirement Savings Plan goes live, and members can again make changes
- October 1, 2020: All features of the LIS strategy will become available to members
- In addition to the default investment option, members will be able to select from a core investment lineup of 15 funds across various asset classes.

Fiscal Year 2020 Defined Contribution Accomplishments

- Completed search for recordkeeping and custom investment solution providers for the SMP/RSP, as well the new supplemental defined contribution / Deferred Compensation Plan created in Public Act 100-0769, selecting Voya Financial as recordkeeper, and Alliance Bernstein to manager the custom target date solution for the SURS Lifetime Income Strategy.
- Approved new lineup of investment options for the defined contribution plans
- Retained Principal Financial Group as the annuity provider for the defined contribution plans
- Approved revised plan documents for the Retirement Savings Plan and the Deferred Compensation Plan

Fiscal Year 2021 Defined Contribution Initiatives

Plans for the Defined Contribution Plan in FY 2021 include the following:

- Continue diligent monitoring of the overall program, providers and investment options.
- Complete transition to the new recordkeeper and investment option
- Launch the new Deferred Compensation Plan.