UNIVERSITY OF MAINE SYSTEM
Board of Trustees

Investment Committee

December 2, 2019
Phone Conference Meeting

Present: **Committee Members:** Kelly Martin, Chair, Sven Bartholomew, James Erwin, Mark Gardner, Trevor Hustus, and Betsey Timm. **Non-Voting, Non Trustee Committee Members:** Robert Blackwood. **Staff:** Tracy Elliott, Ellen Doughty, Chip Gavin, David Demers, Gretchen Catlin, and Ryan Low. **Others:** Chris Klapinski – NEPC, Kelly Regan – NEPC, Jay Roney – NEPC, Michael Pratico – CAPTRUST, Barry Schmidt – CAPTRUST, and Anne Devine.

Absent: James Donnelly.

Trustee Martin, Chair, called the meeting to order and welcomed everyone.

FY2021 Endowment Spending Rate

UMS Vice President for Finance and Controller, Ms. Tracy Elliott provided information on the Endowment Spending rate for FY20 and recommended the same rate for FY21. The Endowment Spending rate has been 4.5% since FY13 and is estimated to generate a distribution of $5.3 million for FY20, including $4.2 million for endowed spending and $1.1 million for internal management fees. The estimated UMS FY20 effective spending rate (which is net of the management fees) is 3.3%.

NEPC Rate of Return Assumption: NEPC reviewed return expectations for the Managed Investment Pool in June 2019. Their analysis, based on market returns, suggests a return expectation in the range of 6.2% to 7.2% (down from a range of 6.2% to 7.3%). This range does not include investment management fees or assumptions for active manager out-performance. As such, they can substantiate a return assumption of 7.5%, noting significant volatility around this each year.

FY21 Endowment Distribution Rate per Share and Estimated Budget: Using the endowment spending rate approved at this December 2nd meeting, management will provide estimated distribution amounts for FY21 to the Committee at its next meeting.

Action Taken:
On a motion by Trustee Hustus, which was seconded by Trustee Gardner, the Investment Committee approved the following resolution:

> The Board of Trustees, acting through the Investment Committee, approved an endowment spending rate of 4.5% for FY21.

Enterprise Risk Management Update
Gretchen Catlin, UMS Risk Manager, presented an update to the Investment Committee regarding the implementation of Enterprise Risk Management (ERM). Previous guidance from the Board of Trustees has been reflected in the development and implementation of the ERM program. Based on Trustee suggestions, Risk Management is preliminarily tracking 15 University risks. One of those risks is assigned to the Investment Committee for oversight. Each risk is also assigned a leader who is

responsible for implementing mitigation and control strategies. In preparation for this meeting, Ms. Caitlin worked with NEPC and Ms. Elliott to review the risk of investment decline including standard deviation, probabilities, and potential dollar impacts for the three portfolios and briefed the Committee on those results.

Defined Contribution – Investment Policy Statement.

Michael Pratico and Barry Schmitt, Senior Vice Presidents with CAPTRUST Financial Advisors, provided several updates to the Investment Policy Statement. These updates are the result of changes to the data utilized in CAPTRUST's evaluation methodology along with some formatting changes including the removal of Appendices A through D which were replaced with a separate document entitled the CAPTRUST Investment Policy Monitoring Document.

Action Taken:

On a motion by Trustee Hustus, which was seconded by Trustee Erwin, the Investment Committee approved the following resolution:

> The Board of Trustees, acting through the Investment Committee, approved the CAPTRUST recommended updates to the Investment Policy Statement.

Defined Contribution Plans Review.

Mr. Pratico and Mr. Schmitt also provided a quarterly update regarding the Defined Contribution Plan.

Industry Update: CAPTRUST highlighted the industry topic of data privacy regarding the ownership and value of participant data, and the increasing interest in how service providers protect and use participant information. Several recent retirement plan lawsuits have included plaintiff claims alleging that fees charged by service providers are failing to consider the value of access to participant data for marketing purposes. The Committee considered TIAA's bonding and the availability of a liability waiver and CAPTRUST committed to requesting this information from TIAA.

Market Commentary: CAPTRUST noted that most asset classes added to their 2019 gains in the third quarter, despite attention-grabbing headlines and fears of waning global economic growth.

Plan Investment Review: CAPTRUST reviewed with the Committee all funds consistent with the process outlined in the Investment Policy Statement. All funds, with two exceptions, are currently in "good standing" based on the CAPTRUST scoring methodology. All funds were discussed with emphasis on the following:

- **Carillon Eagle Small Cap Growth** - The fund is marked "consider for termination" based on the CAPTRUST scoring methodology. CAPTRUST continues to recommend holding the fund based on the experienced investment team, consistent investment process and long-term performance. With the exception of 2013, the strategy remained in the top half of the peer group from 2009-2017 and avoided any significant underperformance versus the benchmark.

  Following solid results in 2017, the strategy modestly lagged the benchmark in 2018. All of the 2018 underperformance occurred in the first half. The strategy was roughly in-line with the benchmark during the sharp Q4 2018 sell-off. Through the first half of 2019, the strategy was slightly ahead of the benchmark in a very strong rally for small cap growth (+20%). Q3 was a difficult period as the strategy lagged the benchmark by over 200 basis points. Underperformance was driven by negative stock selection in healthcare, financials, and consumer discretionary. CAPTRUST will monitor the performance closely but is not recommending any action at this time.

- **DFA Emerging Markets**: The fund is marked for review based on CAPTRUST scoring methodology. The strategy's year to date results lagged the benchmark and were in the fourth quartile of the peer group. While recent performance has been challenging, the strategy's five-year results are only slightly trailing the benchmark and are roughly in-line with the peer group. CAPTRUST continues to recommend this strategy.

- **CREF Stock**: For participants looking for a largely actively managed Global Equity fund, CREF Stock continues to be an appropriate choice. The fund is well diversified across several asset classes and has expenses well below industry averages.

- **TIAA Real Estate**: Real Estate provides additional diversification for participants and the TIAA Real Estate fund offers a unique ability to invest directly in real estate as opposed to traditional REIT funds. CAPTRUST and the Committee continue to believe TIAA Real Estate is an appropriate option within a participant choice retirement plan.

Outsourced Chief Investment Officer Discussion.

Chris Klapinsky of NEPC provided an educational presentation on Outsourced Chief Investment Officer (OCIO) investment consulting. Mr. Klapinsky discussed what OCIO is, the benefits and considerations, costs, and provided information about NEPC's OCIO capabilities.

Under the NEPC relationship model, there are two services, advisory (which UMS currently utilizes) and discretionary (OCIO). In the advisory model, NEPC advises on all four fiduciary functions - Investment Policy Statements (IPS), Asset Allocation (AA), Investment Manager Selection and Implementation, with the client and its Board being the ultimate decision authority and has responsibility for executing those decisions. Under the discretionary model, NEPC still advises to the IPS and AA and the client still controls the ultimate decision. However, under the discretionary model, the client could give authority to NEPC to select the investment manager(s) to implement the asset allocation as well as direct the manager(s) and custodian to trade the funds. There are different options available to clients when deciding to outsource with NEPC. UMS, for example, could control the IPS, AA and manager selection for the Pension and Operating Funds, but delegate implementation to NEPC. For the MIP, UMS could delegate both manager selection and implementation to NEPC. NEPC is flexible in their approach when working with clients.

Mr. Klapinsky provided background on NEPC's capabilities with OCIO. As of June 30, 2019, NEPC managed 131 investment programs for 65 clients totaling $29.5 billion in assets. As of June 30, 2019, NEPC's discretionary team consisted of 3 Portfolio Strategists and 16 operational professionals.

NEPC described some of the benefits to UMS if the decision were made to outsource some of its fiduciary functions. The first is potentially lower fees and costs. NEPC estimated that under their OCIO model, roughly $250 thousand in investment manager fees could be saved as NEPC has negotiated lower fees for OCIO clients. Manager fee savings can offset any additional investment consulting fees. Secondly, NEPC would be able to track UMS assets daily utilizing their OCIO operational systems. This would allow NEPC to monitor compliance with the IPS targets and ranges and make adjustments immediately if needed. It would also allow NEPC to make tactical decisions within IPS ranges if a market opportunity presented itself. Lastly, NEPC documents all trades and decisions which is essential for audit and oversight purposes.

Mr. Klapinsky noted some of the areas that NEPC would improve upon under the OCIO model:

- Swapping out some managers for others that have lower negotiated fees.
- Looking to add more global equity managers.
- Reducing the Global Asset Allocation exposure as NEPC could manage some of the tactical asset allocation decisions.
- Reviewing the existing hedge fund of fund mandate as well as discussing appetite for private markets.

NEPC Portfolio Performance Reviews.

Kelly Regan and Jay Roney of NEPC provided a brief performance review for all three portfolios for the quarter ended September 30, 2019, with the following highlights:

Managed Investment Pool (MIP): The MIP returned -0.4% fiscal-year-to-date ending September 30, 2019. The MIP has a higher allocation to non-US equity compared to the Operating and Pension Funds which led to the negative returns. During this period, managers detracted 60 basis points of value as only 5 out of 13 active managers outperformed their respective benchmarks (excludes Timber and Private Equity). In the month of October 2019, the MIP returned 1.7%, bringing the fiscal-year-to-date return to 1.3% and the calendar year-to-date return to 11.9% outpacing the expected return goal of 7.5%.

Defined Benefit Pension Fund: The Defined Benefit Pension Fund returned 1.2% fiscal-year-to-date ending September 30, 2019. During this period, managers added 40 basis points of value as all but one active manager outperformed their respective benchmarks. In the month of October 2019, the Pension Fund returned 1.0%, bringing the fiscal-year-to-date return to 2.1% and the calendar year-to-date return to 10.7% outpacing the expected return goal of 6.25%. Additionally, over the calendar year-to-date time frae, investment gains outpaced net Fund outflows.

Operating Fund: The Operating Fund returned 0.6% fiscal-year-to-date ending September 30, 2019. Over all trailing time periods, managers in aggregate have kept pace with their benchmarks as measured by the Composite vs. Allocation index. In the month of October 2019, the Operating Fund returned 0.6%, bringing the fiscal-year-to-date return to 1.2% and the calendar year-to-date return to 5.8% outpacing the expected return goal of 4%.

Adjournment

Tracy Elliott for
Ellen N. Doughty, Clerk