FISCAL YEAR 2022 INVESTMENT PLAN

S·U·R·S
STATE UNIVERSITIES RETIREMENT SYSTEM

September 2021

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S·U·R·S
STATE UNIVERSITIES RETIREMENT SYSTEM

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Investment Department

August 30, 2021

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

RE: ***Fiscal Year 2022 Investment Plan***

Dear Board of Trustees:

The Investment Staff is pleased to provide the SURS Investment Plan for Fiscal Year 2022. 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 2022 marks the eleventh year of the formal plan for the SURS investment program.

The Investment Plan reviews the results of Fiscal Year 2021 and defines the strategy for Fiscal Year 2022 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 investment portfolio successfully navigated the volatile financial markets to produce robust returns during Fiscal Year 2021. The SURS investment portfolio returned 23.8%, net of fees, well ahead of the assumed rate but slightly trailing the policy benchmark. This return marked the 4th highest fiscal year return in SURS history.

From a long-term perspective, the SURS portfolio has performed well, earning an 8.5% annualized rate of return over the past 30 years, exceeding the 8.2% policy portfolio return. This return is also in excess of the 7.9% average assumed rate of return in effect over the last 30 years and the current 6.75% assumed rate of return.

As of June 30, 2021, the defined benefit plan is valued at approximately \$23.5 billion while the Retirement Savings Plan (RSP) is valued at approximately \$3.9 billion (including forfeiture and disability reserve assets).

Given the significant economic impact from the ongoing global pandemic and the resulting change in the portfolio's risk/return profile, prudence dictated the initiation of an updated asset-liability study in 2021. At the conclusion of the study in June 2021, new long-term strategic policy targets were adopted. This new asset mix is positioned to generate an expected return in-line with the current actuarial rate and offers an attractive mix of liquidity, drawdown protection, and expected return.

Fiscal Year 2021 also brought meaningful change to the SURS defined contribution plans. Highlights included the redesign and launch of the SURS Retirement Savings Plan (RSP) and the introduction of a new supplemental Deferred Compensation Plan (DCP). This new voluntary plan, called the SURS Deferred Compensation Plan (DCP), will provide members an avenue to save more and generate additional income in retirement.

Other key accomplishments in the defined benefit portfolio include:

- Completion of a private credit specialty advisor search;
- Continued commitment to core real assets portfolio;
- Continued implementation of non-traditional growth allocations (private equity and real assets), including the addition of a new farmland asset type;
- Restructuring of traditional growth portfolio;
- Increased allocation to the Crisis Risk Offset (CRO) class. The CRO class contains diversifying investments that are expected to exhibit offsetting behavior to growth investments during periods of significant drawdown; and
- Increase in assets under management by diverse firms by $2.6 billion during FY 2021 (from $7.2 billion, or 36.9%, to $9.8 billion, or 41.6%).

Numerous projects are planned for Fiscal Year 2022, including, but not limited to, the following:

- Implementation of strategic allocation study;
- Evaluation of Traditional Growth portfolio structure;
- Continued implementation of Private Credit and Non-Traditional Growth allocations;
- Education on potential new strategies in the Crisis Risk Offset (CRO) class;
- Continued review of opportunities to include firms owned by minorities, women and persons with a disability in the investment program;
- Completion of Master Custodian and Securities Lending provider searches; and
- Completion of search for proxy voting service provider.

The Investment Plan for Fiscal Year 2022 contains additional details on Fiscal Year 2021 accomplishments and strategic initiatives for Fiscal Year 2022. While much was achieved during Fiscal Year 2021, it is important to maintain focus on the future. The investment team and external partners continue to seek excellence in every aspect of the investment program. I look forward to discussing the ***Fiscal Year 2022 Investment Plan*** at future meetings.

Sincerely,

Doug Wesley

Douglas C. Wesley, CFA
Chief Investment Officer

cc: Suzanne Mayer, Interim Executive Director

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I. Purpose

The Investment Plan reviews the results of Fiscal Year 2021 and defines the strategy for Fiscal Year 2022 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 240,000 active, inactive and retired participants. SURS maintains both a defined benefit and a defined contribution plan, known as the SURS Retirement Savings Plan (RSP). In addition, beginning March 1, 2021, SURS introduced a new supplemental defined contribution plan, called the SURS Deferred Compensation Plan (DCP). The DCP will provide members an avenue to save more and generate additional income in retirement. As of June 30, 2021, the defined benefit plan is valued at approximately $23.5 billion while the RSP is valued at approximately $3.9 billion (including forfeiture and disability reserve assets). The investment portfolio is broadly diversified across several functional classes.

Fiscal Year 2021 Performance Review

The SURS investment portfolio successfully navigated the volatile markets to produce robust returns during FY 2021. The SURS investment portfolio returned 23.8%, net of fees, well ahead of the assumed rate but slightly trailing the policy benchmark. This return marked the 4th highest fiscal year return in SURS history.

Over the last year, global equity markets produced strong returns, largely driven by record fiscal and monetary policy stimulus and an accelerated COVID-19 vaccine rollout. In the U.S., the economic recovery continued to gain strength as jobless claims declined steadily to reach pandemic-era lows in the June quarter. Concerns have risen, however, that the historic economic stimulus could lead to higher inflation and, ultimately, higher interest rates. Longer term bond yields have increased in anticipation.

The table that follows illustrates the performance of the overall SURS investment portfolio relative to the policy portfolio and average assumed rates of investment return, as of June 30, 2021.

Investment Performance*
As of June 30, 2021

	1 Year	3 Years	5 Years	10 Years	20 Years	25 Years	30 Years
SURS	23.8%	10.4%	10.3%	8.5%	7.3%	7.9%	8.5%
Policy Portfolio	24.4%	10.7%	10.3%	8.6%	7.3%	7.8%	8.2%
SURS Assumed Rate	6.8%	6.8%	6.8%	7.1%	7.7%	7.9%	7.9%

*Net of investment management fees

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

The Total Fund's underperformance relative to the policy portfolio for Fiscal 2021 was due to a number of factors, including:

- Weak relative performance by the non-U.S. and the global equity segments of the Traditional Growth portfolio;
- Underperformance by the option strategies component of the Stabilized Growth portfolio;
- Underperformance by the non-core real estate segment of the Non-Traditional Growth portfolio;
- Weak relative performance by the Crisis Risk Offset class; and
- An underweight to the options strategies component of the Stabilized Growth portfolio. Although the options portfolio lagged its benchmark, it was the best absolute performing segment of the Stabilized Growth portfolio.

Portfolio highlights included:

- Outperformance by the stabilized real assets and credit fixed income segments of the Stabilized Growth portfolio;
- Strong relative performance in the non-core real estate debt and infrastructure portfolios (Non-Traditional Growth);
- Modest excess performance by the private equity segment of the Non-Traditional Growth portfolio; and
- Modest relative performance by the Principal Protection portfolio;

At the aggregate level, the Stabilized Growth and Principal Protection portfolios exceeded their performance benchmarks for the year ending June 30, 2021, while the Inflation Sensitive portfolio matched the benchmark. The Non-Traditional Growth, Traditional Growth, and Crisis Risk Offset classes lagged their benchmarks for the period.

Of the private, illiquid asset classes, the private equity portfolio provided the strongest absolute return, +60.8%. The non-core real estate debt asset class provided the strongest relative return, exceeding the benchmark for the one-year period by 1,730 basis points.

Performance of each of the broad asset classes during FY 2021 is shown in the table that follows.

SURS FY 2021 Asset Class Returns
(Net of Fees)

Asset Class	FY 2021 Return
Growth-Oriented	
Non-Traditional Growth	42.3%
Performance Benchmark	43.5%
Excess	-1.2%
Traditional Growth	40.5%
Performance Benchmark	40.9%
Excess	-0.4%
Stabilized Growth	13.1%
Performance Benchmark	12.0%
Excess	1.1%

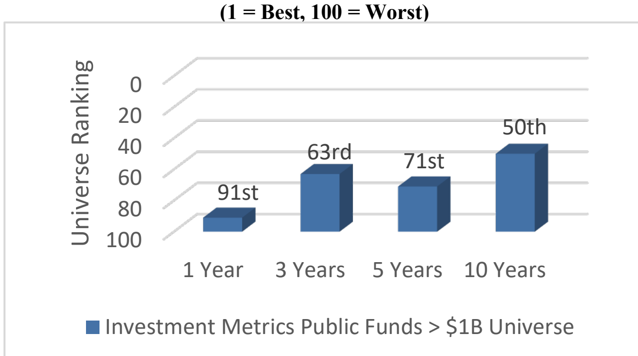
Asset Class	FY 2021 Return
Diversifying	
Inflation Sensitive	6.5%
Performance Benchmark	6.5%
Excess	0.0%
Principal Protection	-0.2%
Performance Benchmark	-0.7%
Excess	0.5%
Crisis Risk Offset	-0.1%
Performance Benchmark	6.6%
Excess	-6.7%

From a long-term perspective, the SURS portfolio has performed well, earning an 8.5% annualized rate of return over the past 30 years, exceeding the 8.2% policy portfolio return. This return is also in excess of the 7.9% 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 6.3% over this time period, exceeding the current actuarial real assumed rate target of 4.5% (6.75% less the 2.25% assumed rate of price inflation).

Peer Analysis

When compared to a universe of other large public funds, the SURS return trails that of the median plan for the one-, three- and five-year periods ending June 30, 2021, and matches the median plan for the ten-year period. The primary reason for the below-median results in the shorter term periods is a more defensive posture compared to peers. The SURS portfolio has a lower equity allocation and a higher Crisis Risk Offset allocation than the median plan in the universe. While this positioning will result in weaker relative results in very strong equity markets like those seen in FY 2021, it is expected to provide critical downside protection during periods of significant equity market declines. Asset allocation is the primary determinant of a fund's ranking in a peer universe.

SURS Total Fund Return vs. Public Funds > $1 Billion
Periods Ending 6/30/21
(1 = Best, 100 = Worst)



Risk-Adjusted Results

On a risk-adjusted basis, the SURS portfolio compares much more favorably to the Median Public Fund, as shown in the table below. Over the three-, five-, and ten-year periods, SURS performance either matches or exceeds that of the median public fund.

Risk-Adjusted Return of SURS vs. Peers

	1 Year	3 Years	5 Years	10 Years
Total Fund (Gross of Fees)	24.0%	10.7%	10.6%	8.7%
Risk-Adjusted Median[3]	24.2%	10.2%	10.2%	8.7%
Excess Return	**-0.2%**	**0.5%**	**0.4%**	**0.0%**

The pursuit of a more efficient (i.e., higher return per unit of risk) portfolio has been an explicit consideration of the SURS Board over the last two asset-liability studies, in particular.

[2] On June 3, 2021, the SURS Board of Trustees approved lowering the System's assumed rate of investment return to 6.50% from 6.75%. The rate is first effective with the valuation as of June 30, 2021.
[3] Risk-adjusted median normalizes the median fund to the SURS exhibited volatility. Calculated as: risk-adjusted median = unadjusted median return * (SURS volatility/peer volatility). Source: Meketa.

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. SURS asset allocation framework 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.

Industry best practices suggest completing an asset-liability (A-L) study every three-to-five years. SURS has adhered to this practice by completing recent studies in 2011, 2014, and 2018. Given the significant economic impact from the ongoing global pandemic and the resulting change in the portfolio's risk/return profile, the Board decided it was prudent to embark on an updated asset-liability study in 2021.

The goals of the 2021 asset-liability process were the same as those in 2018, to balance the following objectives:

1. To minimize the likelihood of material deterioration in the funded ratio over the near-term;
2. To achieve a long-term funded ratio in-line with the statutory goal of 90% in 2045;
3. To maintain contributions within a reasonable band and with a reasonable volatility; and
4. To improve the portfolio's expected efficiency by achieving portfolio performance targets in-line with the current actuarial rate and at a similar or lower expected risk than the current portfolio.

At the conclusion of the study in June 2021, the Board adopted the long-term strategic policy targets shown in the table that follows. This asset mix is positioned to generate an expected return in-line with the current actuarial rate and offers an attractive mix of liquidity, drawdown protection, and expected return. In addition, the new strategic policy targets continue the changes first approved in 2018, including the growth of both CRO and private market investments while continuing the reduction of traditional growth from current levels, although to a higher target than that adopted in 2018. The funding source for much of the 2021 portfolio changes would be from a reduction in the stabilized growth portfolio.

	Functional Asset Class	Strategic Policy Target as of 7/01//21	Previous Long-Term Strategic Policy Target	New Long-Term Strategic Policy Target
Growth-oriented	Non-Traditional Growth	11%	15%	16%
	Traditional Growth	40%	25%	35%
	Stabilized Growth	21%	26%	17%
Diversifying	Inflation Sensitive	5%	6%	5%
	Principal Protection	8%	8%	8%
	Crisis Risk Offset	15%	20%	19%

An implementation timeline is included in the Appendix.

At the highest level, assets are classified as either growth-oriented or diversifying strategies, as shown in the following table.

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 that follows, 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 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 2021 Accomplishments

Much of the activity completed during Fiscal Year 2021 was tied to implementation of the functional-based portfolio structure approved in September 2018. The 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** – Aksia TorreyCove (formerly TorreyCove Capital Partners) has served as SURS' discretionary private equity advisor since September 2019. This approach 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. During FY 2021, SURS made a total of nine commitments to private equity investments, totaling $291 million. These commitments were in accordance with the strategic plan and pacing model completed by Aksia TorreyCove. Importantly, 60% of the commitments during this period were made to diverse firms. Highlights of commitments made during FY 2021 include:
    - **Expansion of the Relationship with Fairview Capital Partners** – An additional $100 million was committed to the Fairview Lincoln Fund I (Series B) portfolio to focus on venture capital and small-to-mid buyout funds in the diverse private equity space.
    - **Emphasis on Co-Investments** – The allocation within Mesirow Financial Private Equity Special Fund B was revised to increase exposure to co-investments via Mesirow Financial Private Equity Fund VIII-B. Co-investments offer benefits of investing directly into private companies at a significantly reduced cost.
    - **Increased Exposure to the Asia Pacific Region** – In order to better reflect the composition of the global private equity universe, additional commitments were made by Aksia TorreyCove to experienced General Partners for investment in the Asia Pacific region.

  - **Non-Core Real Assets**
    - **Addition of a New Asset Class Within Real Assets** - With the assistance of SURS' specialty real assets consultant, Callan, a new strategy was introduced. Farmland is the newest asset type to receive an allocation within the real assets portfolio. Farmland is anticipated to make up 5% of the real assets portfolio over time. SURS has committed $60 million to one fund to date.
    - **Consideration of Non-Traditional Growth Real Assets Strategies**

During FY 2021, the Board approved the following commitments to non-traditional growth real assets funds in accordance with the strategic plan and pacing study recently completed by Callan.

- Non-Traditional Growth
  - Homestead Capital USA Farmland Fund III ($60 million)
  - BIG Real Estate Fund II (lesser of $50 million or 10% of total commitments)
  - Torchlight Real Estate Fund VII ($50 million)
  - Newport Capital Partners III (lesser of $30 million or 10% of total commitments)
  - Ember Infrastructure Partners Fund I (lesser of $50 million or 10% of total commitments)
  - Brookfield Strategic Real Estate Partners Fund IV ($75 million)

- **Implementation of Traditional Growth Portfolio Restructuring**

  - **Equities** - In FY 2020, the Board approved a new structure for the Traditional Growth portfolio with the goal to reduce exposure to fund the Crisis Risk Offset (CRO) class, capture the global equity risk premium and increase reliance on passive/structured-active strategies. Between December 2019 and July 2020, SURS' Traditional Growth allocation was reduced from 52% to 40% of SURS' total fund, in line with interim policy targets. The proceeds of the transition were reallocated to fund the Principal Protection, Inflation Sensitive, Credit and CRO portfolios. The completion of the asset-liability study in June 2021 resulted in a long term policy target of 35% to Traditional Growth. Due to market gains over the past year, SURS' assets in Traditional growth were at 43.5% as of June 2021. An additional step of the transition was completed at that time, bringing Traditional Growth assets back to 40%, in line with the current interim policy and closer to the long term target. This reduction was used to partially fund the most recent increase to CRO.

- **Continued Implementation of Stabilized Growth Portfolio**

  - **Completion of Private Credit Specialty Advisor Search** – In September 2020, the search for a private credit specialty advisor concluded with the Board's selection of Meketa Investment Group as discretionary private credit advisor. In their role, Meketa will assist in the buildout of this new segment of the overall credit portfolio. The discretionary advisor provides a high level of control on private credit portfolio construction, pacing and evaluation. In addition, the use of a specialty advisory may 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.

    Since their selection in September 2020, Meketa has completed a strategic plan and five-year pacing model for private credit and has begun making commitments on SURS behalf. Through June 30, 2021, commitments totaling $425 million have been made to three private credit investments. Commitments to minority-owned firms represented $50 million of the total during the year.

- **Continued Commitment to Core Real Assets Portfolio** - SURS made the following commitments to the core real assets portfolio during FY 2021:
  - BlackRock Global Renewable Power Fund III ($100 million)
  - Carlyle Property Investors ($100 million).

Diversifying Strategies

- **Crisis Risk Offset Continued Implementation** – The CRO class includes long duration, trend-following and alternative risk premia strategies. The target breakdown between the three classes is 21% long duration, 53% trend-following, and 26% 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. The completion of the asset-liability study in June 2021 resulted in a policy target of 19% to the CRO class. An interim step of additional funding, from various classes, to reach an approximate 15% weighting was completed in June 2021. All the interim funding steps were made to managers selected during a search process completed in December 2019.

Defined Contribution Plans

- **Roll-out of new Retirement Savings Plan (RSP) -** Fiscal Year 2021 brought meaningful change to the SURS defined contribution plans. First, the Self-Managed Plan (SMP) was redesigned and launched September 1, 2020. The revamped plan has been renamed the SURS Retirement Savings Plan (RSP). Enhancements include a new default investment option, a new simplified best-in-class fund lineup, new planning and education tools and a new recordkeeper, Voya Financial.

- **Introduction of New Supplemental Deferred Compensation Plan (DCP)** - SURS is excited to announce a new supplemental defined contribution plan that became available from participating SURS employers beginning March 1, 2021. This new voluntary plan, called the SURS Deferred Compensation Plan (DCP), will provide members an avenue to save more and generate additional income in retirement. Most active SURS members employed by a state university, community college or other government entity will be able to participate.

  The DCP was made available on March 1, 2021, to eligible employers who must adopt the plan before members may begin participation. All eligible employers are required to adopt the SURS Deferred Compensation Plan before June 30, 2021. Voya Financial is the recordkeeper for SURS DCP.

- **Revisions to the DC Investment Policy** were reviewed and approved in March 2021.

Policies, Investment Beliefs & Trustee Education

- **Investment Policy Revision** – The defined benefit Investment Policy statement was updated multiple times during FY 2021 as the asset allocation implementation progressed.

- **Procurement Policy Revision** – The Procurement Policy was reviewed and updated in January 2021.

- **Trustee Education –** Education was provided to Trustees on a number of relevant topics, during FY 2021, including:
  - Diversity and Inclusion Considerations in Procurement
  - Farmland
  - Infrastructure
  - Asset-Liability Study
  - Real Estate Specialty Property Types
  - Active vs. Passive
  - Calendar Year 2021 Capital Market Assumptions

Diversity & Inclusion

- **Diverse Manager Week** – SURS hosted its third annual Diverse Manager Week during the week of August 2, 2021. SURS investment staff conducted one-hour meetings with 21 firms across different asset classes. SURS' consultant/advisor partners also participated, with representatives from Meketa, Callan, Aksia TorreyCove, Fairview Capital Partners, The Bivium Group and Xponance.

- **Co-Host of Various Webinars Focused on Diversity** – SURS has co-hosted webinars throughout the year alongside Bivium Capital and the National Association of Investment Companies (NAIC). Panelists shared best practices in the industry on a variety of topics, including ESG investing. In addition, SURS participated in an Institutional Investor Roadshow with NAIC where potential private equity firms presented their capabilities to SURS and our external private equity partners.

- **Revision to MWDBE Brokerage Utilization Goals** – At the December 2020 meeting, the Board reviewed the asset and brokerage goals for the utilization of diverse firms. Upon recommendation by staff, the Board increased the brokerage goals for U.S. Equity, Non-U.S. Equity, and Global Equity as indicated in the table below.

Asset Class	Goal	New Goal
U.S. Equity	30%	35%
Non-U.S. Equity	20%	25%
Global Equity	20%	22%

- **Commitment to Diversity** – SURS continues to be strongly committed to diversity throughout the investment program. In total, 32 firms owned by minorities, women, or persons with a disability (MWDB) directly manage a total of $9.8 billion, or 41.6% of the Total Fund, as of June 30, 2021. 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 MWDB investment management firms. Managers in the MDP contract directly with SURS. As of June 30, the MDP totals $5.6 billion and includes 29 minority- or women-owned investment managers across 32 strategies.

    - Increase in MDP assets of approximately $1.5 billion during Fiscal Year 2021.

- Second, SURS partners with two firms to construct manager of emerging managers programs. The Bivium Group manages a credit portfolio, and Xponance manages non-US and global equity portfolios. These collaborations allow SURS to extend its reach into the minority manager universe. As of June 30, 2021, the Bivium program includes five minority- or women-owned investment managers (with six mandates) and has total assets of $395 million. The Xponance portfolio includes eight minority- or women-owned investment managers (with ten mandates) and has total assets of $305 million, as of June 30, 2021.

- 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 MWDB firm, bringing the total number of MWDB firms in direct partnership with SURS to 32. As mentioned previously, assets managed for SURS by these 32 firms are approximately $9.8 billion, or 41.6% of the Total Fund, as of June 30, 2021.
    - Increase in total assets with diverse firms of approximately $2.6 billion during Fiscal Year 2021
    - Increase in percentage of assets with diverse firms from 36.9% to 41.6% of SURS total assets.

V. Fiscal Year 2022 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.

Implementation of Strategic Allocation Study

As mentioned previously, the Board authorized an updated asset-liability study during FY 2021. With input from Meketa, the Board adopted new policy targets (see Section III for additional information). The new strategic offers an attractive mix of liquidity, drawdown protection, and expected return. The most significant changes in the new policy targets are an increase in the traditional growth strategic allocation and a reduction in the stabilized growth strategic allocation. Implementation activity will begin during FY 2022.

Growth Oriented Strategies

- **Evaluation of Traditional Growth Portfolio Structure –** Staff will work with Meketa to evaluate the current structure of the Traditional Growth portfolio, looking for areas to improve overall diversification and eliminate any unintentional regional tilts.

- **Continued Implementation of Private Credit Allocation (Stabilized Growth portfolio)** Meketa, SURS' private credit specialty advisor, will continue to build out the new allocation, with a goal to commit to four to six funds totaling approximately $500 million during FY 2022.

- **Continued Implementation of Non-Traditional Growth Allocation**
    - **Real Assets** - Staff will continue to work with Callan 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. Recently, the overall asset allocation has changed because of a new study completed by the SURS general consultant, Meketa. As a result, the real assets long-term target has changed from 10% of the total fund to 13% (8% to stabilized growth and 5% to non-traditional growth). Toward these efforts, two commitments within non-traditional growth that were approved in FY 2021 are expected to close in FY 2022 for a total of up to $125 million within real estate and infrastructure.

    - **Private Equity** – The long-term policy target for private equity is 11% of the total portfolio. During FY 2022, Aksia TorreyCove, SURS' discretionary private equity advisor, will continue implementation of the private equity strategic plan. An update to the pacing model is planned in late 2021 and is designed to reach the target level over the next several years. In total, commitments of approximately $550 million are planned during FY 2022.

Diversifying Strategies

- **Education on Potential New CRO Strategies**
  Staff will work with Meketa to research and provide education to the Board on potential strategies to complement the existing long duration (first responder) portfolio. An education session on long volatility tail risk hedging strategies is planned for the September meeting. In addition, other uncorrelated strategies will be considered to provide additional downside protection in the event of equity market declines.

Master Custodian and Securities Lending Provider Searches

A search for master custodian and securities lending provider was initiated in late FY 2021 and is expected to conclude during FY 2022. A custodian is a vital component to the operations, trust and administration of the SURS investment program. Custodial systems provide reliable access to investment holdings, accurate pricing information, and transaction data on a regular and timely basis. Currently, The Northern Trust Company provides custodial and banking services to SURS, and Deutsche Bank provides securities lending services.

Proxy Voting Service Provider Search

A search for a proxy voting service provider was initiated in late FY 2021 and is expected to conclude during FY 2022. The role of the proxy voting service provider is to primarily vote domestic and international proxies on behalf of SURS, based on proxy voting guidelines approved by the Board of Trustees. Currently, Glass Lewis serves as proxy voting service provider.

Investment Policy Review

The Investment Policy was last reviewed and approved by the Board at the January 2021 Investment Committee meeting. Additional review will be conducted and potential revisions to the Policy will be considered during FY 2022.

Diversity Initiatives

SURS will continue to review opportunities in the investment program to consider the utilization of minorities, women 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. In August 2021, SURS hosted its third 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, 21 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 continue implementation of 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 2021, staff negotiated more favorable fee arrangements with eight new and existing investment service providers. In aggregate, these fee negotiations are expected to result in nearly $900,000 in fee savings.

In total, SURS paid approximately $79.9 million or approximately 36 basis points in investment management fees and administrative expenses for Fiscal Year 2021. Total investment management fees for Fiscal Year 2022 are projected to increase by $11.9 million from fiscal year 2021 budgeted fees and include fees paid directly from alternative asset funds. This increase is due to the continued growth of the non-traditional growth 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 140 public, union and corporate employee benefit plans, endowments and foundations with combined assets of approximately $4 trillion. CII is a "leading voice for effective corporate governance, strong shareowner rights and sensible financial regulations that foster fair, vibrant capital markets." Additionally, CII "works with its members to identify and promote effective engagement practices between companies and their shareholders and best disclosure of company policies on engaging with shareholders."

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, women, and persons with a disability.

Key items of note:

- Developed in 2004 to identify and retain MWDB firms
- Managers contract directly with SURS
- Market Value of $5.6 billion, as of June 30, 2021

Asset Class	Number of MWDB Managers	Market Value* as of June 30, 2021	Commitment Amount (Private Equity & Real Assets Only)
Traditional Growth			
U.S. Equity	3	$571 million	N/A
Non-U.S. Equity	3	$1,157 million	N/A
Global Equity	4	$757 million	N/A
Non-Traditional Growth			
Private Equity	9	$297 million	$490 million
Non-Core Real Assets	3	$93 million	$235 million
Stabilized Growth			
Options	1	$346 million	N/A
Principal Protection	4	$1,740 million	N/A
Crisis Risk Offset			
Systematic Trend	1	$447 million	N/A
Alternative Risk Premia	1	$226 million	N/A
Total	29**	$5,632 million	

*Totals may not add due to rounding

**29 firms and 32 strategies due to 2 strategies with 1 private equity investment manager, 2 strategies with 1 real assets manager, and 2 strategies with 1 public equity investment 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 2021 Performance Review

The MDP returned 19.4% for the fiscal year 2021, lagging the benchmark return of 23.2%. The highest absolute returns came from the public equity and private equity managers. GlobeFlex returned 42.3% outperforming their non-U.S. equity benchmark by 658 basis points. The weakest returns came from the Crisis Risk Offset asset class as the trend following and alternative risk premia managers underperformed their benchmarks. In addition, the Franklin Templeton MDP program significantly underperformed their benchmark in the real estate asset class.

Investment Performance*
As of June 30, 2021

	1 Year	3 Years	5 Years	Since Inception
SURS MDP	19.4%	7.5%	8.7%	6.5%
Benchmark	23.2%	10.0%	10.1%	6.9%

*Net of investment management fees

Fiscal Year 2021 MDP Accomplishments

As of June 30, 2021, the MDP is valued at approximately $5.6 billion. A summary of MDP activities follows.

- SURS made private equity commitments totaling $175 million to MWDBE-owned private equity firms, including multiple commitments via SURS' discretionary private equity advisor, Aksia TorreyCove. In addition, an additional allocation was made to an existing account with Fairview Capital Partners, a private equity fund-of-funds provider. Commitments were made to the following funds during FY 2021, although not all had drawn capital by June 30, 2021:
    - Fairview Lincoln Fund I (Series B) ($100 million)
    - Oak HC-FT Partners IV ($25 million)
    - Base10 Advancement Initiative I ($25 million)
    - Avance Investment Partners ($25 million)
- SURS made direct real assets allocations via our real assets consultant, Callan. Commitments were made to the following funds during FY 2021, although not all had drawn capital by June 30, 2021:
    - BIG Real Estate Fund II (lesser of $50 million or 10% of total commitments)
    - Newport Capital Partners III (lesser of $30 million or 10% of total commitments)
    - Ember Infrastructure Partners Fund I (lesser of $50 million or 10% of total commitments
- SURS initiated its private credit program in 2020 and committed $50 million to Crayhill Capital via private credit consultant, Meketa.
- SURS hosted the 3rd Annual SURS Diverse Manager Week event.

SURS' commitment to diversity extends beyond the bounds of the MDP. In addition to the 29 firms utilized in the MDP, SURS contracts with three additional MWDB firms, bringing the total number of MWDB firms in partnership with SURS to 32. 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 32 firms are approaching $9.8 billion, or 41.6% of the Total Fund, as of June 30, 2021.

Fiscal Year 2022 MDP Initiatives

Plans for the MDP in FY 2022 include the following:

- Expand industry outreach efforts
- Host the 4th 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 2022 Board meeting
- Identify potential opportunities to increase funding to existing qualified investment managers
- Continued interaction with system consultant, Meketa, via more frequent discussions regarding MWDB investment managers

VIII. Defined Contribution Plans

Retirement Savings Plan

The Retirement Savings Plan (RSP), formerly called the Self Managed Plan, is a 401(a) plan type defined contribution option available to SURS members. The RSP has grown steadily since the plan's inception in April 1998. Highlights of the plan include:

- Approximately $3.9 billion in assets as of June 30, 2021
- RSP forfeiture assets were $149 million as of June 30, 2021
- Disability reserve assets were $13 million as of June 30, 2021
- Administrator and recordkeeper
    - Voya Financial ($3.4 billion of plan assets)
- Legacy service provider
    - TIAA ($394 million of plan assets)
- Custom lifecycle solution, the SURS Lifetime Income Strategy (LIS), managed by AllianceBernstein
- 16 investment options as of June 30, 2021, including the default option of LIS.
- Over 22,000 Participants currently invested
    - 14,188 active participants
    - 8,463 inactive participants

Deferred Compensation Plan

The Deferred Compensation Plan (DCP), is a new supplemental defined contribution 457(b) type plan created in Public Act 100-0769. This plan became available to SURS members beginning in March 2021.

- Approximately $237,000 in assets as of June 30, 2021
- Administrator and recordkeeper
    - Voya Financial
- Custom lifecycle solution, the SURS Lifetime Income Strategy (LIS), managed by AllianceBernstein
- 16 investment options as of June 30, 2021, including the default option of LIS.

Fiscal Year 2021 Defined Contribution Accomplishments

- Completed transition to the new administrator and recordkeeper, Voya Financial, for the RSP.
- Approved new lineup of investment options for the defined contribution plans, streamlining the number of options from 29 to 16.
- Worked with AllianceBernstein to create a custom lifecycle solution with a guaranteed income component (SURS LIS).

- SURS was recognized by industry publication Pensions and Investments with an Eddy Award for communications excellence in the category of plan conversions.
- SURS was a finalist for the 2021 PLANSPONSOR Plan Sponsor of the year award.

Fiscal Year 2022 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.
- Continue the roll out of the Deferred Compensation plan to eligible SURS covered employers.
- Prepare for automatic enrollment of new members into the DCP plan as of July 1, 2023, as outlined in SB2301, which is expected to become law.

Appendix A

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MEKETA
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MEMORANDUM

TO: State Universities Retirement System of Illinois ("SURS")
FROM: Colin Bebee, CFA; David Sancewich; Ghiane Jones; Neil Rue, CFA;
Meketa Investment Group, Inc.
DATE: September 9, 2021
RE: 2020/2021 Asset-Liability Study – Evolving Policy Plan

Recommendation

Meketa recommends that SURS adopt the Evolving Policy Plan presented on page 2. This Evolving Policy Plan pertains to the planned transition of the SURS portfolio to the recently approved long-term strategic allocation policy targets.

Summary

At the June 2021 meeting, the SURS Board approved a new long-term strategic allocation policy. As an investment portfolio with over $23.5 billion in assets, transitioning from one strategic allocation to another requires appropriate planning, and in most cases, several stages of transitions in order to prudently shift the investment portfolio to the new long-term strategic allocation targets.

The Evolving Policy Plan that is presented on the following page was designed to transition the portfolio to the new long-term strategic allocation targets in a smooth manner without material increases or decreases in the portfolio's aggregate risk/return posture or individual class allocation levels. Moreover, the proposed Evolving Policy Plan was designed in concert with the currently anticipated private markets pacing plans. This plan steps into the new allocations in a systematic and prudent fashion. It is important to note, however, that the plan may be modified over time as the cash flows associated with funding private markets are difficult to predict as well as due to general market dynamics. As a result, Meketa and the SURS Staff will review the Evolving Policy Plan on an ongoing basis and update accordingly.

Evolving Policy Plan

	Current Policy				New Policy
	7/1/2021	7/1/2022	7/1/2023	7/1/2024	7/1/2025
Traditional Growth	40.0%	38.0%	37.0%	36.0%	35.0%
Stabilized Growth	21.0%	17.0%	17.0%	17.0%	17.0%
Core Real Assets	4.5%	5.5%	6.5%	7.0%	8.0%
Options Strategies	4.0%	2.0%	2.0%	2.0%	2.0%
Liquid Credit	12.0%	8.0%	5.5%	4.0%	2.0%
Private Credit	0.5%	1.5%	3.0%	4.0%	5.0%
Non-Traditional Growth	11.0%	13.0%	14.0%	15.0%	16.0%
Private Equity	8.5%	10.0%	10.5%	11.0%	11.0%
Non-Core Real Assets	2.5%	3.0%	3.5%	4.0%	5.0%
Inflation Sensitive	5.0%	5.0%	5.0%	5.0%	5.0%
Principal Protection	8.0%	8.0%	8.0%	8.0%	8.0%
CRO	15.0%	19.0%	19.0%	19.0%	19.0%
Total Illiquid Assets	16.0%	20.0%	23.5%	26.0%	29.0%
Total	100.0%	100.0%	100.0%	100.0%	100.0%

Key Takeaways

- During the summer months of 2021, SURS Staff increased the policy allocations of *CRO* from 10% to 15% and *Non-Traditional Growth* from 10% to 11% with corresponding policy reductions of 1% coming from both *Inflation Sensitive and Traditional Growth* and 4% coming from *Stabilized Growth*. These incremental changes were discussed at the June 2021 meeting and were in-line with prevailing allocation ranges per policy.
- During the current 2022 fiscal year, the allocation to *CRO* will increase from 15% to 19% and the allocation for *Stabilized Growth* will decrease from 21% to 17%. By the end of the fiscal year, *Stabilized Growth*, *Inflation Sensitive*, *Principal Protection*, and *CRO* will be at their new long-term strategic allocation policy targets.
- Over the next three fiscal years, there are two remaining transitions, both of which will be continual and deliberate:
    1. A reallocation of growth-oriented assets from *Traditional Growth* (i.e., public equity) to *Non-Traditional Growth* (i.e., high return-seeking private markets).
    2. A reconstitution of *Stabilized Growth*. The assets that make up *Stabilized Growth* will generally transition from public markets (i.e., Options Strategies and Liquid Credit) to private markets (i.e., Core Real Estate and Private Credit).