

**COMPTROLLER'S  
INVESTMENT ADVISORY BOARD MEETING  
Tuesday, November 6, 2018  
*Minutes***

The Comptroller's Investment Advisory Board (the "Board") met at 10 a.m. on Tuesday, November 6, 2018, at the LBJ State Office Building, 111 E. 17<sup>th</sup> Street, Room 114, Austin, Texas.

**Board Members ("The Board") Present**

Laurie Dotter, Jim Hille, Steve Strake, and Scott Wise.

**Board Members Absent**

Tucker Bridwell and Adolpho Telles.

**Comptroller of Public Accounts Staff Present**

Comptroller Glenn Hegar; Lisa Craven, Deputy Comptroller; and Phillip Ashley, Associate Deputy Comptroller.

**Texas Treasury Safekeeping Trust Company ("Trust Company") Staff Present**

Paul Ballard, Chief Executive Officer and Chief Investment Officer ("CEO"); Danny Sachnowitz, Deputy Director and Deputy Chief Investment Officer; Frank Zahn, Chief Financial Officer ("CFO"); Mike Samples, Director of Internal Investments; Anca Ion, Deputy Director of Internal Investments; Marianne S. Dwight, General Counsel; Gena Minjares, Deputy CFO; Laura Montoya, Chief Operating Officer; Whitney Blanton, Deputy General Counsel; Spencer Brown, Compliance Officer; Jorge de LaFuente, Director of Operational Due Diligence; Patrick Jue, Investment Analyst; Hugh Ohn, Director of Accounting Strategy and Planning; Mike Leifeste, Portfolio Manager; Byron Beasley, Portfolio Manager; Lalo Torres, Portfolio Manager; Jyoti Gupta, Portfolio Manager; Mohamed Elkordy, Portfolio Manager; Ruchit Shah, Portfolio Manager; Adam Levine, Risk Strategist; Chad Turn, Risk Manager; Mat Williams, Investment Analyst; Jacob Price, Investment Analyst; Nora Arredondo, Special Projects Coordinator; Brandy Bianco, Project Manager; Yunke Yu, Quantitative Data Analyst; Scott Cowin, Investment Analyst; and Corrine Hall, Program Administrator.

**Additional Participants**

Lori Mills, Asset Consulting Group ("ACG").

**Call to Order**

Comptroller Glenn Hegar declared that a quorum was present and called the meeting to order at 10:01 a.m.

## **Approval of Minutes of August 16, 2018 Meeting (Tab 1)**

*Ms. Laurie Dotter made a motion to accept and approve the minutes of the August 16, 2018 Comptroller's Investment Advisory Board meeting. The motion was seconded by Mr. Steve Strake and unanimously approved by the Board.*

## **Economic Outlook, Investment and Review of Treasury Pool (Tab 2)**

Mr. Mike Samples reported on current economic conditions and noted that the Federal Reserve (the "Fed") continued its path of aggressive tightening and is expected to raise interest rates again in December and in 2019. The U.S. economy experienced a 4.2% real gross domestic product ("GDP") increase for the quarter, in part driven by the tax cuts. That was the fifth best quarter of recovery. Mr. Samples believes the economy will not sustain this growth and will begin to slow. He reported that new and existing housing sales, auto sales and retail sales were down from a year ago. Mr. Samples continues to believe the U.S. deficit is the most looming issue. He pointed out that Social Security will be in a negative flow soon. Mr. Samples expects the Fed to continue to tighten until the economy slows significantly.

Mr. Samples reviewed the Treasury Pool data as of September 30, 2018. He reported that the portfolio yield for said quarter was approximately 2.27%, up approximately 18 basis points from the previous quarter. The portfolio had a market value of approximately \$35 billion and continued to maintain a AAA rating by Standard & Poor's. He reported that commercial paper and U.S. Treasuries account for a little more than 50% of the portfolio's composition. Mr. Samples stated that the portfolio was able to capture approximately 75% of the Fed interest rate increase and was positioned to capture future rate increases relatively quickly. He reported that currently the portfolio was able to stay ahead of the Fed funds yield and has an approximately 15 basis point advantage. Since the expectation is that future interest rate increases will be nominal and gradual, the Treasury Pool management team expects to maintain an average maturity neutral to its benchmark.

## **Capital Markets Overview and Investment Performance Review for the Quarter Ending June 30, 2018, and Related Matters (Tab 3)**

Ms. Lori Mills of ACG presented ACG's view of the economy and market environment. She explained that October was a challenging month and global equity markets gave up 7% - 10%. November was better thus far and equity markets were up 1% - 4%. For the quarter ending September 30, 2018, with the exception of commodities, markets have been strong since the downdraft in 2008. The unemployment rate for the quarter was 3.7% and is not expected to climb in the near future. She explained that although economic recovery has been long, it has not been strong, and ACG continues to expect slow economic growth between 2.5% - 3.5%. ACG believes 2019 will present challenging markets. They will continue to closely monitor overall portfolio allocations relative to strategic objectives and they will continue to recommend diversified hedged strategies for downside protection.

Ms. Mills reviewed the total portfolio summary for the period ending June 30, 2018. She reported that the total portfolio returns outperformed the Endowment policy benchmark with similar risk over the past quarter, and the past three and five year periods. Relative to broad market benchmarks, the total portfolio has generated 95% of the return with 48% of the risk. The fixed income portion of the portfolio has significantly outperformed the fixed blend over the second

quarter and the one, three and five year periods. Equity and real assets strategies trailed their benchmarks over the past year, but have generated excess returns over the three and five year periods. Ms. Mills reported that real estate related investments have more than offset the struggles in natural resource related investments. Private equity strategies were the best performing component of the equity portfolio over the last five years. Ms. Mills explained that the overall objective of the portfolio is to provide predictable and stable distributions with minimum downside risk and inflation protection.

Ms. Mills reported that the SWIFT portfolio produced a 3.25% annualized return since its inception, outperforming its annualized policy benchmark by 2.14%. With the exception of the fixed income strategy, each of the other broad asset classes (equity and real assets) have exceeded their benchmarks over the quarter, one, three, and five-year periods. The portfolio generated excess returns versus its dynamic benchmark over all periods since inception. Overall, the SWIFT portfolio has generated higher returns and lower risk than both the policy and dynamic benchmarks since inception.

The TESTIF portfolio produced a -0.30% return for the quarter, underperforming the policy and dynamic benchmarks by -0.30 for each. It has outperformed the policy and dynamic benchmarks since inception (September 2015), and delivered a higher risk-adjusted return relative to both benchmarks.

#### **Endowment, SWIFT and TESTIF Portfolio Updates and Related Matters (Tab 4)**

Mr. Ballard presented an overview of the Endowment portfolio for the second quarter of 2018 and reported that the portfolio was in compliance with its investment policy. He reported that as of June 30, 2018, the value of the Endowment portfolio was approximately \$4.08 billion. He explained that the portfolio performed as expected. The best performing strategies were alternative fixed income (2.9%), private debt (2.8%), and private equity (2.2%). Mr. Ballard reviewed the asset allocation summary and explained that each asset class was within the policy target range. Mr. Ballard explained the performance summary charts and noted that the portfolio was obtaining more of the up capture than the down capture. He reported that in April of 2019 there will be an approximate \$70 million distribution from the Tobacco Endowment to the political subdivisions named in the statute. Mr. Ballard updated the Board on the current performance of the Endowment portfolio: the return for July was 1.3%, August +0.3% and September +0.2%, bringing the year-to-date performance to 4.9%

Mr. Ballard stated that a persistence investment pool was created within the Endowment portfolio. Mr. Leifeste explained that this pool is comprised of lower volatility strategies that are uncorrelated to equity and fixed income portions of the greater portfolio. Mr. Ballard also reported that the commodities portion of the real assets class was being eliminated from the Endowment and SWIFT portfolios.

Each portfolio manager from the Trust Company briefly recapped the portion of the portfolio they managed and summarized the information included in the presentation behind Tab 4.

Mr. Ballard presented an overview of the SWIFT portfolio. The portfolio value as of June 30, 2018 was approximately \$1.87 billion and it produced an approximate 1.5% return. The portfolio has earned approximately \$300 million and has distributed approximately \$600 million inception-to-date. The portfolio is within its asset allocation target ranges. The portfolio's top performing strategies were private debt (2.2%), real estate (1.9%) and hedged equity (1.8%). Mr. Ballard

reported that the portfolio return in July was +0.8%, in August it was +0.4% and in September it was +0.4%, bringing the year-to-date approximate return to 4.1%. He stated that the SWIFT was meeting its performance objectives.

Mr. Ballard reviewed the TESTIF portfolio and reported that it was performing as expected. The portfolio value as of August 31, 2018 was approximately \$3.25 billion, an increase of about \$15 million from the previous quarter. The portfolio remains highly liquid and continues to stay ahead of inflation.

#### **Broker/Dealer Update (Tab 5)**

Mr. Ballard presented the current broker/dealer list to the Board. He noted that Brean Capital and Guggenheim Partners were added to the list this year.

Comptroller Hegar asked the Board to break for lunch.

Comptroller Hegar informed the Board that revenue for the state continues to track in higher. Summer sales tax receipts and jobs continue to increase. He reported that we were in the longest economic recovery in history. He believes that in the next legislative session economic needs will be met without tapping into the Economic Stabilization Fund (“ESF”); however, he remains cautious. The ESF is approximately \$11.9 billion. Comptroller Hegar stated that he believes the biggest hurdles for the next legislative session will be school finance and property taxes.

#### **Discussion of Next Meeting and Agenda Items**

Comptroller Hegar announced that the next meeting would be scheduled for some time in January. No future agenda items were suggested.

#### **Public Comment**

None.

Comptroller Hegar and Mr. Ballard recognized Mr. Scott Wise for his 11 years of service.

#### **Adjourn**

The meeting adjourned at 12:48 p.m.