UNIVERSITY OF MAINE SYSTEM
Board of Trustees

Investment Committee

February 27, 2020
UMS Rudman Conference Room 253, Estabrooke Hall, Orono

Present: Committee Members: Sven Bartholomew, Chair Pro tem; Kelly Martin (by phone) James Erwin (by phone), Mark Gardner (by phone), and Betsey Timm (by phone). **Non-Voting, Non Trustee Committee Members:** Robert Blackwood (at USM) and Peter Handy (at USM). **Staff:** Tracy Elliott, Heather Massey, and Ryan Low (at UMA). **Others:** Kelly Regan – NEPC, Jay Roney – NEPC (at USM), Michael Pratico – CAPTRUST (at USM), Barry Schmidt – CAPTRUST (by phone), and Jean Deighan.

Absent: James Donnelly and Trevor Hustus.

Trustee Bartholomew, Chair Pro tem, called the meeting to order and welcomed everyone.

Contributory Retirement Plans – Investment Advisory Services Contract Extension.
UMS Vice President of Finance and Controller, Ms. Tracy Elliott provided information on the UMS Investment Advisory Services contract extension for the Defined Contribution plans. Through a competitive procurement process, UMS engaged CAPTRUST Financial Advisors (CAPTRUST) to perform investment advisory services commencing January 2, 2013. The contract allowed for a set 7-year period with three 1-year extensions. The contract is currently in its eighth year and management recommends that the Investment Committee approve the extension of CAPTRUST for calendar year 2021.

This extension would be based on the terms of the Request of Proposal (RFP) issued in 2012 and CAPTRUST's pricing provided at that time. CAPTRUST fees are $99,995 for calendar year 2020 and the contract allows for a Consumer Price Index for all Urban Consumers (CPI-U) based annual increase capped at 5% annually, for a maximum annual fee of $104,995 for calendar year 2021.

> On a motion by Trustee Erwin, which was seconded by Trustee Timm, the Board of Trustees, acting through the Investment Committee, approved the extension of CAPTRUST's appointment as the University of Maine System's investment advisers for the Contributory Retirement Plans for calendar year 2021.

FY2021 Endowment Spending Rate.
Ms. Elliott provided an update on the FY2021 Endowment Spending Rate. At its December 2, 2019 meeting, the Investment Committee reviewed and supported the recommended fiscal year 2021 (FY21) endowment spending rate of 4.5% which is estimated to generate nearly $5.9 million for the fiscal year. This total includes $4.7 million for endowed spending and $1.2 million for management fees.

Market Update
Kelly Regan and Jay Roney, with NEPC, provided a market update on calendar year 2019 which was an exceptional year for all assets classes as returns were positive across the board. Global Equites experienced double digit returns in 2019 with US Equities favoring the best return at 31.5% (S&P 500). Fixed Income also experienced strong returns as U.S. yields fell significantly in 2019 causing

prices to increase. U.S. Fixed Income as measured by the Barclays Aggregate was up 8.7% in 2019.

NEPC also reviewed their forward-looking outlook and discussed their four themes that they believe will drive markets going forward. The one new theme of Permanent Interventions was discussed in detail as the remaining three themes were consistent with past years and had been reviewed with the Committee in previous meetings. In general, Permanent Interventions captures NEPC's belief that both Global Central Banks and Global Fiscal Policy have the potential to continue to support market returns. These policies may continue to push fixed income yields lower which may support higher equity valuations. Additionally, NEPC reviewed the current opportunities they see in the marketplace and stated that not all are applicable for the System's portfolios, but the ones that were applicable have been implemented in the portfolios. Those opportunities are reduced lower quality credit exposure (High Yield), overweight Emerging Market Equities, and fund Emerging Market Local Debt (exposure is currently through flexible Global Asset Allocation managers). In addition, NEPC briefly commented on the coronavirus and the recent impact to the markets.

Asset Allocation Review.

Ms. Regan and Mr. Roney reviewed the asset allocation for all three portfolios (Managed Investment Pool, Pension Fund and Operating Fund). There were no recommended changes to the Pension or Operating Funds' asset allocation. However, NEPC made slight asset allocation recommendations for the Managed Investment Pool (MIP) which focused on the construction of the equity portfolio. NEPC recommended to maintain the 61% target allocation to equity, but to re-distribute funds from large cap, small cap and international developed equity to a global equity manager. A global equity manager would provide potential for more alpha and more flexibility as global equity managers can invest across global equity markets. NEPC's recommended hiring Walter Scott which is a current manager in the Pension Fund. Additionally, NEPC recommended replacing a current international developed equity manager, Globeflex, with JO Hambro. NEPC's analysis showed the potential for higher alpha with no additional risk with the change. Additionally, the MIP focuses on Environmental, Social and Governance (ESG) factors and both Walter Scott and JO Hambro incorporate ESG into their investment process. The recommended reallocation would therefore improve the overall ESG profile of the MIP.

NEPC provided their forward-looking expected returns for the Pension and Operating Fund based on NEPC's capital market assumptions for the asset classes that the Funds' invest in. The Pension Fund is expected to return 5.7% over the next 30 years on a beta only perspective. NEPC expects the managers in the Pension Fund will provide 40-50 basis points of alpha and can support the Pension Fund's return goal of 6.25% based on their assumptions. The Operating Fund is expected to return 4.0% over the next 30 years on a beta only perspective. NEPC expects the managers in the Operating Fund will provide 20-30 basis points of alpha and can support the Operating Fund's return goal of 4.00% based on their assumptions. The MIP is expected to return 6.5% over the next 30 years on a beta only perspective. NEPC expects the managers in the MIP will provide 40-50 basis points of alpha and, therefore, cannot support the MIP's current return goal of 7.5% based on their assumptions. Ms. Elliott noted that a reduction of the supported return assumption would have negative financial implications for the University related to the actuarial valuation of the Other Post Employment Benefits (OPEB) Trust, which invests in the MIP. Based on last year's valuation results, a 50 basis point decrease in the return assumption, which is used as the valuation discount rate, has about a $12 million impact on the liability.

> On a motion by Trustee Gardner, which was seconded by Trustee Erwin, the Board of Trustees, acting through the Investment Committee, approved the following asset allocation recommendations:

Managed Investment Pool

1. Add a 10% allocation to global equity by reducing large cap equity (5%), small cap equity (1%), international developed equity (3%) and international small cap equity (1%).
2. Implement the global equity allocation through Walter Scott's Global Equity strategy which is currently utilized in the Pension Fund.
3. Diversify the international developed equity manager line-up with the addition of JO Hambro International Select and elimination of Globeflex International All Cap.

NEPC Portfolio Performance Reviews.

Ms. Regan and Mr. Roney provided a brief performance review for all three portfolios for the quarter ended December 30, 2019, with the following highlights:

Managed Investment Pool (MIP):

The Managed Investment Pool (MIP) returned 5.7% fiscal-year-to-date ending December 31, 2019. The MIP has a higher allocation to equity compared to the Operating and Pension Funds which led to the higher returns. During this period, managers detracted 60 basis points of value as 7 out of 13 active managers underperformed their respective benchmarks (excludes Private Equity). Most of these managers that underperformed had a value, quality or conservative investment approach which was out of favor during the recent market rally. In the month of January 2020, the MIP returned -0.6%, bringing the fiscal-year-to-date return to 5.1%.

Defined Benefit Pension Fund:

The Defined Benefit Pension Fund returned 4.8% fiscal-year-to-date ending December 31, 2019. During this period, managers added 10 basis points of value with all but one active manager outperforming their respective benchmarks. In the month of January 2020, the Pension Fund returned 0.4%, bringing the fiscal-year-to-date return to 5.3%. Additionally, over the last quarter, fiscal year-to-date and the trailing one-year time frame (as of December 31, 2019), investment gains outpaced net Fund outflows.

Operating Fund:

The Operating Fund returned 2.6% fiscal-year-to-date ending December 31, 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 January 2020, the Operating Fund returned 0.3%, bringing the fiscal-year-to-date return to 2.9%. At the end of 2019, the asset allocation of the Operating Fund was off policy targets with an underweight to the Liquidity Pool, however a sizable cash inflow in January 2020 brought the Liquidity Pool above policy targets. NEPC will be working with the System on potential rebalancing.

Defined Contribution Plan Quarterly Review.

Michael Pratico, Senior Vice President, and Barry Schmitt, Principal, with CAPTRUST Financial Advisors, provided a review of administrative items, topical spotlights, and a quarterly update of the Defined Contribution Plans.

CAPTRUST provided an overview of the Setting Every Community up for Retirement Enhancement (SECURE) ACT provisions and the potential impact on the UMS plan including:

- Increase age at which retirement plan participants need to take Required Minimum Distributions from 70.5 to 72.

- Permit penalty-free withdrawals to defray the cost of having or adopting a child.
- Safe harbor permits selection of an in-plan lifetime income solution.

CAPTRUST followed up on a prior Committee due diligence discussion about TIAA and participant data. According to TIAA, they do not pro-actively solicit or cross sell products or services unless the participant engages them in this area.

Regarding the markets, all asset classes posted solid results for calendar year 2019. U.S. and international stocks and bonds performed well as the Federal Reserve and other central banks implemented policies to counter fears of slowing global economic growth. U.S. stocks posted their best year since 2013, aided by easing U.S.-China trade tensions and a boost from the Federal Reserve. CAPTRUST touched upon the impact of the coronavirus on the market in 2020.

The Committee and CAPTRUST then reviewed all funds consistent with the process outlined in the Investment Policy Statement. All funds, with two exceptions, were currently “in good standing” based on the CAPTRUST scoring methodology. Emphasis was placed on the following:

JHancock Disciplined Value experienced short-term underperformance due to a strict value discipline when many peers invested in more growth oriented stocks.

Vanguard Institutional Target Retirement Series Funds finished off a solid year in 2019 as those funds performed in line with their benchmark and mostly outperformed peers. The series’ performance was driven by its equity portfolio in the fourth quarter as global equity markets moved higher during the period.

Carillon Eagle Small Cap Growth: CAPTRUST continues to recommend this strategy. This is a very experienced investment team that has recently faced challenges in small cap growth. When looking at recent performance, it is important to understand the dynamics of the small cap growth asset class. Some of the peer group has benefitted from large sector bets and more exposure to higher growth stocks such as biotech. Over a full market cycle, CAPTRUST believes that the more conservative approach used by the team at Eagle should pay off although it has been a headwind recently.

Almost all the strategy’s calendar 2019 underperformance occurred in Q3. Performance stabilized in Q4, as the strategy was in-line with the benchmark and near the top quartile in the peer group. The Committee agreed with CAPTRUST’s recommendation to continue to hold the fund.

DFA Emerging Markets: The fund is marked for review based on CAPTRUST’s scoring methodology. 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.

Vanguard Institutional index: fund has now surpassed $100 million in assets. This is a threshold to qualify for a lower share class- the Vanguard institutional index Plus. CAPTRUST and the System will work with TIAA to proceed with this share class change once the conversion to the new contracts are completed in mid-March.

Socially Responsible investing: CAPTRUST touched on this topic and provided thoughts on the current core offering (CREF Social Choice) along with appropriateness of the brokerage window usage for those participants that want to invest in a specific socially responsible manner.

Other items discussed:
TIAA Bonding: At the last quarterly meeting, a question was asked about TIAA's bonding. Below is their response:

TIAA, FSB (TIAA Trust) is covered by TIAA's comprehensive corporate insurance coverage program. Current coverage details include:

1. Errors and Omissions coverage of at least $10 million. This coverage is underwritten by U.S. Specialty Insurance Company (a subsidiary of HCC Insurance Holdings, Inc.). The policy provides coverage for errors and omissions committed by company employees.

2. Fidelity Bonding with coverage limits of at least $10 million. Federal Insurance Company is the lead underwriter for this coverage. The policy provides protection against fidelity losses committed by company employees as well as the theft of money or securities.

3. Workers Compensation coverage of at least $1 million. This coverage is underwritten by QBE (Stonington Insurance Company and Praetorian Insurance Company). The policy provides coverage for employee injuries in compliance with state regulations.

4. General Liability primary coverage of at least $2 million. This coverage is underwritten by Federal Insurance Company. The policy provides coverage for bodily injury, property damages and personal injury claims.

In addition, TIAA maintains significant additional property and casualty insurance coverage to protect the assets of the company against lawsuits and other hazards.

TIAA solicitation guidelines: At the last quarterly meeting, a question was asked about TIAA's solicitation policy. Below is their response:

- TIAA financial consultants will only provide information about services beyond the plan if they are asked by the individual. They do not solicit or cross-sell products and services.

Adjournment

Tracy Elliott for
Ellen N. Doughty, Clerk