



**MINUTES  
PUBLIC MEETING  
May 22, 2015  
9:00 am  
IGCS Conference Room D**

**I. Call to Order/Roll Call**

State Auditor Suzanne Crouch called the meeting to order at 9:00 a.m. Other Committee members present were Lisa Acobert, IDOE; Zac Jackson, SBA; and, Mike Frick, Deputy Treasurer. Also present were Erin Sheridan, Deputy Auditor of State and Maggie Johnson with the Auditor of State's Office; Jaimie Beisel & Matthew Bates with Great-West Financial (Third Party Administrator to the Plan); Mike Paton of Barnes & Thornburg (Counsel to the Committee and the Administrator); and, Corey Waddell, Amanda Black, and Tarek Zeni with Capital Cities, L.L.C. (Investment Consultants to the Committee).

**II. Reading of the Minutes**

Auditor Crouch asked for a motion to approve the minutes from the March 19, 2015 meeting. Mr. Jackson moved to approve the minutes. Mr. Frick seconded. The minutes were approved unanimously.

**III. Live-Streaming Disclaimer**

The meeting was live-streamed on a closed circuit for testing purposes. Future meetings will be live-streamed for public access. Ms. Johnson provided the new live-streaming disclaimer that will be read at the beginning of each meeting. Mr. Paton provided additional commentary on the disclaimer and its purpose going forward.

**IV. Administrators Report**

Auditor Crouch had no updates for the committee.

**V. Investment Consultant Report**

**Market Review**

Mr. Zeni highlighted the market environment for the first quarter of 2015. Overall, it paid to be invested in the stock and fixed income markets for the period. Specifically, the S&P 500 was positive 1.0% and the Barclays Aggregate Bond Index was positive 1.6%.

Mr. Zeni noted the S&P 500 recorded its 9<sup>th</sup> consecutive quarterly advance. Furthermore, within equities the best places to be were U.S. Growth Stocks, where Large Cap Growth was +3.8% and Small Cap Growth was +6.6%. Developed International equities were also strong performers returning 4.9% and outpacing their U.S. counterparts. Emerging Market equities were also positive at +2.3%.

Turning to fixed income, Mr. Zeni noted that Corporate Bonds and High Yield provided the strongest returns posting a +2.2% and +2.5% return respectively. On the other hand, Mr. Zeni noted that the worst place to be invested was Non-Dollar Bonds, which were down -4.4%, as the U.S. Dollar continued to strengthen.

Lastly, Mr. Zeni walked through Capital Cities' new reporting template. Going forward, Capital Cities will provide two books to the Committee. The first will be the traditional performance and evaluation report, and the second will be a book of any of the additional presentations for the meeting.

## **Manager Updates**

### **Perkins Mid Cap Value Search Book**

Mr. Waddell presented the Perkins Mid Cap Value Watchlist update and Mid Cap Value Search Book. The Perkins Mid Cap Value Fund is a specialty, stand-alone option in the Plan that offers participants active exposure to the mid-cap value space. \$23.8 million in Plan assets were invested in the Fund as of March, 31 2015, which represented 2.3% of total Plan assets. The Fund is a compliment to the very popular Vanguard Capital Opportunities Fund, which represents 9.4% of total Plan assets and invests in the mid-cap growth space.

Mr. Waddell reminded the Committee that the Perkins Mid Cap Value Fund was placed on Watchlist status during the February 2014 meeting given portfolio construction changes. Mr. Waddell also reminded the Committee of the contingency mid-cap value search that Capital Cities performed during the May 2014 meeting given the concerns at Perkins. There were 22 managers reviewed and the two finalists were MFS Mid Cap Value and Lee Munder Mid Cap Value. At that time, the Committee ultimately voted to keep Perkins in the Plan with close monitoring on Watchlist status.

Since placing the Fund on Watchlist, the Fund has experienced underperformance as well as asset outflows. More recently, on April 5<sup>th</sup>, it was announced that Jeff Kautz, CEO, CIO, and Co-PM of the Perkins Mid Cap Value Fund would be resigning from Perkins. Mr. Kautz had been with Perkins for over 18 years, and Capital Cities viewed his resignation as material. Given Mr. Kautz's departure, the underperformance and asset outflows, and the upcoming participant communication already planned, Capital Cities recommended terminating the Perkins Mid Cap Value Fund from the Plan lineup. Mr. Frick moved to terminate Perkins Mid Cap Value from the Plan lineup. Mr. Jackson seconded the motion. Perkins Mid Cap Value was terminated unanimously.

Capital Cities leveraged the contingency search and performed update calls with both MFS and Lee Munder. It was discovered that Lee Munder recently had a key personnel change. As a result, the Fund was eliminated from consideration. The Vanguard S&P Mid Cap 400 Value Index Fund was added to the search as a potential replacement along with MFS Value. The Committee debated the merits of active management versus low-cost passive management and ultimately decided to remain with an active manager. Mr. Frick moved to hire the MFS Value Fund to replace the Perkins Mid Cap Value Fund. Mr. Jackson seconded the motion. MFS Mid Cap Value was unanimously voted into the Plan.

### **Alternative Investments Search Findings**

Mr. Waddell presented the Alternative Investments Search Findings. He reminded the Committee that, during the October, 2014 meeting, Capital Cities recommended to survey the Alternative Investments marketplace given the growing availability of liquid, daily-traded Alternative funds. Alternative Investments are currently utilized within the construction of the custom Indiana Target Date Funds and are not offered to Hoosier S.T.A.R.T. participants on a stand-alone basis. The Alternatives' allocation is presently comprised of one fund, the Wellington Real Total Return Fund. Given the growth in the space, and the potential to diversify the alternatives exposure, Capital Cities conducted a search.

Capital Cities issued a Broad Agency Announcement for the search and received 47 responses. Three semi-finalists were identified as a result of the review process. Phone interviews were conducted with the semi-finalists, however none of the Strategies proved to be a good fit for the Plan. Capital Cities recommended to maintain the current allocation to Wellington Real Total Return and to survey the marketplace again within the next few years in order to further assess opportunities to diversify the Alternatives' component of the Indiana Target Date Funds.

### **Ironbridge SMID Cap Fund Memo**

Mr. Zeni presented a memo on the Ironbridge SMID Cap Fund. The Fund provides participants with active exposure to small- and mid-cap stocks. The Fund represented \$30.1 million, or 2.9% of Plan assets, as of March 31, 2015. The Fund's three- and five-year performance has lagged its peers and the benchmark. As a result, there have been asset outflows from the Fund. Underperformance has primarily occurred due to the Fund's high quality focus during a period where low quality and leveraged companies have been rewarded. Despite these issues, the Fund enjoys a tenured portfolio team and a favorable expense ratio relative to peers. Capital Cities recommended that the Committee place the Fund on Watchlist. Mr. Jackson moved to place the Fund on Watchlist given the underperformance and asset outflows. Mr. Frick seconded the motion. The Watchlist status was approved unanimously. Capital Cities will continue monitoring the Fund and look for stable asset flows and improved performance.

### **Scout Unconstrained Fixed Income Memo**

Ms. Black presented a memo on the Scout Unconstrained Bond Fund. The Scout Unconstrained Bond Fund is an active fixed income Fund managed by Reams in Columbus, Indiana. The Fund is part of the Indiana Flexible Bond Fund as well as a component of the Indiana Target Retirement Funds. The Fund has experienced significant short-term underperformance over the last year.

Ms. Black noted that the Fund is a truly active fixed income strategy and its construction will more often than not have a different performance profile from the benchmark, the Barclays Aggregate Index. While the recent underperformance has been disappointing, it is not outside the realm of expectations, particularly given the current fixed income market dynamics and Ream's portfolio construction compared to that of the Barclays Aggregate Index and peers.

Reams began 2014 with the thought that interest rates would be rising in the near future. Strong employment figures, consumer sentiment, and strong corporate earnings all supported Ream's thought that a rate hike was imminent. In this environment, Reams felt it was prudent to implement a lower duration, which would shield investors from negative returns resulting from a rate hike.

In 2014, interest rates actually continued to fall. This resulted in very strong performance for the Barclays Aggregate Index, and also very weak performance for the Scout Unconstrained Bond Fund.

That said, Reams strongly believed that the potential risk of reaching for yield outweighed the potential benefit, particularly given the low coupon rates offered in the market in light of an uncertain rate environment.

Capital Cities still maintains a positive view on Reams and the Scout Unconstrained Bond Fund. There have been no qualitative changes at Reams and asset levels are at all-time highs. Capital Cities will continue to monitor performance closely, but no action is necessary at this time.

### **PIMCO Total Return/Unconstrained Bond Watchlist Updates**

Ms. Black provided an update on PIMCO. Ms. Black reminded the Committee that PIMCO presented at a special Committee meeting on March 19, 2015 given the recent changes at the firm.

The PIMCO Total Return and Unconstrained Bond Funds were placed on Watchlist status in February of 2014 by the Committee. The PIMCO Unconstrained Bond Fund serves as an underlying component of the Indiana Flexible Bond Fund, while the PIMCO Total Return Fund is offered to participants on a stand-alone basis. Ms. Black provided a review of the situation. It was discussed that in January of 2014, Co-CIO Mohamed El-Erian announced his departure from the firm, creating a domino effect of organizational changes, warranting Watchlist. Bill Gross, Founder and Managing Director of PIMCO, submitted his resignation on September 26th. He immediately left the firm and accepted a position at Janus Capital. Ms. Black also noted that on January 12, 2015, a key Portfolio Manager of the PIMCO Unconstrained Bond Fund, Saumil Parikh, announced his resignation. Despite the personnel departures, PIMCO continues to be well-resourced with highly regarded investment professionals. In fact, PIMCO hired 28 investment professionals on a net basis since the beginning of 2014. Ms. Black also noted that firm asset outflows appear to be stabilizing. The firm remains large with \$1.59 trillion in assets under management.

Capital Cities will continue to closely monitor PIMCO on Watchlist status, but there have been no material changes since the special March 19 meeting that would warrant action.

### **Indiana Target Date Funds**

Mr. Zeni noted that during the November, 2014 meeting, the Committee approved the 2015 glide path roll-down for the custom Target Date Funds. Furthermore, the Indiana 2015 Fund will be mapped to the Indiana Retirement Fund and a new Indiana 2060 Fund will be created for Plan participants. These changes will be included in the upcoming participant communication.

### **Neuberger Berman Global Thematic Opportunities Watchlist Update**

Mr. Zeni discussed that the Neuberger Berman Global Thematic Opportunities Fund was placed on Watchlist status in August of 2014 given short-term performance (last three-year time period) and asset outflows. The Neuberger Berman Global Thematic Opportunities Fund serves as an underlying component of the custom Target Date Funds and is not offered to participants on a stand-alone basis. The Fund's short-term performance has trailed the median peer performance and its benchmark. Underperformance has largely occurred from the Fund's emerging markets exposure, allocations to inflation-related strategies (e.g., gold), and cash holdings. As a result of the recent underperformance, the Fund has experienced asset outflows. Most recently, assets decreased to approximately \$200 million within the Strategy.

During the February meeting, the Committee elected to replace Neuberger Berman Global Thematic Opportunities with Epoch Global Shareholder Equity. The change will be concurrent with the Perkins

Mid Cap Value replacement & Target Date Fund roll-down.

**Empower Plan Participant Letter**

Mr. Waddell presented the first draft of the Empower Plan Participant Letter that will detail the upcoming changes to the Plan. The communication includes the Perkins Mid Cap Value termination/replacement, the Neuberger Berman Global Thematic Opportunities termination/replacement, as well as the changes to the Indiana Target Date Funds. Mr. Beisel also added commentary and noted that he will be finalizing the draft for the upcoming communication.

**VI. Old Business**

None.

**VII. New Business**

Ms. Sheridan provided an update on the Hoosier S.T.A.R.T. program's social media campaigns. There is a mobile application that has launched and the program now has a Twitter profile.

Auditor Crouch proposed the idea of moving the standard meeting time to the third Thursday of the second month of the quarter in order to avoid holidays. Mr. Frick moved to approve the new schedule. Mr. Jackson seconded. The new schedule was approved unanimously.

**VI. Adjournment**

There being no further business before the Committee the meeting was adjourned at 10:20 a.m. The next meeting is August 20, 2015.