EPISODE 71:

Investing in the Future

with the North Dakota Retirement and Investment Office

Robert Morier: Welcome to the Dakota Live! Podcast. I'm your host Robert Morier. The goal of this podcast is to help you better know the people behind investment decisions. We introduce you to chief investment officers, manager research professionals and other important players in the industry who will help you sell in between the lines and better understand the investment sales ecosystem. If you're not familiar with Dakota and our Dakota Live! content, please check out dakota.com to learn more about our services. This content is provided for informational purposes and should not be relied upon as recommendations or advice about investing in securities. All investments involve risk and may lose money. Dakota does not guarantee the accuracy of any of the information provided by the speaker who is not affiliated with Dakota. Not a solicitation, testimonial, or an endorsement by Dakota or its affiliates. Nothing herein is intended to indicate approval, support, or recommendation of the investment advisor or its supervised persons by Dakota. Today's episode is brought to you by Dakota Marketplace. Are you tired of constantly jumping between multiple databases and channels to find the right investment opportunities? Introducing Dakota Marketplace, the comprehensive institutional and intermediary database built by fundraisers for fundraisers. With Dakota Marketplace, you'll have access to all channels and asset classes in one place, saving you time and streamlining your fundraising process. Say goodbye to the frustration of searching through multiple databases and say hello to a seamless and efficient fundraising experience. Sign up now and see the difference Dakota Marketplace can make for you. Visit dakotamarketplace.com today. Well, I am thrilled to introduce our audience today to Scott Anderson, Chief Investment Officer of the North Dakota Retirement and Investment Office. Scott, welcome to the show.

Scott Anderson: Thank you. I appreciate being on.

Robert Morier: Well, we appreciate you being here. And as always, I want to welcome my partner on the desk, Tim Dolan, from Dakota. Tim, welcome back.

Tim Dolan: Of course. Thank you for having me.

Robert Morier: Thank you for being here. We look forward to asking Scott a number of questions. But before we do, Scott, we're going to read your biography for our audience. Scott Anderson is the Chief Investment Officer for the North Dakota Retirement and Investment Office, which coordinates the activities of the State Investment Board and the Teachers Fund for Retirement. Scott joined North Dakota from American Family Insurance, where he was managing director of Corporate Development and Mergers and Acquisitions. Prior to American Family, Scott spent nearly five years at the state of Wisconsin Investment Board, where he was managing director of Asset and Risk Allocation. Before moving to Wisconsin, Scott was director of Performance and Risk Investments at American Family for nearly 10 years. And before that he spent seven years as a senior manager at Deloitte. Scott earned his bachelor's degree in electrical and computer engineering and an MBA from the University of Wisconsin at Madison. He is a CFA charter holder as well. Scott, thank you for being here and congratulations on all your success. We are really excited to ask you questions about everything you've been working on. We know you've been quite busy, so thanks for the hour.

Scott Anderson: Well, thank you again for having me.

Robert Morier: Well, for our audience who may be less familiar with the North Dakota Retirement and Investment Office, would you mind setting the stage for us as it relates to an overview of the plan?

Scott Anderson: Sure. I'd be happy to. So, our organization is the North Dakota state government, but we are the Retirement and Investment Office within the North Dakota state government. And within the Retirement and Investment Office, we have benefits administration of the Teachers Fund for Retirement. And then we have the Investment Office. The Investment Office invests on behalf of 29 client funds. We have the TFFR pension… Teachers Fund for Retirement… the Public Employee Retirement System, other pension funds, such as the city of Bismarck. We also have a very large endowment-like structure, the Legacy Sovereign Wealth Fund, which is kind of an interesting and exciting opportunity for us going forward as it's growing. And then we have the Workforce Safety Insurance portfolio, as well as various other funds. We have about $21 billion of assets under management currently. But again, growing the legacy fund itself is growing almost at $1 billion a year in contributions not counting returns. Our investment organization has a team of eight investment professionals. And we're also improved to increase our staff to 13 by the end of the year, and that would be to accommodate an internal direct investment program. And what that is… is to invest some of our portfolios directly rather than through external managers. So that's just a broad overview of the content, the benefits administration, the investment office, and our general structure and client funds.

Robert Morier: It sounds like you've got a lot going on this year. So, we look forward to digging into what some of those agenda items are going to look like more specifically. But before we do, take us back to Madison. You studied electrical and computer engineering. Every good engineer has a plan. What was your plan?

Scott Anderson: Well, you know, it's interesting, I've always been fascinated by technology. And I try to think about why that might be. And I remember I grew up in the era where there were a lot of space activity… landing on the moon, et cetera. Even in second grade, we had a reader where some little boy's father was a computer scientist and helping his son program a computer. And I was fascinated by that book. And then I followed technology. And I remember one year… it must have been maybe 1976, when I was about an eighth grader, looking at a popular electronics magazine and there was this article about this cosmic elf 1365 chip. That was the really early days of micro computing.

And I said, man, I have to have one of those. So, I mowed lawns. And eventually, about a year later, I was able to acquire my own TSR 80 computer, 16K ram. And actually, I got so into it I was coding machine code to operate the computer early on. I started high school. There was a computer program in high school. In high school I was ahead of what they were doing, and so they gave me independent study. And then they had me… they were taking me around the state and programming contests and all kinds of stuff like that. That said, there's another thread in my life is that I come from an entrepreneurial family. So, my father had a business and that's where I was mowing the lawns and then later performing other activities for the family business. And so, I was always very interested in business, and I always was following the markets. Even in college, I was following the markets and the market page in the newspaper. My roommates would even tease me about that. I had a plan in mind when I was in undergrad for electrical and computer engineering, that I would go on for my MBA. That was somewhat of a popular career back then. Getting a technology engineering degree and then getting an MBA. And so, I had that in mind. And really, I was even taking economics classes and I took a… when I graduated, I took an accounting class. So, I was preparing myself for that MBA path anyway. But my first job out of school was with AT&T. This was right after deregulation of telecom. And I was designing and developing telecommunications systems. And that was… for the engineers out there listening, that was Unix internals back in the early days of Unix. So, we were actually developing… it was a real-time fault tolerant operating system that operated the telecom network. And I was coding up basically the code that was the operating system for that telecom network. And that was a really good experience, but I only did that for two years and I transitioned into business. So, the bottom line is I had a thread of technology throughout my career. And then I've had a thread of business and markets throughout my career. And it's interesting how those two have converged. And even this idea in technology about technology being used to communicate faster and better, technology used to process, solve problems faster and better. And then thinking about information and really the whole investment industry relies on having advantages in acquiring and processing information. So that sums up how I got there.

Robert Morier: No, that's helpful. Thank you for sharing that. I teach at that intersection of engineering and entrepreneurship, so there's a lot to be gleaned from that. But when you think about all of your experiences leading up to North Dakota, that intersection of those familiar aspects of those roles through the years, what have you put together, if you will, to take you to North Dakota today? What are some of the experiences that you gleaned and have taken with you?

Scott Anderson: Yeah, so when I think of that, I think of maybe three, four major… four major buckets. It would be my engineering experience, my Deloitte experience, my American Family experience, my state of Wisconsin Investment Board experience. All of those really converged to enable me to take on this opportunity here at North Dakota.

Engineering… that was information technology and somewhat of what I was saying before that it allows us to solve problems and communicate in ways that can't be done with a pen and paper or even with face-to-face communication. Although I believe that human element and that face-to-face communication is actually very critical as you progress in your career and really determinant of success. But think of the Stock Exchange and the speed of light communication that's required for the Stock Exchange and decision making to determine prices. Or think of Excel workbooks or Python notebooks and what's required there in order to even solve investment problems. So that engineering platform of my career really followed me throughout my experiences and enabled certain successes for me. The Deloitte experience, I'll say was a really, really important transition for me in the sense that it was almost like a polishing experience for me because I joined an organization that was… their global consulting practice. And I was in their global strategy consulting practice. And Deloitte has some of the most talented professionals in the world and it's designed as an organization that helps other organizations create strategies and change. And so, I learned that whole process. So, the consultant process taught me strategy, how to look forward to your goals and then reason back, and what steps are required to achieve those goals, whether it's in a work plan or implementation project or even personally. It also taught me a transformation process. So, I think, subsequent to Deloitte, I see everything as really a continuous transformation process. And there are certain kind of repeatable activities in the transformation process that enable an organization to achieve a higher level of capability, but then to sustain that higher level capability in a competitive market. So that was really helpful for me.
At Deloitte, I was involved in a lot of high-level growth strategy, M&A. And then as a result of the M&A trading and risk management, Deloitte taught me a very rigorous due diligence process for acquiring a company. What are the value drivers of a company and then even what's required once you acquire a company to make sure that that company performs at a higher level than what you acquired it for because you got to achieve a value to pay for the cost of the transaction. And then lastly, Deloitte introduced me to trading and risk management, which I found to be an incredible foundational technology enabler for an investment organization. I often say to our board, investments are operations, operations are investments. So, you have to have a methodology, but that methodology, because of the complexity and the amount of information that needs to be processed, needs a really solid infrastructure and that infrastructure is a trading risk management system. So, I'm saying a lot about the Deloitte experience because that really shaped how I interacted with the business world after that. And then at American Family Insurance, that really is where I learned the nuts and bolts of an investment organization. So how do you manage cash flows, asset liability management, portfolio construction, derivatives overlays, manager selection, monitoring and termination, active risk management, fund level portfolio management, insurance and pension allocation, managing funds with a combination of internal/external managers, hiring, managing and retaining a team, all the skills that I think were necessary to learn to become a chief investment officer. I think many professionals, particularly technical professionals, kind of

get caught in a silo, and that's OK if they want to only excel at their technical or functional role. But if they want to expand beyond to higher level, senior level management, I think it's critical for them to know that the people skills, the managing skills, the leadership skills, the interacting with stakeholders' skills really are what's required to succeed at those higher levels. So, what gets you there is necessarily what's going to get you to the next… next level. And this was an experience to me that helped me with those sorts of capabilities. I also worked on some corporate development M&A activities because I had this M&A background. And so American Family itself was going through a transformation when I joined. And I think the organization recognized my skill for that. So, I was involved in other activities like M&A activities. And that later led to my coming back to American Family Insurance as managing director of Corporate Development M&A. And we completed an acquisition of Ameriprise's home and auto business and some insurance tech while I was there as a managing director of corporate development M&A. That was one of those experiences where I took all what I knew and applied them. And so, it was a learning experience for sure. It was one where I was actually harvesting my learnings from earlier experiences. I would say the state of Wisconsin Investment Board is another one of those real important experiences for me. And that here the scale was so much bigger. It was about $120 billion pension plan, plus it had maybe like a $12 billion cash portfolio, plus it had a few other billion dollars in various funds. And my role there was as managing director of asset and risk allocation, and so I was responsible for plan allocation, its implementation, allocation of capital to active strategies, policy portfolio implementation. I had a quant team. I was responsible for exposure management. Exposure management is tilting the fund in slight ways towards equity or fixed income based on changes in capital market assumptions. And managing active risk derivatives… I was responsible for the derivatives portfolio. I had an index team for a time. So, we had a large equity index portfolio. And I had a risk arb team report to me for a time. And the risk arb team evolved out of the index portfolio. As you learn what the corporate events are going to be, and an index portfolio are able to take that information and then use that to construct a risk arb portfolio. And so that was a successful portfolio. And I was very fortunate to have a very talented team working for me. I was also the front office sponsor for a large organization-wide transformation project. And so there, again, this is where both my technology background, but more importantly my Deloitte strategy and transformation background, helped. So, I think they saw that and so the managing directors was the front office sponsor for that particular project. It was a large project. It was about a $50 million transformation project from the back office through the front office to upgrade our capabilities. So, I'd say all my previous experience were put to work but at a much larger scale in a much more complex and sophisticated way. So, we had a large-levered allocation. $120 billion plan that was levered. So, we actually levered the allocation. We got the best return per risk at the plan level. And then we leveled… so we were traveling along the capital market line, so we leveraged it to get the right return. So, it's a way of getting a little bit more efficient as a plan.

We also had some really sophisticated internal investment strategies. So, we even had an internal hedge fund that we were operating… or they still operate at state of Wisconsin Investment Board. So, I think all my experiences led up to that. But then when you come to this North Dakota, now I've got this set of skills that's transformation. But I come to North Dakota, and it just is at the point where it can start to take advantage of some scale economies. My mission, since I've been here, is to help move the North Dakota plan to the next level. It's really blessed with 29 client funds and $21 billion and growing. And in a way blessed with the fact it's kind of had a clean slate. It doesn't have some of these 30-year-old processes that you have to take down and put winds up. We can actually just put the best practice processes in place right away. And that's what we're working towards doing. So, it's an exciting… exciting opportunity. So, if I summed it all up, it's technology, business strategy, fundamental investment skills and education, quantitative investment skills and education, the transformation toolkit, portfolio and risk approach to investing, leadership and stakeholder management, including boards. All those experiences are what are required if you want to be a performing chief investment officer. And you can't forget that all of it has to be done with and through other people. So probably the most critical thing is to make sure you're working with really talented people. So, talent management is a high priority for me. I mean, I realize that any of my successes are due to the governance structure around me and the people that are working with me.

Robert Morier: Thank you for sharing all that, Scott. It was very helpful. And it sets the stage for us, particularly when we think about how you prioritized all of these initiatives. So, you have a blank slate. You're able to go into something relatively clean, which is unusual for a state pension plan. So how did you set those priorities out? When you sat down at the desk for the first time, just about two years ago, what were the objectives and how did you go about prioritizing which came first?

Scott Anderson: So, going back to that Deloitte experience, look forward and reason back. So, the best I could do is when I look across the states… and I've been exposed to a lot of public plans… and I would think state of Wisconsin Investment Board is the best or at least one of the best for sure plans in terms of its sophistication and in all aspects. And so, I looked at that as kind of a model you want to get to. Then I reasoned, well, where are we now? Well, we're kind of in a model where we're a little bit like a city plan where we have a board. It's an appointed board. And we have a lot of consulting help. And when I landed, we only had two investment professionals here. Great, very talented investment professionals, but understaffed. So, we get from this kind of almost procurement funds management organization to an advanced funds management organization to something more like state of Wisconsin Investment Board, which is an asset and risk allocation organization. So, what makes a really good public fund investment organization, it starts with governance. And then the next part that really makes a good public pension plan is talent management. And then once you have the talent, well, they have to have operations and infrastructure that enables them properly. And then lastly, and certainly not least, there needs to be a really strong investment analyst culture. So, it can't be more of a procurement culture relying on others' decisions or relying on… over reliant on consulting advice. It needs to be able to analyze the markets and rapidly make high quality investment decisions itself and always being focused on trying to improve the performance of the plan. So, this culture thing is really important. So, governance… the best practice for governance would be to have some board committees so the board can focus on particular topics for a transformation. And this was already in the works when I joined, created a governance committee. And from the governance committee, we created an investment committee. Now, we had such a small set of staff, that we couldn't have a staff-led investment committee. So, we created a hybrid committee. So that was a couple of board members… me, the deputy CIO, and a couple of external professionals that could bring in some professional advice, a couple of professors from local universities. So, we've got this hybrid investment committee, very critical committee for us to perform. We had an executive review committee, but we appended to that a compensation committee that enabled us to look at the talent management opportunity. We have a very functioning internal audit function within RIO, Retirement Investment Office. But we recognized, looking forward and reaching back, if we're going to take on more sophisticated investment processes, we're going to have to beef up our internal auditing capabilities. So, we hired an external consultant to help us look at our internal audit processes. We're building the capabilities we're going to need then. Now we hired a chief risk officer. In order to have good governance, we have to have a good chief risk officer. We hired a chief risk officer from Invesco. So that's the governance layer. Talent management layer is to introduce and get approved an incentive comp plan. Also, to identify what our organization structure should look like, what the roles are, and make sure we have the right people on board. So, we moved from two people when I landed to eight people now. And then we went through a legislative process to come up with another five people to be at about 13 people at the end of this year. And that will get us to that advanced fund management stage. Operations… we're in the process of acquiring a portfolio management system, order management system. We already have a very sophisticated risk management system… actually a couple of them. And we already have a private market system. But we're creating an infrastructure that's more integrated and one that can enable us to have internal direct investment strategies. And in addition to that, a data warehouse so that we can bring all this information together and then we can use more advanced tools, machine learning. And to the extent that it can be leveraged in an investment process, we'd be open to AI types of tools to the extent that they can help us. I don't think AI tools would help us make investment decisions. But I think they would help us process information and manage our operations in a more efficient way. And we actually have a state drive to incorporate AI tools into our processes where possible. Our governor is the former CEO of Microsoft's Business Solutions practice. And so, the entire state is very commercial-oriented and very focused on being innovative and transformative.

Robert Morier: Well, you can definitely ask AI to help you with your to-do list because it is unbelievable how much is going on. But it's exciting for us to hear about. Thank you for sharing all that.

Tim Dolan: Scott, as we segue and transition into the investment operation there at the plan, I'd love to just touch on a little deeper on the investment team. Obviously, you've hired some individuals. You touched on that, that capability of investment analysts. Have you broken out areas of coverage or focus for these new individuals?

Scott Anderson: I call them verticals. And the way to think of it is that we have an investment organization. We have a risk vertical. That's an active risk management vertical that's involved in all our investment decisions. So, it's helping… assisting quantitatively with portfolio analysis, but also looking at the various risks of various investment decisions. We have a public markets funds management vertical. So, this would be a vertical that's responsible for selecting and monitoring. And we're required terminating external investment managers. So, it builds this external investment manager portfolio to optimize active return for active risk with external managers. We have a private-markets vertical. The private markets vertical is responsible for all things private markets. Now, clearly, you get to areas like private debt, there's kind of an overlap in terms of private markets and public markets. And that's where we work in a very coordinated way. And then lastly, we're just starting to build our internal direct vertical. So, this internal direct vertical would have an equity portion of its responsibility, internal portfolios, a fixed income portion of its responsibilities, and then a funds management kind of overlay responsibility for itself. And so all of those combined enable us to do some things that we wouldn't otherwise be able to do. I think the advantage that we have as a funds manager is that we're getting information from all kinds of managers regarding what is the market, what strategies are performing well or not performing well. And we also know the various returns and risks of our managers, but our managers don't know the returns and risks of all our other managers. So, we're the ones that really have to be responsible for constructing our portfolios of this fund of funds managers making sure that they're at the right size and have the right performance from an active return per risk. But at the same time maintain fidelity with our overall asset allocation because we think that's our number one source of return and risk. So, we're really, at the end of the day, an advanced funds management organization that uses advanced techniques for portfolio construction and optimizing the performance of our client funds. So that's kind of the layout so. So, within the public markets vertical, we have our deputy CIO. We have a senior investment officer, and we have an investment officer. Within our risk vertical, we have a chief risk officer and a risk officer. Within our private markets vertical, we have two senior risk officers. They have a big agenda. They're very busy. And then for the internal direct, we'll have two portfolio managers… an equity and a fixed income portfolio manager… two analysts… an equity analyst and fixed income analyst, and then a funds management analyst.

Tim Dolan: Now, that's an insanely helpful overview, and obviously a lot of thought and consideration have gone through each of those verticals. So, thank you for that overview. Can you touch on any relationship you may have with an outside consultant in regard to the investment process? Do you work with anyone helping you vet managers or source ideas from an outside manager standpoint?

Scott Anderson: First of all, we always use an investment consultant when we allocate for a particular fund. But we're very active in developing what our methodology is and making decisions regarding what our asset allocations are. And then they're finally approved by the investment committee and the board. So, it goes through a governance process. So, it's not just a consultant that would make an asset allocation decision. They would bring to us what their capital market assumptions are and some modeling, and then we'd work through various alternatives. Regarding manager selection, as you move from being kind of a city-sized fund that's smaller, a few billion dollars, to an advanced funds management organization to something even larger, there's kind of a natural evolution in terms of your use of consultants. I think when you're a very small plan, you have very few staff, and you act more like a procurement organization than you do like an investing organization. RIO, when I landed, was more of a funds management organization where it was actively searching for its own managers, then asking the consultant regarding you know what their thoughts are for the manager. We're carrying that process forward, but I think we're becoming even a little bit more advanced in terms of when we look at managers, we look at, in perhaps a more sophisticated way, how a manager would impact our portfolio construction. And then we've developed some tools both to identify the large set of managers and then also to screen through those managers quantitatively and qualitatively and then select particular managers. And our criteria are not just does that manager by themselves perform well, but how will that manager perform systematically in our portfolio? But even more importantly yet, because we can adjust some of those systematic risks, is how does that manager perform in our portfolio construction? In other words, how do we maximize our active return for risk with a portfolio of fund managers? So, you want to have a diverse group of managers that don't all look the same, that you don't crowd particular securities. An example I'd give you, if you have a large set of highly concentrated managers, let's say, in the active space, either they all look the same, or if they look different, you're going to end up with the index anyway. So, you have to be… you have to create kind of a diverse portfolio of managers, and that requires portfolio construction thinking. And so, when you're looking at a manager, you have to think through those issues. An external consultant isn't really going to help you make those kinds of decisions.

Tim Dolan: No, that's great, and obviously, having that in-house capability and expertise allows you to support that investment process. Can we dig a little deeper into that underwriting process? So, when an investment firm or salesperson or a portfolio manager calls on you and your team, what does that underwriting process look like? And how long does an investment decision typically take before you ultimately get comfortable and make an investment?

Scott Anderson: There's a selection process, a monitoring process, and a termination process. And that's important to understand because that impacts who might be a candidate as a manager and the timeline of that candidate as a manager. We always say if you want to buy something, you've got to sell something. If you want to sell something, you've got to buy something. So, we've got a portfolio… hopefully, when take on a manager, we're going to have a relationship with that manager for a long time. So, it's either the manager has not performed well, or we've grown to an extent where we can build out our manager portfolio a little bit more because of our scale. So, because of that, most of our processes are search processes. We'll look, hey, we want to build out our private debt portfolio in the legacy fund. We make a decision like that. I'm saying this qualitative… we make a decision like that. Well, then what we're going to do is we're going to look at our database of all the private debt managers. And then we're going to use some of our tools to screen based on what we think are critical performance statistics historically and consistency of performance over time to make a decision of which managers might get into that pool. Now, there potentially could be managers that have a shorter history, and they look interesting. And so, we might include those in the pool as well. Or there could be managers that we've met at various conferences and through networking, et cetera, and in which case, hey, remember we spoke with this manager. And they're doing this kind of work in this area. Hey, why don't we put them on the list and at least have a conversation and see what they can deliver? So that's generally how a manager kind of gets incorporated into our process, and that process can take several months. Now, if we meet a manager at a conference or we see a manager maybe in our database accidentally in a certain category that seems to be performing well… we're kind of watching that manager… it could take years because we may not have a reason for switching managers. We might have a really good portfolio of managers, and it might just not be worthwhile to go on a search for someone to replace our existing good manager. In other words, if we're going to sell our existing good manager, that bar is really high for a manager to replace them. So, it could either be months, if we have a search process, or it could be years if we don't have a specific place in mind for a given manager.

Tim Dolan: No, that's great, and, Scott, our audience is largely investment sales professionals across all asset classes, across tenure, size, boutique, emerging, the brand names. Can you give us some insight? What is the best way to approach you and your team in terms of reaching out, coming to town, doing meetings, doing Zoom? Are you all traveling as well, going onsite to meet with managers? But let's just start with what's the best way to get in front of you and your team. My email box is so full. People I know very well and interact on a day-to-day basis, once in a while I miss a message. So, it's really difficult to just get a random email from someone. In fact, I've got two email boxes. The state has kind of set it up to have kind of two tiers… people you interact with frequently, people you don't interact. I don't think ever look at that other email box, and it's not that an investment manager that I haven't met is not important. It could be the most important manager in the world to me if I knew them, but it's really difficult to speak with them through email. Also, by phone, voicemail or voicemail box gets so full with calls that it's just difficult. I think the best place to meet up with managers we haven't met with are at various conferences. If I'm at a conference, and I see a manager, and they're presenting, and they have something really interesting to say, that will catch your eye. Or occasionally, we might be at a conference, and we might be talking with someone who says, hey. Have you met this manager? And they might introduce us to them, and we'd say, OK, I'll talk with them. In which case, many times we've set up like a Teams meeting and had an initial conversation. But we always say, look, what your strategy is, is something we already have in our portfolio. And we have a really good manager now. Your performance is comparable. Your performance is better, but whatever. We basically would say it's a bit bar for us to make a decision to change a manager, bring you into our portfolio. So, it's a longer process when it goes through a channel like that. The best way I think a manager, perhaps, could be reached by us is that they perform really well. They show up well in the databases, and they show up at conferences. And they're recognized, and they have a top-notch management team. And they have a really good reputation in terms of their operations and approach to the market. And I think based on that, then when we are making a search, they would likely show up on our list. And if they're really good, we might hire them. And they might be happy by that because if they really are that good, then they know if we do hire them, they'd be in our portfolio for a long time. And any manager we hire is a partner of ours. So, we're partners. We're giving capital to them. So that's more than just an arm's length kind of relationship. We meet with our managers at least twice a year and have plenty of conversations with them. And they fulfill a very important part of our portfolio. And so, as such, they're partners of ours, and so they tend to be sticky.

Robert Morier: Scott, you mentioned earlier… specifically, you stressed the importance of private markets, and you used private debt as an example as well. You've got $1 billion in contributions coming in annually. So how do you see the role of private equity evolving in the overall portfolio in the coming years?

Scott Anderson: We're in a unique situation. Our pension plans are fully allocated to private assets. So, we've got, oh, gosh, about 30% private assets in the pension plan… maybe 4.5% in private debt, maybe 7% private equity. It varies a little bit by pension plan. We've got 11% real estate, and we've got 8% infrastructure with maybe a 1% timber. So, we're pretty full in our pension plans. Within our legacy fund, though… it's our sovereign wealth plan… it was allocated to be a very liquid plan early in its life. And we just completed an asset allocation this last year which would require us to build out more private assets in that portfolio. So, we're in a unique position where we've got a lot of what I call green capital. It's not capital that's turning over over long periods of time with a consistent asset allocation. We actually have to grow our private assets in the legacy fund, and so we're actively doing that. The team is out looking for managers. We also, in the last year… say, like 2022… we had a kind of a swoon in the public markets. And when that happens, you have something called the denominator effect. That's when, of course, the private assets don't have the same kind of drawdown that the public assets do, and so you become over allocated. That's lessened quite a bit. In fact, we're pretty close to our targets with the exception of, I think, we're maybe just a little bit over allocated in private equity. But one of the options, given the legacy fund that we've looked into, is creating something like a master trust where you put all of our private assets in a master trust, and we unitize. We can have the same private equity, real estate, and infrastructure allocation across all our plans. And then we could have a fund like the legacy fund, potentially. This is not in place yet, but we're exploring. This potentially could buy units into this master trust. And that would give it access to vintage years that otherwise wouldn't have access to, and it also would then relieve the pension plans of their over allocation. In the pension plan, I mentioned that we have the real estate, the infrastructure. We probably have a larger infrastructure portfolio than most plans already. So, we have about 8% infrastructure. We look at comparable plans, I think we're maybe 4% more than many plans have. And that's benefited us over the last couple of years. Private debt, I think we were early into the private debt allocation. So, we've had a private debt allocation in the pension plans for a bit, and that's benefited us. When I look at, within the private equity funds, we're at about 25% venture capital. I would say that our go-for-it plan would be 25% or less, probably. You're always going to want some venture capital. It's an important part of our economy and has become an increasingly important part of our economy. But the challenge with venture capital is the track record for venture capital investments on a risk return basis hasn't been great. So, you really have to be careful when you invest in venture capital to get a really high-performing manager. And sometimes getting access to those high-performing managers is not easy. So, I think we want to be… we want to allocate capital to private markets where we feel that we're going to get an advantage of in private markets over public markets. We think of private markets as a strategy as opposed to an asset class. And so, we want to allocate capital to private market investments only when we feel confident that private market investment is going to exceed the return and risk characteristics of the public market asset classes.

Tim Dolan: No, very helpful overview, and obviously, across those asset classes, even within private equity, hearing that allocation of venture, I'm sure a lot of our listeners, their ears perked up, which is good. And again, going back to my comment, a good amount of our audience, again, are working with brand name funds, some of the larger ones. But a lot of them are working at some either newer one… boutique… which leads me into the emerging manager conversation. We see a lot of your state pension peers have a dedicated emerging manager program, certain qualifications. Maybe to start higher level, do you all, one, have an emerging manager program? And if so, what is your definition of an emerging manager? And then we'll go from there.

Scott Anderson: Let me make a distinction. We have the legacy fund, and we have an in-state investment program. And within that in-state investment program, we have an equity sleeve, a private equity sleeve. And within that private equity, it's meant for growth capital in the state of North Dakota. So, we do invest in, I would say, earlier stages of companies in North Dakota. And a lot of those managers are what I would call emerging. The general philosophy we have is that a manager has to have a track record. Now, it could be a new entity with principles who have a track record that they're taking with them that we might be interested to take a look at. But it's really difficult, particularly in the private markets. We're fiduciaries. We've got to get the best benefit on behalf of our beneficiaries, the best return per risk at an appropriate level of risk of comparable assets. And so, it's difficult to justify, well, let's just kind of shoot from the hip, and, hey. They're new. I kind of like these guys, so let's just invest in them. And we really have to have a rigorous underwriting process and know why… what the sources of value of the particular manager is, and what's the likelihood of that manager providing a durable return stream? And then what are the capabilities of the manager even of managing itself in terms of its operations? How does it interact with custodians, and what are its accounting processes like and those sorts of things? So, the bottom line, what I'm saying is, we don't make a distinction regarding emerging manager. We look at any manager we felt had some justification for being a high-value manager in our portfolio. But a new, new manager, one who doesn't have a track record, hasn't invested before, has a really steep hill to climb to be in our portfolio. And we really… on behalf of our beneficiaries, we have a hard time not having that as a requirement.

Robert Morier: Before we let you go… on the asset allocation side, I did want to ask you about your exposure to hedge funds. I'm just curious what the hedge fund mix looks like today and just your general thoughts and outlook on those types of hedge strategies as you think about the overall portfolios.

Scott Anderson: Yeah, thank you. We do not have hedge funds in our portfolio. We do have some very sophisticated, what I call kind of quantamental managers in our portfolio. And they're larger managers with very strong technology enablers and… but their processes are based on some sort of fundamental factor model. And we do have those in our portfolio. When I was at State of Wisconsin Investment Board, we had a sizable hedge fund portfolio. And I'll say that some of the most sophisticated investors are hedge funds. So, I respect what they do, and a lot of them have a lot of capability. The challenge I have with hedge funds is it's a difficult asset group or strategy to allocate to. So again, if we want to buy something, we've got to sell something. So, if I want to put hedge funds in our portfolio, I've got to sell some other systematic risk to put the hedge fund in. Hedge funds typically have a lower return. So where does it fit into the portfolio? So, I think what we discovered at State of Wisconsin Investment Board, perhaps a better strategy is you have an asset allocation. The asset allocation is your systematic risk, and you separate what we call beta or the systematic risk from alpha. And then we build alpha either with physicals, with liquidity risk like in private markets, or we port a hedge fund portfolio onto our asset allocation in the right size, so we get the right active return per risk. If we were to pursue a hedge fund strategy here at North Dakota, I think that's what I would advocate because it's very difficult to take a hedge fund and put it in our asset allocation. And so, therefore, the managers we'd be interested in as hedge funds would be ones that have… I won't say idiosyncratic risk because I think it's difficult to say anything is an idiosyncratic risk. But I would say they have to have uncorrelated risks to be ported onto our asset allocation. And that's what we'd be most interested in.

Robert Morier: That's helpful context, Scott. Thanks for sharing that. Well, just one more question just as it relates to the plan in North Dakota. In your executive director's strategy review, they laid out North Dakota's big, hairy, audacious goals… so that's in the public record, so I'm quoting it directly… over the next 5 to 10 years. Can you touch on some of the more important goals that you see, taking everything that we've talked about over the last hour and going back to that prioritization? What are the BHAGs from your perspective?

Scott Anderson: Jan Murtha is our executive director, and she and I and all the organization are very passionate about the strategy of the retirement investment office. And the entire organization has been involved in our crafting our strategy for the organization. And we put one together a couple of years ago, and we're putting one together now, the one that you've seen. And it's not just strategic plan on shelf. It's a sincere set of goals that we want to achieve going forward. And every item on that list, I think, is really important and will contribute a lot of value to the state of North Dakota. That said, there are particular initiatives that are related to the investment program. So those are the ones I'll talk about. But just understand that the broader reorganization operates as a team and is very performance motivated. And everybody is kind of actuated to add as much value to North Dakota as possible. The three basic initiatives that I think on that big, hairy, audacious goal set are, one, our intern program. So, one thing over time that we recognize, that to be a top tier investment organization, we have to have top tier investment professionals. And over time, we want to grow our future leaders, and over time, we want to have more of our staff come from North Dakota. Currently, we have a hybrid or remote workforce, and we have some individuals living in other states and some individuals living in North Dakota. And so, we're starting an internship program, and this summer, we'll have an investment intern from some local college or from somewhere else come join us here in Bismarck. And then over time, when we have an opportunity, we'll hire some of these interns in full-time roles within the organization. That helps the intern. They get exposed to the investment world, and they get exposed to our organization. And we get exposed to top talent, and then over time, we can grow that talent from the ground up. So that's really an exciting goal. And we're going to expand that program and make it more sophisticated as we go. And then the second would be a cash management program. So statewide there's a study regarding how can we manage our cash assets in a more sophisticated way? And we're part of that because some of the cash assets are managed by us. And to the extent that the findings from that cash management study impact our investment processes… in other words, if we take on other portfolios or other investment processes related to cash management… that that's an interesting initiative for us. And it fits well with having an aspiration in two or three years that we stand up a more sophisticated investment at what I'd call Treasury function. That's where you buy and sell liquidity, and you manage liquidity assets of your portfolio. And it's necessary for us to take on these more advanced funds management capabilities. So, cash management is something we're going to do anyway, but as the results come out from this cash management story… cash management project… that we're going to implement those. And then the third would be our phase two of our internal direct program. So, phase one of our internal direct program is basically, let's overlay cash with derivatives and rebalance with derivatives. There's actually quite a big benefit from doing that. If you have cash, cash in your portfolios waiting for capital calls or benefit distributions or paying earnings for the legacy fund, we call that a cash drag. The cash doesn't earn as much as other assets can earn. And so, we'd like to overlay those with derivatives, and then you still have the liquid cash underneath the derivatives. But we can always have enough ready cash assets for whatever the liquidity needs might be of the plan plus have a higher return over time. And then we would also rebalance with derivatives. So, what that does is we rebalance our liquidity funds, and as a result, that's a portfolio construction issue. We can manage our active return and risk with our rebalance process and make sure that we don't impose too many transaction costs on our plan by rebalancing through our active managers, external or internal. So, we will have specific liquidity funds that we manage internally, either with derivatives or physical securities, that we rebalance through. And then we're going to stand up an index fund for equity and fixed income. We're going to make it an enhanced index, so it will give a little bit of a return but not a lot of risk. And so, it's one of those commodity sorts of mandates that we have in our portfolio that we can manage at a much lower cost with an internal direct team and an external treatment. Because it has a lower cost, basically, for the same net active return, we can do it for lower risk, which means we have a much higher probability of achieving that enhanced return. And then sometime next year, we'll expand that enhanced indexing program. The next phase is phase two, and that's where we'd move in a more active direction with our portfolio. So, we bring more of the assets to be managed internally, and we'd have more active management of our portfolios. We believe that we'll never likely get to have more than maybe 50% of our assets managed internally, and that's because there are certain strategies where we would not have the scale. We would not have the scale to have the specific expertise to execute the strategy or the scale for the infrastructure required to execute some of those strategies and then also maybe the scale for the search process like in direct private equity. So, there's certain parts of our balance sheets, of our client funds, that we think are always going to be with external managers and certain parts of our client funds' balance sheet that can be managed internally. And that's part of our allocation process. What can we do for a lower cost with a higher probability of success internally? And what we can't, then that would be managed externally. So that's that phase two is what I would call advanced funds management two. So, it's the more sophisticated exposure management, the more sophisticated active management of our internal portfolios.

Robert Morier: Thank you for sharing all that, Scott. We wish you the best of luck with those goals. I should say for our audience, the reason that we met is because this show is going to North Dakota. We're going to North Dakota State University at the end of the month. We're going to be speaking with some of those students you're going to be recruiting as interns. So, I will make sure to let the audience know that you are in the process of building out that internship program. I think that's incredibly exciting. It's music to my ears as an educator, so I wish you the best of luck with that as well.

Scott Anderson: Thank you.

Robert Morier: Well, just two more questions for you, and then we'll let you go. We know you have a busy day ahead of you. But when we look at the current environment, I like to look for locals and local quotes. Lawrence Welk said, "There are good days, and there are bad days. And this is one of them." so when you think about just what markets are presenting on a day-to-day basis, what principles guide you to ensure the long-term sustainability and growth of the North Dakota assets?

Scott Anderson: Yeah, thank you for that question. And I think you said it… long term. That's the word. It's interesting, there's a chart that I think you can find in the JP Morgan guide to markets, and it shows what is the range of returns for equity and fixed income on a one-year basis, a three-year basis, a five-year basis, a 20-year basis. And it's interesting how you get this wide dispersion for equity on a one-year basis and not as much dispersion for fixed income on a one-year basis. But you get out to 20 years, and there's never been a year where equities haven't returned more than like 6.5%, 7% over a 20-year period. And so, the long term is really important, and we're long-term investors. That said, because of our scale, we have an opportunity to allocate well. And basically, what you're doing when you allocate, each sliver of capital that you're allocating, basically, conceptually, is the highest returning sliver of capital for a particular state that the economy is undertaking at any point in time. So if you have a diverse allocation of uncorrelated return streams, as much as possible, and if you are able to achieve with that diversification the appropriate return so you don't under return your expectation to ease your liability, that over a long period of time, that asset allocation itself will just flex and take care of itself depending on what the ups and downs are in the particular market. As an example, in 2022, the public equity market, obviously, did not perform well, and the fixed income market had probably its worst year ever. And… but our infrastructure portfolio and our private equity portfolio and even then, our real estate portfolio performed OK. And then as we're coming out of that, we had a great equity market last year, and fixed income… still challenges. Rates are still kind of trying to settle… find their settle point. But real estate started to form a little bit less well, as an example. But it's here, again, infrastructure is still performing well. So, if you have a diverse portfolio, it takes care of some of that for you. Certainly, on a day or a week or a month, one cannot overreact to how the market behaves. Now, if the market were to drop like 20% in a short period of months, it would make you to take pause, like in the global financial crisis. But in normal times, you expect that there's going to be drawdowns at 10% multiple times during a year, and you'll get a drawdown of 20% like once every five, six, seven years, kind of typically. So, you've got to expect that sort of thing to happen in your portfolio, and you got to roll with the punches. And I always say, at that point, to a board, hey, it's really this kind of risk that allows us to have the kinds of returns that we need in the future because it creates the kind of market sentiments and risk aversion that enables these asset classes to trade at levels that provide us with returns.

Robert Morier: Wonderful. Thank you for sharing. One last question, and the question we like to end our podcast with are the people who were most important to you over your career, the mentors that have stayed with you and have lasted through all these years.

Scott Anderson: Yeah, thank you for that question. I'll tell you, I have been so blessed with so many good colleagues, so many good leaders and mentors. It's hard to name them all, and I go back to CEO of a company that I performed duties as a corporate development executive, a chief operating officer of Deloitte that was the managing director of our Deloitte office, another managing director of my Deloitte office who became the head of the global M&A practice, another who from my office became the head of the global energy practice, another who became… a couple who became vice chairs of Deloitte. Those exposures were priceless in terms of being able to observe extremely high-quality professionals in action, how they communicated, how they held themselves up in front of the public and decisions that they would make and how they would make their decisions. And I think of, at American Family, our chief investment officer and later became head of our P&L and our innovation practice. And I think of David Villa at State of Wisconsin Investment Board, a very creative guy that really drove SWIB to be a very commercially oriented state investment plan. All of those experiences really, really helped me. In fact, I think if I didn't have them on average, I'd be probably less well off than most. I was just very blessed to have these people around me. But one thing I notice about all of them is they were… all had goals. They were all driven for a mission. They were all constantly in action. They weren't like pie in the sky dreamers. They were like I want to achieve this. This is a way we can do it. Let's go do it. Does it work or not? Well, maybe not. Let's do this. Did it work? Yeah, it did work. Do more of that. They're guys that just are in motion and constantly achieving, and I learned from them that it's not just about talking and thinking. It's about actually acting and doing, the acting and doing. And secondly, they were all very much people people. They were all you know very good interpersonally, and they cared about other people. They were always mentoring people. They were always trying to help people advance in their careers. And I think probably they probably had similar experiences. Others were helping them in their careers and passing it on. But it's the kind of person whose very people oriented that's able to solve problems because all problems need to be solved through people. So, these are people who are high achievers, always in action, always interacting positively with other people, always trying to help other people. And that's what I learned from them. And I probably don't even do them justice, but I hope over time I can.

Robert Morier: I'm sure you have, Scott. Thank you for sharing all of that. We greatly appreciate it. Thank you for taking time to be here today. Congratulations on all of your accomplishments. We wish you the best of luck going forward. We know there are a lot of goals. You're going to have a lot of actions in front of you that you're going to need to accomplish, but we absolutely wish you all the best. So, thank you for being here.

Scott Anderson: Thank you. Thanks for having me on the show.

Robert Morier: If you want to learn more about Scott and the North Dakota Retirement and Investment Office, please visit their website at www.rio.nd.gov. You can find this episode and past episodes on Spotify, Apple, or your favorite podcast platform. We are also available on YouTube, if you prefer to watch while you listen. If you'd like to catch up on past episodes, check out our website at dakota.com. Finally, if you like what you're seeing and hearing, please be sure to like, follow, and share these episodes. We welcome your feedback as well. Scott, thank you again for being here. Tim, thank you as always. And to our audience, thank you for investing your time with Dakota.