

**COMPTROLLER'S  
INVESTMENT ADVISORY BOARD MEETING  
Thursday, February 6, 2020  
*Minutes***

The Comptroller's Investment Advisory Board (the "Board") met at 10 a.m. on Thursday, February 6, 2020, 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, Adolpho Telles and Ben Wall. Sam Vinson participated by phone.

**Board Members Absent**

None.

**Comptroller of Public Accounts Staff Present**

Comptroller Glenn Hegar; Phillip Ashley, Associate Deputy Comptroller; and Cheryl Scott, Internal Auditor.

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

Mike Reissig, Acting Chief Executive Officer ("CEO"); Ruchit Shah, Acting Chief Investment Officer ("CIO"); Genoveva Minjares, Chief Financial Officer ("CFO"); Anca Ion, Head of Internal Investments; Whitney Blanton, General Counsel; Laura Montoya, Chief Operating Officer; Spencer Brown, Assistant General Counsel; Jorge de LaFuente, Director of Operational Due Diligence; Hugh Ohn, Director of Accounting Strategy and Planning; Steve Rohrich, Investment Analyst; Lalo Torres, Portfolio Manager; Jyoti Gupta, Portfolio Manager; Mike Leifeste, Portfolio Manager; Adam Levine, Chief Strategist; Chad Turner, Risk Manager; Mat Williams, Investment Analyst; Jacob Price, Investment Analyst; Nora Arredondo, Program Specialist; Brandy Bianco, Project Manager; Yunke Yu, Quantitative Data Analyst; Ramsey Abarca, Compliance Officer; Patrick Jue, Investment Analyst; Rob Krause, Trader/Cash Manager; and Corrine Hall, Program Administrator.

**Additional Participants**

Roger Willis and Brad Davis, Asset Consulting Group ("ACG"); and Mike O'Brien and Angela Dawson, RSM & Co., LLP.

**Call to Order**

Comptroller Glenn Hegar declared that a quorum was present and called the meeting to order at 10:00 a.m. Due to snow and weather conditions in Abilene, Sam Vinson was unable to fly into Austin. He called in to participate.

## **Approval of Minutes of October 17, 2019 Meeting (Tab 1)**

*Mr. Steve Strake made a motion to accept and approve the minutes of the October 17, 2019 Comptroller's Investment Advisory Board meeting. The motion was seconded by Mr. Adolpho Telles and unanimously approved by the Board.*

## **Presentation of Independent Auditor's Report for the Trust Company (under separate cover)**

Mr. Mike O'Brien summarized the audit reports in the handout and reported that RSM & Company issued an unqualified financial audit opinion with respect to the Trust Company for the fiscal year ending August 31, 2019. Mr. O'Brien reported that no audit adjustments were recorded during the audit engagement that indicate deficiencies in the accounting process, nor was a management letter issued.

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

Ms. Anca Ion reported on current economic conditions. She reported that since the last meeting in October, the markets have been relatively calm. Currently, the treasury market is displaying more volatility. Long term interest rates were coming down from 1.90% - 1.50%. The Federal Reserve (the "Fed") started providing liquidity to the banks in repo operations and they also started non-quantitative easing and buying treasury bills. In total, the Fed cut interest rates by 75 basis points in the previous year. Investors expect the Fed will cut rates even further. Ms. Ion explained that the market was mostly driven by domestic and global fundamental data. European markets were demonstrating negative Gross Domestic Product ("GDP") numbers for the fourth quarter of 2019. She reported that the Corona virus was causing market uncertainty as well. Domestically, GDP was approximately 2.10%, about the same as it was for the third quarter of 2019. Net exports accounted for approximately 1.50% of the 2.10%, and imports fell significantly. Manufacturing was slightly improving after contracting over the previous five-month period. Consumer confidence was higher than expected yet personal consumption was lower than anticipated. The labor market also proved strong.

Ms. Ion reviewed the Treasury Pool portfolio as of December 31, 2019. She explained that the Treasury Pool balance was lower for the quarter due to payments from the pool made to school districts. The Treasury Pool balance for the quarter ending December 31, 2019 was approximately \$36.4 billion. Ms. Ion reviewed the Treasury Pool portfolio composition. The Pool was comprised of approximately 30% commercial paper, 18% treasuries, 12% agencies, 12% cash and equivalents, 10% asset backed, 8% corporate bonds, 8% mortgage backed securities and 2% other. She reported that the mortgage allocation was working well as prepayments were rising. Corporate spreads were tight and there was a focus on callable agencies. Ms. Ion explained that the portfolio is positioned accordingly. Ms. Ion stated that she remains cautiously optimistic for 2020 and the portfolio is positioned accordingly. The current yield of the Treasury Pool was approximately 1.90%.

## **Capital Markets Overview and Investment Performance Review for the Quarter Ending September 30, 2019, and Related Matters (Tab 3)**

Mr. Roger Willis of ACG presented ACG's view of the economy and market environment. He compared the beginning of 2010 versus 2020. In the beginning of 2010, pessimism was high, the Fed Funds rate had fallen, equities had declined, real rates were negative for most of the decade, unemployment was around 10% and the U.S. was experiencing the longest economic expansion in history. Forward to the start of 2020, optimism is high, Fed Funds rate has risen, equities have appreciated, unemployment is approximately 3.5% and a recession is more likely within 1-3 years. Mr. Willis reviewed ACG's disciplined process graph which identifies areas that will drive investment returns over the intermediate term. ACG is focused on market and economic considerations relevant in the context of enhancing risk-adjusted outcomes. He reviewed the remaining graphs that represent key areas of focus and he summarized the implementation strategies relating to those key areas. Mr. Willis explained that ACG believes a recession is likely sometime soon, but not likely to be a deep recession.

The Board and ACG discussed volatility assumptions by asset class.

Mr. Brad Davis of ACG presented a capital markets update for the period ending December 31, 2019. He reported that global equities finished 2019 robustly, capping off a year of robust returns across markets. Global fixed income produced strong returns in 2019 assisted by central bank policy and demand for income. Commodities rose higher, led by gains in gold and oil.

Mr. Davis reviewed the total portfolio summary for the period ending September 30, 2019. He reported that the total portfolio returns outperformed the Endowment policy benchmark over the past one, three and five-year periods. The third quarter return was 0.32% which was -0.35% less than the policy benchmark. The total portfolio returns outperformed the 65/35 benchmark over the quarter, one, three and five-year time periods. Relative to broad market benchmarks, the total portfolio has generated 102% of the return with 45% of the risk. The total portfolio produced a 0.32% return for the third quarter of 2019 and a 5.26% return over the five-year period. The fixed income investments managed positive three and five-year returns. Alternative fixed and private debt strategies provided differentiated and enhanced returns. Equity strategies benefitted from the longest economic expansion in U.S. history, and have been the best performers of the portfolio. Real assets continued to do well and demonstrate strong relative results longer term, annualizing 103 basis points of outperformance over the trailing five-year period. The objective of the portfolio is to provide predictable and stable distributions with minimum downside risk and inflation protection.

Mr. Davis reported that the State Water Implementation Fund for Texas ("SWIFT") portfolio produced solid returns since inception, with a 4.13% rate of return since inception and a standard deviation of 2.57%. For the quarter ending September 30, 2019, the portfolio produced a return of 0.90%. The portfolio outperformed its policy benchmark and its dynamic benchmark over quarter, one-year, three-year and five-year periods. The fixed income portion of the portfolio underperformed over the one and three-year periods but has maintained positive relative results over the past five years. Equity and real assets outperformed their benchmarks since inception. Overall, the SWIFT portfolio generated higher returns and lower risk than the policy and dynamic benchmarks since inception.

Mr. Davis explained that the objective of the Texas Economic Stabilization Investment Fund (“TESTIF”) is to outperform the Treasury Pool and exceed inflation. The TESTIF portfolio has generated slightly lower returns and lower risk than the policy benchmark since inception. Relative to the policy and dynamic benchmarks, the portfolio has delivered a higher risk-adjusted return. For the quarter ending September 30, 2019, the portfolio produced a return of 0.65%.

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

Mr. Shah presented an overview of the Endowment portfolio for the third quarter of 2019 and reported that the portfolio was in compliance with its investment and asset allocation policies. He reported that in the third quarter of 2019, the Endowment returned 0.3%, and the value of the Endowment portfolio was approximately \$4.17 billion. He explained that the portfolio performed as expected. The best performing strategies were private equity, followed by real estate. New commitments in private equity were more directed towards specialist funds. Overall, new commitments were light for the quarter. Mr. Shah summarized the performance summary charts and noted that the portfolio continued to produce more of the up than the down capture. He reviewed the asset allocation summary and reported that the portfolio appears to be temporarily overweight in hedged and private equity and in stable value real estate. Mr. Shah reviewed the actual versus target allocations. Mr. Jim Hille discussed his concern with the deviations in allocations and target allocations. Mr. Shah continued the presentation and summarized the information relating to the investment strategies. He reported that as of September 30, 2019, the portfolio has distributed approximately \$2.05 billion. He explained that the current value at risk (“VaR”) was approximately 3.5% and slightly higher than the policy VaR of 3.3%.

Mr. Shah reviewed the SWIFT portfolio and reported that the portfolio was in compliance with its investment policy for the quarter. The portfolio value as of September 30, 2019 was approximately \$1.76 billion and produced a 0.90% return for the quarter. Mr. Shah reported that the portfolio remained highly liquid and was meeting its investment objectives.

Mr. Shah reviewed the TESTIF portfolio and reported that it was performing as designed by preserving its purchasing power and earning more than inflation. The portfolio value as of October 31, 2019 was approximately \$6.04 billion. The portfolio has produced an annualized return through October 2019 of approximately 3.65%. He reported that in the third quarter \$650 million was invested along with another \$440 million through early January. The portfolio has outperformed the Treasury Pool by 4.11% year to date. The portfolio remains extremely liquid.

#### **TESTIF Investment Policy Review (Tab 5)**

The Trust Company is recommending revisions to the TESTIF investment policy to address the statutory revisions made pursuant to Senate Bill 69. The cash allocation range should be at least 25% up to 100%. Mr. Shah stated the portfolio cash allocation range would be 25% for now or until the Trust Company knows the rate the legislature will spend the assets.

***Mr. Jim Hille made a motion to recommend the proposed revisions to the TESTIF Investment Policy as presented by the Trust Company. The motion was seconded by Mr. Steve Strake and unanimously approved by the Board.***

**Discussion of Next Meeting and Agenda Items**

Comptroller Hegar announced that the next meeting would be scheduled for some time in April. Ms. Nora Arredondo will be contacting the Board. No future agenda items were suggested.

**Public Comment**

None.

**Adjourn**

The meeting adjourned at 12:47 p.m.