

**TOBACCO SETTLEMENT PERMANENT TRUST ACCOUNT INVESTMENT
ADVISORY COMMITTEE
Friday, October 25, 2013
*Minutes***

The Tobacco Settlement Permanent Trust Account Investment Advisory Committee (the “**Committee**”) met on Friday, October 25, 2013 at 10:00 a.m. in Room 320, Rusk State Office Building, 208 E. 10th Street, Austin, Texas.

Committee Members Present

Stuart Ford, Chairman; Judge Mike Brown; Roy Browning, Jr.; Peggy Deming; Commissioner Roger Galvan; Judge Dan Gattis; Fred Greene; Noe Hinojosa; and Chuck Norris.

Committee Members Absent

Judge Wayne Gent 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; J. Germentis, Public Markets Manager; Byron Beasley, Private Markets Manager; Michael Leifeste, Real Estate Portfolio Manager; Genoveva Minjares, Director of General Ledger Accounting; Victor Scott, Director of Financial Reporting; Michael Anderson, Compliance Officer; Chad Turner, Investment Analyst; Babatunde Oguntade, Investment Analyst; and Nora Arredondo, Special Projects Coordinator.

Additional Participants Present

Tom Janisch and Lori Mills, 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 10:13 a.m.

Chairman Ford read a statement regarding a temporary ruling on the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) requiring that municipal advisors register with the SEC. The temporary ruling resulted in a disagreement over the definition of municipal advisory services. The Comptroller’s office does not believe the usual activities of this committee constitute municipal advisory activities and they are working with the Attorney General’s office to clarify its application. Chairman Ford asked the Trust Company’s General Counsel, Marianne Dwight, to monitor the committee’s discussions and to advise them to stop if they began to engage in anything that would be considered municipal advisory activities

Approval of Minutes (Tab 1)

A motion was made by Mr. Chuck Norris to approve the March 27, 2013 meeting minutes. The motion was seconded by Mr. Fred Greene and unanimously approved.

Capital Markets Outlook and Discussion (Tab 2)

Mr. Tom Janisch and Ms. Lori Mills of ACG presented an economic overview of 2013. They reported that the Federal Reserve (the “Fed”) announced it was prepared to reduce or taper its monthly bond purchases later in the year. Mr. Janisch explained that the construction and housing markets have strengthened and shown signs of recovery as mortgage rates remained low. He reported that the unemployment rate fell slightly for the third consecutive month but not enough to demonstrate significant improvement in the unemployment outlook. Mr. Janisch explained that ACG continues to expect slow domestic economic growth and does not expect the Fed to increase interest rates in the near future as long as the unemployment rate exceeded 6.5% and inflation remained no higher than 2.5%.

Ms. Lori Mills reviewed the broad market returns for the period ending September 30, 2013. She stated that the equity markets were doing well while the bond markets struggled. ACG is bullish on equity markets over the long-term and they continue to believe that emerging markets present the largest opportunity for growth. She summarized the asset class relative rankings as of the third quarter of 2013 and reported that there were no changes to the tactical outlook for the quarter.

Endowment Portfolio Update and Related Matters (Tab 3)

Mr. Ballard presented an overview of the endowment portfolio and reported that it was in compliance with the investment policy. As of June 30, 2013 the portfolio value was approximately \$2.12 billion. Mr. Ballard reviewed the asset allocation evolution graph and explained that the portfolio was in alignment with its asset allocation targets. He explained the various strategies within each asset class and the types of managers each asset class contained. Mr. Ballard and Mr. Sachnowitz explained in further detail the roles of enhanced equity index and activist managers. They reviewed the performance of the portfolio’s investment managers and discussed the managers that have been added or redeemed from the portfolio. He also explained that the Value at Risk (VaR) for the portfolio was 3.6% and in line with expectations. In conclusion, Mr. Ballard reported that the portfolio performance was within expectations, given the current economic environment.

Presentation and Discussion of Investment Performance for the Period Ending 6/30/13 (Tab 4)

Ms. Pam Sliman of State Street reviewed the investment performance of the endowment funds for the period ending June 30, 2013. The portfolio return was approximately -0.96% for the quarter, which was approximately 81 basis points behind the benchmark; however, longer term results demonstrated that the portfolio had outperformed its benchmark. From inception to date, the portfolio’s return is approximately 5.20%, outperforming its benchmark by approximately 15 basis points. Ms. Sliman reviewed each asset class. The portfolio realized a lower level of volatility than its peers. As of September 30, 2013, the portfolio’s trailing one year return was approximately 8.3%.

Discussion of 2014 Annual Distribution (handout)

Mr. Paul 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 2013, the market value of the Trust was approximately \$2.20 billion and the expected adjusted corpus value for 2013 is approximately \$2.249 billion. He explained that the statute 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 which included a \$4 million withdrawal from the DSA. As of October 23, 2013, the income was approximately \$31 million and was expected to increase by

year end. He explained that much depends on the performance of the capital markets in the fourth quarter. The Committee will decide on the amount of the 2014 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 2014, when a vote on the annual distribution will be taken.

Public Comment

None.

Adjourn

The meeting was adjourned at 12:06 p.m.