

**TOBACCO SETTLEMENT PERMANENT TRUST ACCOUNT INVESTMENT  
ADVISORY COMMITTEE  
Friday, March 27, 2020  
Minutes**

The Tobacco Settlement Permanent Trust Account Investment Advisory Committee (the “Committee”) conducted a virtual WebEx meeting on Friday, March 27, 2020, at 10:00 a.m.

**Committee Members Present**

Stuart Ford, Chairman; Commissioner Rick Bailey; Commissioner Mark Beauchamp; Mr. Stephen Bowerman; Mr. Fred Greene; Mr. Noe Hinojosa; Mr. Reed Hurley; Mr. Ted Matthews; Judge James Teal; and Judge Ben Zeller.

**Committee Members Absent**

Judge Bill Gravell.

**Texas Treasury Safekeeping Trust Company (“Trust Company”) Executive Staff and Participant Members Present**

Mike Reissig, Acting Chief Executive Officer; Ruchit Shah, Acting Chief Investment Officer; Laura Montoya, Chief Operating Officer; Genoveva Minjares, Chief Financial Officer; Whitney Blanton, General Counsel; Nora Arredondo, Program Specialist and Shantel Geeslin, Program Specialist.

**Additional Participants Present**

Angela Dawson, RSM & Co., LLP; and Roger Willis and Alex Nixon, Asset Consulting Group (“ACG”).

**Call to Order**

Chairman Stuart Ford called roll, declared that a quorum was present and called the meeting to order at 10:06 a.m.

**Approval of Minutes (Tab 1)**

*A motion to approve the November 1, 2019 meeting minutes was made by Ted Matthews. The motion was seconded by Commissioner Rick Bailey and unanimously approved by the Committee.*

**Presentation of Annual Audit (Handout)**

Ms. Angela Dawson reviewed the annual audit report by RSM & Co. She reported that RSM & Co. issued an unqualified audit opinion with respect to the Tobacco Settlement Permanent Trust Account (“Account”) for the year ending December 31, 2019. Ms. Dawson affirmed that the account had been managed in compliance with the Investment Policy and the Distribution Policy. Ms. Dawson reviewed the distribution calculation process as described in the distribution attestation report. She explained that the audit attests to the calculation process, not the decided distribution amount, since it has yet to be determined. No audit adjustments were recorded during the audit engagement, nor was a management letter issued.

### **Discussion and Approval of Annual Trust Distribution (Tab 3)**

The Board reviewed the distribution amounts and asked Trust Company staff the procedure for potentially changing distribution amounts, in light of the pandemic. Mr. Whitney Blanton informed the Committee that in order to change the methodology for calculating the distribution, the Endowment Investment Policy would have to be revised. The Committee would notify the Comptroller's Investment Advisory Board ("CIAB") and the CIAB would make the final recommendation for revision to the Comptroller for approval. If approved, the subsequent distribution could not be retroactive. Mr. Blanton also noted that multiple distributions would require a statutory change. Current statute requires one annual distribution.

Mr. Ruchit Shah reviewed the corpus versus market value of the Trust. He reported that 1) the market value was approximately \$2.729 billion, up from \$2.517 billion this time last year, 2) that as of December 31, 2019, the inflation-adjusted corpus was approximately \$2.46 billion, 3) the Trust corpus was approximately \$1.683 billion, 4) total earnings were approximately \$1.046 billion and 5) total distributions since inception have totaled approximately \$1.03 billion. To summarize, the portfolio began with approximately \$1.683 billion, has distributed over \$1 billion, and currently has a market value of approximately \$2.73 billion. He reminded the Committee that the calculation is based the revised rule and is 3% of the 20-quarter moving average value of the Trust ending December 31, 2020. Mr. Ford stated that the recommended distribution amount is therefore \$73,831,823.77 and called for a motion.

***Mr. Fred Greene made a motion to approve the distribution of \$73,831,823.77 to the beneficiaries of the Tobacco Settlement Permanent Trust Account. The motion was seconded by Commissioner Rick Bailey and unanimously approved by the Committee.***

### **Capital Markets Overview and Investment Performance Review for the Quarter ending December 31, 2019 and Related Matters (Tab 2)**

Mr. Roger Willis presented an economic overview. He explained that the challenge at hand is that the Coronavirus is not well understood and governments are in a shutdown phase and are trying to flatten the curve or slow the rates of transmission. To counter some of the impact of the economic shutdown, central banks have acted quickly with significant impact in terms of liquidity to small businesses and households. The next few weeks, months and even quarters will provide more clarity relating to how this will impact the Gross Domestic Product ("GDP") and earnings. Mr. Willis explained that the portfolio contains a mix of asset classes, both publicly and privately traded assets, that creates diversification. This should help ameliorate any major impact to the annual distribution. He suggested that the portfolio would have less downside volatility while still able to participate in the recovery. Mr. Willis reported that although the stock market went up when the government stimulus package was announced, day to day volatility continued in the equity markets both domestic and foreign. On the fixed income side, there is very little liquidity, not many buyers coming to market. He explained that it is too early to draw conclusions at this point regarding future economic conditions; however, it is encouraging to note that the Federal Reserve Board (the "Fed") and the U.S. Treasury are working closely together and closely monitoring the environment.

Mr. Alex Nixon of ACG summarized the investment performance of the portfolio for the quarter ending December 31, 2019. He reported that the total portfolio (Tobacco Settlement Permanent Trust) over the last five years ending December 31, 2019, produced an annualized return of 6.15%. The total portfolio generated a higher return with similar risk compared to the endowment policy benchmark over the last five years. The portfolio lagged slightly behind the 65/35 benchmark. Relative to broad market benchmarks, the portfolio generated 97% of the return with 44% of the risk. He explained that the portfolio is very diversified and more diversified and more hedged than the global 65/35 benchmark while still trying to approximate the return with less risk over time. The standard deviation was 3.56% for the portfolio, but the

65/35 benchmark standard deviation was 8.05%, which translates to the portfolio experiencing much less volatility in returns than that of the public market benchmark or the 65/35 benchmark.

Mr. Nixon reported that the portfolio generated an 11.74% return last year. For the quarter ending December 31, 21019, the portfolio produced a 4.07% return, outperforming the policy benchmark by 1.20%. The fixed income portion of the portfolio outpaced the fixed blend benchmark for the quarter, three, and five-year periods but modestly lagged over the one-year period. Equity strategies have outperformed over all time periods and produced a return of 6.32% for the quarter. Real Assets continued to demonstrate strong relative results longer term. The portfolio was up 11.74% despite lagging in the fourth quarter, the fixed income portion of the portfolio outpaced the fixed blend benchmark over the one, three, and five-year time periods. Equity strategies outperformed its benchmark by 1.10% for the quarter and produced an annualized return for the five-year period of 5.26%. Real assets continue to demonstrate strong relative results longer term and posted a return of 2.39% for the quarter. Overall, ACG believes the portfolio is well positioned and they will continue to closely monitor the market environment. Mr. Shah commented that in this global financial crisis event we are experiencing so far this year, the portfolio has proven to be better protected and beating the broader markets.

#### **Tobacco Endowment Portfolio Update and Related Matters (Tab 4)**

Mr. Shah explained that it was important that the Tobacco Endowment was able to meet liquidity demands without incurring any substantial loss and also important to stay fully invested. The portfolio should also be sufficiently opportunistic. Mr. Shah reported that he and the portfolio managers at the Trust Co. along with ACG are aggressively monitoring the portfolio. Mr. Willis explained that in February ACG and Trust Co. investment staff formally met to review in depth strategic asset allocation, risk metrics, portfolio modeling, portfolio scenarios in different market environments, liquidity issues, etc. He stated that remaining focused on the long-term discipline and investment plan and adhering to the investment policy should provide the highest probability of achieving long-term goals and objectives within the portfolio.

Mr. Shah presented an overview of the endowment portfolio and reported that it was in compliance with the asset allocation and investment policies. He reviewed each asset class in detail and the various investment strategies utilized to diversify returns within the portfolio. He noted that the global fixed income class was performing fairly and had a bit of a drag in part due to corporate credit and liquidity issues. The portfolio had some exposure to Asian credit which proved helpful. Allocations to the reinsurance strategies also helped the portfolio. Other strategies which normally fair well struggled this quarter. The global public equity strategy was up almost 21% for 2019. The hedge equity portfolio was performing as expected and acting as protection during a downturn. Private equity, private debt and real estate are long-term investments and Mr. Shah expects performance will lag but will ultimately compare favorably to the market. Mr. Shah stated that investments within the private equity sector included new investments into healthcare. The real estate portfolio has gradually added more industrial related exposure. He also explained that the portfolio will continue to allocate funds to private markets which have outperformed public markets, and he believes will continue to outperform public markets. Leverage and derivatives were discussed, and Mr. Shah reminded the Committee that derivatives were used to get more cash-efficient exposure to equities and fixed income.

Mr. Shah reviewed which asset classes were overweight or underweight and how that related to the target allocations and returns. He explained that the portfolio is put through multiple stress test scenarios and that its construction has proven to be resilient. The objective continues to be consistency of performance with downside protection. Given the current economic market environment, he explained that the portfolio is equipped to take advantage of opportunities that may arise.

**Discussion of Next Meeting and Agenda Items**

The next meeting will be scheduled sometime late October or early November. Ms. Arredondo will contact Committee members to decide on a date.

**Public Comment**

Mr. Jim Allison suggests that the Committee consider what it would need to do in order to keep the distribution about the same level next year. If necessary, reallocating what is defined as net earnings. The Committee should be mindful of what is involved to make any changes to the distribution calculation.

**Adjourn**

*Chairman Stuart Ford adjourned the meeting at 12:16 p.m.*