

**COMPTROLLER'S
INVESTMENT ADVISORY BOARD MEETING
Tuesday, April 16, 2019
*Minutes***

The Comptroller's Investment Advisory Board (the "Board") met at 10 a.m. on Tuesday, April 16, 2019 at the LBJ State Office Building, 111 E. 17th Street, Room 114, Austin, Texas.

Board Members ("The Board") Present

Comptroller Glenn Hegar, Tucker Bridwell, Laurie Dotter, Jim Hille, Adolpho Telles, and Ben Wall.

Board Members Absent

Steve Strake.

Comptroller of Public Accounts Staff Present

Phillip Ashley, Associate Deputy Comptroller; Mike Reissig, Senior Advisor; and Cheryl Scott, Internal Auditor.

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

Paul Ballard, Chief Executive Officer and Chief Investment Officer ("CEO"); Genoveva Minjares, Chief Financial Officer; Anca Ion, Director of Internal Investments; Marianne S. Dwight, General Counsel; Laura Montoya, Chief Operating Officer; Michael Leifeste, Portfolio Manager; Lalo Torres, Portfolio Manager; Ruchit Shah, Portfolio Manager; Jyoti Gupta, Portfolio Manager; Adam Levine, Chief Strategist; Mohamed Elkordy, Portfolio Manager; Nora Arredondo, Program Specialist; Brandy Bianco, Project Manager; Chad Turner, Risk Manager; Whitney Blanton, Deputy General Counsel; Jorge de LaFuente, Director of Operational Due Diligence; Mathew Williams, Investment Analyst; Jacob Price, Investment Analyst; Corrine Hall, Program Administrator; Hugh Ohn, Director of Strategy and Planning; Spencer Brown, Compliance Officer; and Michelle Davis, Paralegal.

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 10:07 a.m.

Comptroller Hegar introduced the new board member, Mr. Ben Wall of the Texas A&M Foundation. He officially replaced Mr. Scott Wise. The Comptroller also announced the retirement of Mike Samples, former Director of Internal Investments and Mr. Danny Sachnowitz, former Deputy CIO. He informed the Board that Marianne Dwight, General Counsel for the Trust Company, would be retiring on April 24, 2019.

Approval of Minutes of January 29, 2019 Meeting (Tab 1)

Ms. Laurie Dotter made a motion to accept and approve the minutes of the January 29, 2019 Comptroller's Investment Advisory Board meeting. The motion was seconded by Mr. Tucker Bridwell and unanimously approved by the Board.

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

Ms. Anca Ion reported on current economic conditions. She reported that the fixed income market was unlike that of a year ago. The Treasury yield curve flattened again during the first quarter, with yields on short-term maturities staying relatively stable and those on intermediate-term maturities falling. Inflation has not been picking up and the Federal Reserve (the “Fed”) would like to see inflation above 2%. Currently inflation is hovering around 1.8%. The Fed has acknowledged the slowing global economic growth and in a desire to not drive the U.S. economy into a recession, the Fed has paused any interest rate increases for now. She reported that interest rate increases are not expected for the remainder of 2019. Ms. Ion also noted that consumer spending continues to fall as household debt continues to rise.

Ms. Ion reviewed the Treasury Pool portfolio as of March 31, 2019. She reported that the portfolio reached a market value of approximately \$38 billion and continued to maintain a AAA rating by Standard & Poor’s. The portfolio yield increased from the previous quarter to 2.56%. She reported that commercial paper and Treasuries accounted for approximately 57% of the portfolio. Ms. Ion explained that until there is quantitative easing by the Fed, spreads should be tight; therefore, the portfolio is positioned accordingly.

Capital Markets Outlook and Investment Performance for the Quarter Ending December 31, 2018 By Asset Consulting Group (Tab 3)

Ms. Lori Mills of ACG presented ACG’s view of the economic market environment. Global economic growth was 2.5% - 3.0% and continued to show signs of weakness. Strong returns in February, March and April were reported in U.S. markets. First quarter returns of 2019 were the best since the third quarter of 2009. ACG believes that although the Fed is expected to continue tightening monetary policy at some point in the future, maybe not in 2019, a recession could be on the horizon. There is a big push to delay a recession beyond the next presidential election. ACG does not believe a recession or a major market meltdown is likely near term. Ms. Mills explained that ACG will continue to closely monitor overall portfolio allocations relative to strategic objectives.

Ms. Mills reviewed the total portfolio summary for the period ending December 31, 2018. She reported that the total portfolio returns lagged slightly behind the Endowment policy benchmark for the quarter. The portfolio produced a -3.07% return for the quarter. However, the total portfolio returns outperformed the Endowment policy benchmark in 2018 and continue to outperform over the past three and five year periods, generating higher returns with similar risks. Relative to the broad market passive benchmarks, the total portfolio has generated 146% of the return with just 47% of the risk. The fixed income portion of the portfolio lagged behind the fixed blend benchmark over the fourth quarter, but outpaced the fixed blend over the one, three and five year periods. Equity strategies outperformed the equity blend benchmark during the past quarter and over the one, three, and five year time periods. Private equity strategies have been the best performing component of the equity portfolio over both the three and five year periods. Real assets continued to have strong long-term results resulting in outperformance by 1.36% relative to its benchmark over the trailing five year period. Real estate related investments have been the best performing components of the portfolio over the past five year span.

Ms. Mills reported that the State Water Implementation Fund for Texas (“SWIFT”) portfolio produced a -2.01% for the quarter ending December 31, 2019 and slightly lagged its policy benchmark by -0.04%. The portfolio’s annualized return since inception was 2.90%, outperforming its policy benchmark by 2.12%. It also outperformed its dynamic benchmark by 2.23% since inception. Despite near term underperformance, the fixed income portion of the portfolio has produced strong returns since inception. Equity and real assets strategies continue to outperform their benchmarks over all time periods. Overall, the total portfolio generated higher returns and lower risk than the policy and dynamic benchmarks since inception.

Ms. Mills reported that the Texas Economic Stabilization Investment Fund (“TESTIF”) produced a 0.17 % return for the quarter ending December 31, 2018. She explained the nature of this more conservative portfolio. Relative to both policy and dynamic benchmarks, the total portfolio has delivered a higher risk-adjusted return. Overall, the total portfolio generated similar returns but with lower risk than the policy and dynamic benchmarks since inception (September 1, 2015).

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

Mr. Ballard presented a historical overview of the evolution of the endowment investments. He explained that capital preservation was the main focus when constructing the portfolio. He reported that for the fourth quarter of 2018, the Endowment portfolio was in compliance with its investment policy and as of December 31, 2018, the Endowment portfolio value was approximately \$3.98 billion. Mr. Ballard reviewed the asset allocation targets and explained that since the allocation policy was revised on October 1st, the commodity allocation was eliminated and the proceeds were added to the enhanced real estate strategy. Mr. Ballard reviewed each asset class and reported that the portfolio was performing as expected. He explained there was relatively little volatility in most asset classes for the quarter. The current value at risk (“VaR”) was 3.2%, and was slightly lower than the policy VaR of 3.5%.

Mr. Ballard reviewed the SWIFT portfolio and reported that the portfolio was in compliance with its investment policy for the quarter. The portfolio value as of December 31, 2018 was approximately \$1.65 billion and had made an approximately \$213 million distribution at the request of the Water Board in October. Mr. Ballard reviewed the various asset classes and reported that SWIFT’s real estate and global fixed income portfolios positively impacted performance. On the other hand, the portfolio’s public and hedged equity allocations detracted as volatility spiked throughout the quarter. Returns in 2019 to-date are 1.8% for January, 1.1% for February and 2.9% for March. He reported that the portfolio remained highly liquid and was meeting its investment objectives.

Mr. Ballard reviewed the TESTIF portfolio and reported that it was performing as designed by preserving its purchasing power by earning more than inflation. The portfolio value as of December 31, 2018 was approximately \$4.76 billion. The portfolio has produced an annualized return from inception through January of approximately 2.00%. The portfolio remains highly liquid and continues to stay ahead of inflation.

Lunch Speaker Bill Eigen of J.P. Morgan Asset Management (Tab 5 and handout)

Mr. Bill Eigen, Managing Director with J.P. Morgan Asset Management and head of the Multi-Strategy Fixed Income Team, presented his view on current economic conditions. He felt fairly bullish on the overall economy. Despite the fact that he is a fixed-income manager, he stated that he doesn’t depend on falling interest rates to make money. He reported that there has been little change in economic data such as inflation, gross domestic product (“GDP”) or unemployment since September of 2018. He believes economic growth can be between 2.5% - 3.0% in the next few quarters. In his opinion, inflation is as low as it is going to get and he does not anticipate much change in the consumer price index (“CPI”). Mr. Eigen explained his view on supporting hedged strategies such as alternative credit and structured credit. He believes an absolute return investment approach delivers a low volatility, uncorrelated return stream. In his review he stated that the yield curve has flattened significantly, therefore reducing the incentive to extend duration. He continued his presentation with a review of his handout.

Broker/Dealer List Update (Tab 6)

Mr. Ballard presented the current broker/dealer list to the Board. He noted that Cantor Fitzgerald & Co.; CIBC World Markets Corp.; Daiwa Capital Markets America, Inc.; Loop Capital Markets, LLC; Mutual

Securities, Inc.; SMBC Nikko Securities America, Inc.; and Williams Capital Group. LP were added to the approved broker/dealer list.

Legislative Update

Comptroller Hegar stated that only five weeks remained for the 86th Texas legislative session. A special session is not in the forecast and hopefully the approximately \$250 billion budget would be approved.

Discussion of Next Meeting and Agenda Items

No future agenda items were suggested. The next meeting will be scheduled sometime in July.

Public Comment

None.

Adjourn

The meeting adjourned at 12:37 p.m.