

**TOBACCO SETTLEMENT PERMANENT TRUST ACCOUNT INVESTMENT  
ADVISORY COMMITTEE  
Friday, October 24, 2014  
Minutes**

The Tobacco Settlement Permanent Trust Account Investment Advisory Committee (the “**Committee**”) met on Friday, October 24, 2014 at 10:00 a.m. in Room 320, Rusk State Office Building, 208 E. 10<sup>th</sup> Street, Austin, Texas.

**Committee Members Present**

Stuart Ford, Chairman; Roy Browning, Jr.; Peggy Deming; Judge Dan Gattis; Judge Wayne Gent; Fred Greene; and Chuck Norris.

**Committee Members Absent**

Judge Mike Brown; Commissioner Neil Fritsch; Noe Hinojosa; and Judge David Silva.

**Texas Treasury Safekeeping Trust Company (“Trust Company”) Staff Members Present**

Paul Ballard, Chief Executive Officer and Chief Investment Officer; Danny Sachnowitz, Deputy Chief Investment Officer; Frank Zahn, Chief Financial Officer; Marianne S. Dwight, General Counsel; John Wright, Deputy General Counsel; Jorge de LaFuente, Investment Analyst; Byron Beasley, Private Markets Manager; Michael Leifeste, Real Estate Portfolio Manager; Victor Scott, Director of Financial Reporting; Michael Anderson, Compliance Officer; Chad Turner, Investment Analyst; Laura Montoya, Director of Administration; Nora Arredondo, Special Projects Coordinator; Ruchit Shah, Investment Analyst; and Corrine Hall, CAPCO Administrator.

**Additional Participants Present**

Tom Janisch, Asset Consulting Group (“ACG”); and Pam Sliman, State Street.

**Call to Order**

Chairman Stuart Ford declared that a quorum was present and called the meeting to order at 10:04 a.m.

**Approval of Minutes (Tab 1)**

*A motion was made by Mr. Chuck Norris to approve the March 21, 2014 meeting minutes. The motion was seconded by Mr. Fred Greene and unanimously approved.*

**Capital Markets Outlook and Discussion (Tab 2)**

Mr. Tom Janisch presented a capital markets overview for the period ending June 30, 2014. He explained that the markets were positive during the first half of 2014. The S&P 500 led the way, with positive performance of approximately 7%. The bond markets also offered positive performance as did the emerging markets. Commodities have been on a downward trend since May, but remain positive year to date. The third quarter proved difficult. Although there was positive performance for large cap equities, there was another sharp reversal in the small cap sector, and commodities continued their downward trend. Mr. Janisch reported that European markets were sluggish and Europe continued to be an area of

uncertainty. He also stated that emerging markets did well in the third quarter. ACG continues to be bullish on emerging markets and believes they present a large opportunity for future growth.

Mr. Janisch reported that ACG believes the earliest the Federal Reserve (“the Fed”) will likely begin to raise interest rates will be mid 2015 but may get pushed into 2016. He explained that inflation will likely stay below 2%. Overall, the U.S. economy is doing well and ACG remains positive for the next few quarters and continues to expect slow domestic economic growth.

Mr. Janisch summarized the asset class relative rankings as of the third quarter of 2014 and reported there were no changes in the tactical outlook for the quarter

### **Endowment Portfolio Update and Related Matters (Tab 3)**

Mr. Paul Ballard presented an overview of the endowment portfolio and reported that it was in compliance with the investment policy. As of June 30, 2014 the portfolio value was approximately \$2.34 billion. He reviewed the asset allocation evolution graph and explained that the portfolio was in alignment with its asset allocation targets. He reviewed the portfolio characteristics and stated that the portfolio was very liquid and positioned opportunistically. The portfolio remains extremely diversified as illustrated in the presentation behind Tab 3. Mr. Ballard explained the cautious economic outlook the Trust Company has in relation to the portfolio positioning. He explained the flexibility built into the portfolio that would aide in protecting the portfolio from rising interest rates. Mr. Ballard and Mr. Sachnowitz reviewed various managers and their strategies within each asset class. They reviewed the performance of the portfolio’s investment managers and discussed the managers that have been added to or redeemed from the portfolio. Mr. Ballard explained that the current Value at Risk (VaR) for the portfolio was 3.9% and in line with policy. In conclusion, Mr. Ballard reported that the portfolio was performing in line with expectations, given the current economic environment.

### **Presentation and Discussion of Investment Performance for the Period Ending 6/30/14 (Tab 4)**

Ms. Pam Sliman of State Street reviewed the investment performance of the endowment funds for the period ending June 30, 2014. The portfolio return was approximately 3.0% for the quarter, which was approximately 47 basis points above the policy benchmark. Overall, each asset class outperformed its policy benchmark for the quarter. The portfolio also outperformed the policy benchmark for the trailing one through five year periods. From inception to date, the portfolio’s return was approximately 5.83%, outperforming its benchmark by approximately 22 basis points. Ms. Sliman further reviewed each asset class. She noted that the portfolio realized a lower level of volatility relative to its peers. The most current information as of August 30, 2014, suggests the portfolio’s performance was approximately 6.3%, outperforming the benchmark by approximately 1.3%.

### **Discussion of 2014 Annual Distribution (handout)**

Mr. Ballard led the discussion with a review of the “Corpus vs. Market Value” handout. He explained that at the end of the third quarter of 2014, the market value of the Trust was approximately \$2.322 billion and the expected adjusted corpus value for 2014 is approximately \$2.285 billion. He explained that Texas law prohibits spending Trust corpus (defined as total contributions to the Trust adjusted for inflation). When market value of the Trust is less than adjusted corpus value, only income may be distributed. But it may be supplemented with a withdrawal from the distribution stabilization account (“DSA”). He reminded the Committee that last year \$50 million was distributed and approximately \$15.9 million was contributed to the DSA. A handout of the DSA balance and distribution history was presented and reviewed. The Committee discussed the DSA and distributions further. They will decide on the amount of the 2015 distribution at its next meeting.

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

Committee members will be contacted to determine the best date for the next meeting in March 2015, when a vote on the annual distribution will be taken.

### **Public Comment**

Jim Allison, General Counsel from the County Judges and Commissioners Association of Texas spoke. In summary, he reminded the Committee that the tobacco settlement from which this fund was created, exists to compensate the taxpayers for past and future cost of providing health care for tobacco related treatment to indigent patients. He explained that the basic reason for this fund is to meet a need. He urged the Committee to keep this in mind when deciding future distributions.

### **Adjourn**

The meeting was adjourned at 12:12 p.m.