

**TOBACCO SETTLEMENT PERMANENT TRUST ACCOUNT INVESTMENT
ADVISORY COMMITTEE
Friday, October 29, 2021
*Minutes***

The Tobacco Settlement Permanent Trust Account Investment Advisory Committee (the Committee) met on Friday, October 29, 2021 at 10:00 AM.

Committee Members Present

Stuart Ford, Chairman; Hon. Bill Gravell; Mr. Fred Greene; Mr. Noe Hinojosa (virtual); Mr. Reed Hurley; Hon. Rick Bailey; Mr. Ted Matthews; Hon. Mark Beauchamp; Mr. Stephen Bowerman; and Hon. James Teal.

Committee Members Absent

Hon. Ben Zeller.

Texas Treasury Safekeeping Trust Company (Trust Company) Executive Staff Members and Participant Members Present Onsite and Virtual

Mike Reissig, Chief Executive Officer; Ruchit Shah, Chief Investment Officer; Genoveva Minjares, Chief Financial Officer; Whitney Blanton, General Counsel; Chad Turner, Director of Risk and Quantitative Analytics; Michael Leifeste, Senior Portfolio Manager; Brad Davis, Senior Portfolio Manager; Nora Arredondo, Program Specialist and Shantel Geeslin, Program Specialist.

Additional Participants Present

Alex Nixon, Asset Consulting Group (virtual).

Call to Order

Chairman Stuart Ford called roll and declared that a quorum was present. He called the meeting to order at 10:00 AM.

Approval of Minutes of March 26, 2021 meeting (Tab 1)

Chairman Ford called for a motion to accept the minutes from the March 26, 2021 meeting.

A motion to approve the March 26, 2021 meeting minutes was made by Judge Bill Gravell. The motion was seconded by Mr. Reed Hurley and unanimously approved by the Committee.

Mr. Mike Reissig announced that Mr. Ruchit Shah will be leaving the Trust Company on November 1, 2021 and Ms. Anca Ion, the current Deputy Chief Investment Officer, will be the new Chief Investment Officer effective November 1, 2021.

Capital Markets Overview and Investment Performance Review for the Quarter Ending June 30, 2021 and Related Matters (Tab 2)

Mr. Alex Nixon of Asset Consulting Group (ACG) presented to the Committee a global economic update and capital markets overview. The impact of the Delta variant on economic recovery remains a concern as does the fiscal stimulus and debt ceiling uncertainty. Economic recovery slowed during the third quarter of 2021 and much of that could be attributed to the pause in services due to the Delta variant along with the ongoing supply chain disruptions. Mr. Nixon reported that the official first estimate of third quarter Gross Domestic Product (GDP) was approximately 2.0% annualized, which was the weakest quarter of growth since economic recovery began in mid-2020. The dip experienced in the third quarter is expected to be short lived and estimates for the fourth quarter and into 2022 and 2023 remain robust and above trend barring any other virus variants or mutations. Overall, global economic growth is expected to be positive.

Mr. Nixon discussed monetary policy and reminded everyone that the Federal Reserve Board's (the Fed) primary objective is to promote full employment while maintaining a healthy level of inflation of 2.0%. He reviewed the job recovery and labor shortages information in the presentation. Mr. Nixon explained how swift and severe the decline in payrolls were due to the pandemic; and although recovery has quickly improved, not all jobs lost have been recovered. Currently there is a low labor force participation rate, a high demand for workers and a shift in wage growth. This dynamic in the labor market added to the strong demand for goods and services and the supply chain disruptions, has led into a high inflationary period. He explained that the Fed has given the first official signal that tapering of bond purchases could soon be warranted, and by November they could announce they will begin tapering their purchases. ACG expects continued economic growth as COVID cases wane. If supply chain issues ease, this should help moderate inflation. Monetary policy and further stimulus could create volatility and concerns over economic growth.

Mr. Nixon reviewed a longer-term outlook in capital market assumptions. The outlook over the longer-term, five to ten years, is expected to reveal more muted returns. ACG believes the portfolio can achieve its 6.0% return objective but with more difficulty. ACG will look for ways to generate alpha and additional returns, and also stay disciplined and not compromise the risk profile of the portfolio.

Mr. Nixon summarized the investment performance of the portfolio for the quarter ending June 30, 2021. Over the last five years the Tobacco Settlement Permanent Trust (TSPT) portfolio produced an annualized return of 9.85% and outperformed its policy benchmark by 71 basis points. For the second quarter of 2021, the TSPT portfolio generated a 6.52% return and outperformed its policy benchmark and the 65%ACWI/35% Barclays Global Aggregate by 190 and 142 basis points respectively. Over the last one-year period, ending June 30, 2021, the portfolio returned 27.42%. The portfolio provided strong relative performance for each of the broad asset classes. Relative to broad market benchmarks, the portfolio generated 95% of the return with 53% of the risk. Mr. Nixon explained that over the long-term, the portfolio continues to achieve the target return of 5.5% – 6.0% annualized. Overall, the portfolio had strong 12-month returns from an absolute and relative return perspective.

Update on Endowment Investment Policy (Tab 3)

Ms. Anca Ion reported that the Trust Company together with their consultants, ACG and Aksia, were recommending to the Comptroller's Investment Advisory Board some marginal changes to the Endowment Investment Policy. The recommended revisions were included in the draft behind Tab 3. Some of the revisions included reducing the risk in some of the asset classes, particularly in the alternative fixed income sector. Also recommended for the alternative fixed income sector is a formal review semi-annually by Trust Company staff and its consultants. A few changes to liquidity guidelines for the total portfolio were among other recommended revisions. The Comptroller's Investment Advisory Board will review the recommended revisions again at their next board meeting and proceed with their recommendation to the Comptroller.

Endowment Portfolio Update and Related Matters (Tab 4)

Mr. Ruchit Shah and Ms. Anca Ion presented an overview of the Endowment portfolio as of June 30, 2021 and reported that it was in compliance with the asset allocation and investment policies. As previously reported, in the second quarter of 2021, the Tobacco fund returned approximately 6.5%, bringing the one-year trailing performance up to approximately 27.4%. The fund's private equity asset class was the leading performance contributor for the quarter, followed by hedged equity and real estate classes. Mr. Shah recapped the asset allocation summary. He noted that the alternative fixed income portfolio is underweight, and more managers, exposure and diversification will continue to be increased within this portfolio. The private equity portfolio is overweight and will continue to remain so for a little longer since the value has increased substantially. The real estate portion of the portfolio is working its way towards the 15% target from 20%. Mr. Shah reviewed the portfolio geographic allocation and explained that the emerging markets exposure has decreased over the years. There is also exposure in Asian markets as well. This all plays into diversification.

Mr. Brad Davis presented a fixed income overview. Fixed income represents approximately 35% of the portfolio and is comprised of several strategies including global fixed income, alternative fixed income and private debt. In the alternative fixed income space, two additional funds have been added since this report and a few more should be expected. Rebalancing this portfolio is prudent as is diversification, and lowering the sensitivity to the equity sleeve is an objective.

Mr. Shah reported that the private debt portion of the portfolio continued to do well. There was recovery in the distressed credit position; the portfolio shifted to more performing credit over the last year.

Mr. Shah reported there were no significant changes in the equity portfolio other than growth in private equity. There is considerable diversification in private equity such as exposure in technology, industrial and material companies as well as healthcare. There is growth opportunity in healthcare as the healthcare economy changes.

Mr. Mike Leifeste reviewed the real assets portion of the total portfolio. He reported that the portfolio is positioned in sectors that are performing well through this pandemic crisis. There is less exposure to retail and hospitality, and more exposure to industrial and multifamily. Modifications will be made as time progresses.

Mr. Shah stated there were no changes to report in strategic all asset and overlays sectors.

Mr. Chad Turner reviewed the Value at Risk (VaR) analysis. He reported that as of June 30, 2021, the VaR was 3.9% and slightly higher than the policy VaR of 3.4%. The portfolio risk measured in the long-term basis is slightly riskier than the policy portfolio but quite a bit less than the traditional 65/35 portfolio.

Mr. Shah reviewed the performance table and noted the portfolio was up 11.5% through June. The portfolio was up 1.2% in July, up 1.7% in August, and up 0.9% in September. Year-to-date the total portfolio was up 15.7%.

Discussion of Annual Distribution (Tab 5)

Ms. Ion led the estimated annual distribution discussion. She reported that the market value of the Trust is approximately \$3.089 billion, and the inflation adjusted corpus as of June 30, 2021 is approximately \$2.674 billion. Total earnings were approximately \$1.406 billion. She reported that based on the rule, the estimated distribution that will be made by April 1, 2022 should be approximately \$80.2 million, representing an approximate \$5.3 million increase, or an approximate 6.4% increase over the 2021 distribution. The estimated distribution calculation is based on 3% of the 20-quarter moving average value of the Trust as of September 30, 2021. The actual calculation will be based on the 20-quarters ending December 31, 2021. She explained that we are meeting our objective of growing the distribution at the rate of inflation. The expected actual distribution should not differ greatly from the \$80.2 million estimate because the calculation is based on a long-term average and 18 of the 20-quarter values are already known.

Chairman Ford stated that the Committee will decide on the amount of next year's distribution at its next meeting.

Discussion of Next Meeting and Agenda Items

Commissioner Rick Bailey introduced Cherokee County Commissioner Kelly Traylor who will represent the North and East County Judges and Commissioners Association and replace Commissioner Bailey.

The next Committee meeting will be entirely in person and take place in the traditional meeting room. The suggested meeting date is Friday, March 25, 2022. The Committee will be polled to confirm the March date.

Public Comment

None.

Adjourn

Chairman Stuart Ford adjourned the meeting at 11:57 AM.