



Update on IMD Initiatives

May 29, 2013

Near-term Priorities (0 to 3 Months)

- Maintain momentum in private market investment pipeline
- Review and prioritize public market initiatives
- Review IMD organization and business model
 - Vacancies
- Update/Codify policies and procedures (attached)
- Enhance investments flexibility: legislation
- Investment Forum
- CEM Survey participation
- Prioritize implementation of investment infrastructure
- National Association of State Investment Professionals annual meeting

Seeking More Flexible Statutory Limits

- Access to attractive risk-adjusted investment opportunities can change substantially and quickly over time according to:
 - Capital availability
 - Pricing of risk capital
 - Global economic growth sectors
 - Regulations
- A thoughtful, prudent, and methodical program to build non-public asset class allocations can take a significant period of time
- With more flexibility, 2012 study indicated the NCRS expected return profile could rise roughly 0.50% per year over next five to ten years or \$350 million per year

Growing Internal Management

- Fixed Income assets have been managed internally in the Treasurer's office since the 1940's
- A team of five investment professionals with more than 90 years combined experience manage in excess of \$40 billion
- The total costs to manage IMD's core fixed income portfolio is roughly 1 basis point (0.01% of assets) compared to external management fees of 15 to 25 basis points
- Savings range from \$40-\$70 million a year, plus the team has beat its benchmark consistently over past decade
- Evaluating equity index funds and fund-of-funds as other areas where a portion of ~\$22 million of annual fees could be lowered over time through internal management

CEM Industry Data on Internal Management

- “Funds with more internal management performed better than funds with less...
 - ”For the time period 1991-2010 (5,605 observations): “...for every 10% increase in internal management, there was an increase of 3.6 basis points in net value-added; this increase was driven largely by the lower costs attributed to internal management”.
- For real estate and diversified private equity, fund-of-funds underperforms by a wide margin. For 14 years, ending 2011:
 - Average annual real estate net returns: fund-of-funds was 5.39%; external private direct funds was 7.77%; and internal active direct was 9.26%
 - Returns for diversified private equity are: fund of funds: 5.35%; external direct funds: 10.14%
 - The numbers are drawn from the CEM US Corporate and Public universe

Medium-term Priorities (6 to 9 Months)

- Review strategic portfolio construction
 - Update asset-liability study
 - Develop Annual Investment Work Plans
- Investment initiatives
 - Internal equity index management
 - Infrastructure investments
 - Co-investments program(s)
 - Non-fund vehicles
 - Strategic partnerships
 - Total fund risk portfolio management
 - NC Innovation Fund
 - Emerging/Small/Niche Private Equity Program
- Process map operations/portfolio management support to identify efficiency opportunities and enhance reporting