

**TOBACCO SETTLEMENT PERMANENT TRUST ACCOUNT INVESTMENT  
ADVISORY COMMITTEE  
Friday, November 6, 2015  
*Minutes***

The Tobacco Settlement Permanent Trust Account Investment Advisory Committee (the “**Committee**”) met on Friday, November 6, 2015 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; Judge Dan Gattis; Judge James Teal; Ms. Peggy Deming; Mr. Fred Greene; Mr. Chuck Norris; and Commissioner Byron Underwood.

**Committee Members Absent**

Mr. Roy Browning, Jr.; Judge Woodrow “Woody” Gossom, Jr.; Commissioner Neil Fritsch; and Mr. Noe Hinojosa.

**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; Whitney Blanton, Deputy Assistant General Counsel; Byron Beasley, Portfolio Manager; Michael Anderson, Compliance Officer; Jorge de LaFuente, Director of Operational Due Diligence; Nora Arredondo, Special Projects Coordinator; and Corrine Hall, CAPCO Administrator.

**Additional Participants Present**

Tom Janisch, Asset Consulting Group (“ACG”).

**Call to Order**

Chairman Stuart Ford declared that a quorum was present and called the meeting to order at 10:00 a.m.

**Approval of Minutes (Tab 1)**

*A motion was made by Mr. Chuck Norris to approve the March 27, 2015 meeting minutes. The motion was seconded by Judge Dan Gattis and unanimously approved.*

**Capital Markets Overview and Investment Performance Review for the Quarter Ending June 30, 2015 and Related Matters (Tab 2)**

Mr. Tom Janisch of ACG presented an update on economic conditions since the last meeting in March. He reported that the third quarter was driven by difficulties in China and low oil prices. He explained that from mid-June through the end of September, the Chinese market was down 42% and China has been the largest economic driver of the global economy. Also, demand for oil decreased yet production increased as OPEC refused to stop production despite falling prices. Mr. Janisch reported that as of June 30, 2015 all equity markets were negative and only credit was slightly positive. However, October proved to be the best month in four years for equities, led by S&P large cap and technology. ACG believes this is a positive signal for

the end of the year but the markets remains exceptionally volatile, however, the portfolio has been constructed to mitigate volatility.

Mr. Janisch reviewed capital markets performance for the period ending September 30, 2015. Utilities were the only positive sector in the U.S. for the third quarter but they represent a small component of the index. In October, technology was up 10.7%. Technology represents 20% of the index so it drove much of the market's performance. Non-U.S. equity markets and emerging markets were overall negative performers. And finally, fixed income posted slightly positive performance in the third quarter.

Mr. Janisch reported that unemployment was down to 5% and job numbers exceeded expectations. The Federal Reserve (the "Fed") did not raise interest rates in September. ACG expects the Fed to raise rates slightly in December 2015. Overall, the U.S. demonstrated modest growth and stability. ACG remains positive but continues to expect slow domestic economic growth.

Mr. Janisch presented a summary (handout) of the State Street investment performance data included behind Tab 2 for the second quarter of 2015. He explained that the portfolio returns had exceeded the endowment policy index in all but the second quarter. Fixed income and equities performed below their benchmarks for the second quarter but outperformed the benchmark for the trailing one through five year periods. Real Assets outperformed its benchmark for the second quarter as well as the trailing one through five year periods. Mr. Janisch reported that the portfolio provided meaningful downside protection while participating in up markets (see trailing one year and three year periods).

Mr. Janisch summarized ACG's forward looking view of various asset classes. The overall market outlook is mixed. The outlook for Cash and global fixed income is negative. The outlook for equities is neutral to positive and, despite significant gains, equity markets are likely to continue to provide positive, albeit modest, returns going forward. ACG continues to recommend an overweight to emerging market equities. Although performance has been negative, ACG believes opportunities for positive performance exist going forward. The outlook for high yield fixed income represented the only change from the previous quarter with the outlook moving from underweight to neutral. High yield tends to perform relatively well in a rising interest rate environment.

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

Mr. Paul Ballard presented an overview of the endowment portfolio and reported that it was in compliance with the asset allocation and investment policies. As of June 30, 2015 the portfolio value was approximately \$2.34 billion. The portfolio slightly trailed the benchmark for the quarter but outperformed in the trailing one year and longer periods. He explained that performance for the quarter and trailing one year period was driven by the results of the private portfolios, particularly the private equity and real estate. Mr. Ballard reviewed the asset allocation targets listed on the summary page. He reviewed the portfolio characteristics and stated that the portfolio was very liquid, is positioned opportunistically and is extremely diversified.

Mr. Danny Sachnowitz reviewed the portfolio liquidity handout that illustrated the new liquidity policy. He explained that as a long-term investment portfolio, it could afford to be less liquid. The new guidelines allow 20% of the portfolio to be available within three months and 60% of the portfolio to be liquid inside two years. Mr. Ballard and Mr. Sachnowitz reviewed the portfolio's various investment managers, their strategies and performance within each asset class. They discussed managers that have been added to or redeemed from the portfolio. They explained that the portfolio is put through several stress tests scenarios and the construction of the portfolio is designed to be resilient. Its objective continues to be consistency of performance with downside protection. Mr. Ballard explained that the portfolio was funded with approximately \$1.7 billion and \$774 million has been distributed to beneficiaries to date and approximately \$2.34 billion is the current remaining value. He reported that the portfolio was performing in line with expectations, given the current economic environment.

### **Discussion of 2016 Annual Distribution and DSA Contribution Objectives (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 2015, the market value of the Trust was approximately \$2.252 billion and the expected adjusted corpus value for 2015 is approximately \$2.297 billion. The distribution stabilization account (“DSA”) balance was approximately \$65million. 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 DSA. He explained that Texas law prohibits spending Trust corpus (defined as total contributions to the Trust adjusted for inflation). He reminded the Committee that much still depends on portfolio performance in the fourth quarter. The Committee discussed the DSA and distributions further. The Committee will decide on the amount of the 2016 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 when a vote of the annual distribution will be taken.

### **Public Comment**

Jim Allison, General Counsel from the County Judges and Commissioners Association of Texas asked if there was a report of expense, fees etc. for the fund. It was explained that the annual audit addresses those issues and will be presented at the next meeting.

### **Adjourn**

*Chairman Stuart Ford adjourned the meeting at 11:45a.m.*