

**COMPTROLLER'S
INVESTMENT ADVISORY BOARD MEETING
Thursday, October 8, 2014
Minutes**

The Comptroller's Investment Advisory Board (the "Board") met at 10 a.m. on Wednesday, October 8, 2014 at the LBJ State Office Building, 111 E. 17th Street, Room 114, Austin, Texas.

Board Members ("The Board") Present

Laurie Dotter, Steve Strake (by phone), Adolpho Telles and Scott Wise.

Board Members Absent

Tucker Bridwell and Jim Hille.

Comptroller of Public Accounts Staff Present

Martin Hubert, 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; Mike Samples, Director of Internal Investments; Marianne S. Dwight, General Counsel; John Wright, Deputy General Counsel; Wai Yee Cheng, Portfolio Manager; Byron Beasley, Private Markets Manager; J. Germenis, Public Markets Manager; Michael Leifeste, Real Estate Portfolio Manager; Lalo Torres, Investment Analyst; Jorge de Lafuente, Investment Analyst; Adam Levine, Risk Strategist; Chad Turner, Investment Analysts; Anca Ion, Portfolio Manager; Harry Lindner, Investment Analyst; Nora Arredondo, Special Projects Coordinator; Victor Scott, Director of Financial Reporting; Laura Montoya, Director of Administration; Corrine Hall, CAPCO Administrator; and Susan Colletti, Director of Investment Accounting.

Additional Participants

Lori Mills, Asset Consulting Group ("ACG"); and Pam Sliman, State Street.

Call to Order

Deputy Comptroller Martin Hubert declared that a quorum was present and called the meeting to order at 10:15 a.m.

Approval of Minutes of June 12, 2014 Meeting (Tab 1)

Mr. Scott Wise made a motion to accept and approve the minutes of the June 12, 2014 Comptroller's Investment Advisory Board meeting. The motion was seconded by Mr. Adolpho Telles and unanimously approved by the Board.

Annual Review of Comptroller's Investment Policy (Tab 2)

Mr. Paul Ballard explained that the Comptroller's Investment Policy is required to be reviewed annually and stated that no changes were being recommended at this time.

Capital Markets Outlook and Discussion (Tab 3)

Ms. Lori Mills recapped the market environment over the last nine months. She reported that all asset classes offered positive performance through June 30, 2014. In July, equity markets were down but back up in August with positive performance year to date ("YTD") reaching record levels. Emerging markets continued to improve with high YTD returns. Commodities however, were down over 6%. Ms. Mills noted that the portfolio was structured to weather this type of volatility.

Ms. Mills reported on current economic data stating that economic growth in the U.S. was better but still sluggish. The labor market continued to improve but wages were lagging and consumers had less money to spend. Globally, the dollar had strengthened and the sluggish European economy continued to be a concern. ACG continues to expect slow economic growth. They expect interest rates to remain low throughout 2014 and do not expect the Federal Reserve (the "Fed") to raise rates until 2015.

Ms. Mills reviewed Asset Consulting Group's asset class relative rankings as of the third quarter of 2014. She reported that there were no changes to the tactical outlook for the quarter. ACG and the Trust Company continue to focus on portfolio diversification, maintaining and/or enhancing exposure to fast growing regions such as emerging markets and maintaining diversified global fixed income exposure with a focus on real yields.

Economic Outlook, Investment and Review of Treasury Pool (Tab 4)

Mr. Mike Samples presented his outlook on the economy. He reported that the job market had improved. Inflation remained about the same with little or no changes in the economic climate since the start of QE3 in 2012. The Fed is expected to end quantitative easing by the end of October. With the end of quantitative easing, it is expected that the Fed may start to raise rates in 2015; however, Mr. Samples reported that the bond markets have not shown any signs that interest rates will rise or that the economy is improving. He believes the Fed will begin raising rates gradually sometime next year. He explained that he and his team remain focused on seeking higher relative yields.

Mr. Samples presented a summary of the Treasury Pool as of August 31, 2014. He reported that the pool was producing a net yield of approximately 0.46% and had a market value of approximately \$29.4 billion. He discussed the fact that the Treasury Pool had an appropriately broader investment opportunity set than cash-equivalent money market funds including the ability to extend duration. Active management decisions to extend duration have successfully added to the Treasury Pool's returns in the past. To demonstrate that fact, he reviewed the Treasury Pool's yield over time relative to the Federal Funds rate and noted that when short-term interest rates fell, the incremental yield produced by the Treasury Pool widened relative to the Federal Funds rate. Mr. Samples reviewed the dollar and yield benefit to the state generated by the Treasury Pool since 2007 relative to TexPool, the state's largest local government investment pool.

Endowment and State Water Implementation Fund of Texas (SWIFT) Portfolio Updates and Related Matters (Tab 6)

Mr. Paul Ballard informed the board of a correction to the executive summary on page 4. The total portfolio performance results should read: Q2 = 3.0%; 1yr = 13.3%. He continued with a review of the endowment portfolio and reported that it was in compliance with its investment and asset allocation

policies. As of June 30, 2014 the value was approximately \$3.74 billion. Mr. Ballard reviewed each asset class and the various investment strategies that represent the portfolio's diversification. Mr. Danny Sachnowitz noted new funds added to the portfolio as well as funds that were redeemed or those where exposure was reduced. Mr. Ballard explained the stress test scenarios as they relate to performance of the total portfolio in a crisis relative to the policy portfolio and a portfolio allocated to 65% global equities and 35% to global fixed income. The portfolio would out-perform in these market crisis situations.

Mr. Ballard presented the Board an overview of the SWIFT Investment Fund. He explained that the Trust Company has most recently been structuring the long term piece of the fund. He reported that performance has been better than expected and has outperformed its policy benchmark.

Lunch Presentation (Tab 5)

Paul McCulley, managing director and PIMCO's chief economist and investment committee member, presented his view on global economic conditions during the lunch break.

Endowment Funds Investment Performance Review for the Quarter Ending June 30, 2014 and Related Matters (Tab 7)

Ms. Pam Sliman reviewed the investment performance of the endowment funds for the period ending June 30, 2014. She reported that the portfolio had produced a return of 3.02% for the quarter, outperforming its policy benchmark. The trailing one year return was approximately 13.27%, which was greater than its policy benchmark of 12.31%. The portfolio also exceeded the benchmark return for two, three, and five-year periods. Each asset class produced positive returns and exceeded the benchmarks during the quarter. The performance of the different sectors of the portfolio was reviewed in further detail. The portfolio produced a Sharpe ratio exceeding that of its benchmark. Ms. Sliman reported the performance of the SWIFT for the quarter and noted the relatively short time it had been invested.

Discussion of Next Meeting and Agenda Items

Deputy Comptroller Martin Hubert announced that the next meeting would be scheduled for December 11, 2014. Nora Arredondo will be in contact with board members to confirm.

Public Comment

None.

Adjourn

The meeting adjourned at 1:25 p.m.