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## **PENSION FUND COMMITTEE**

### *Minutes of Meeting*

**August 17, 2017**

The Sussex County Pension Fund Committee met on August 17, 2017 at 10:00 a.m. in the County Council Chambers, Georgetown, Delaware. Those in attendance included members: Gina Jennings, Karen Brewington, Kathy Roth, Hugh Leahy, and Kathleen Ryan. Also in attendance was Patrick Wing of Marquette Associates, the County's Pension Investment Consultant. Committee members Todd Lawson and David Baker were unable to attend.

On August 9, 2017, the Agenda for today's meeting was posted in the County's locked bulletin board located in the lobby of the County Administrative Offices, as well as posted on the County's website.

Ms. Jennings called the meeting to order.

1. **Approval of Minutes**

The minutes of the May 18, 2017 meeting were approved by consent.

2. **Performance Reports of the Pension and OPEB Funds**

Mr. Wing distributed copies of a booklet entitled, "Sussex County Quarterly Performance Report as of June 30, 2017". The report includes information regarding the market environment for the second quarter of 2017, as well as quarterly and annual performances of the Pension and OPEB Plans. The report should be referenced for a detailed analysis.

Mr. Wing referred members to Exhibit II – Sussex County Employee Pension Plan. As of June 30, 2017, the ending market value of the Pension Plan was \$82.8 million. The portfolio saw a second quarter investment gain of \$2.2 million and realized a 2.6 percent return (net of investment management fees) versus a policy index of 2.7 percent. The fund underperformed its policy index by approximately 10 basis points, DuPont and the portfolio's value tilt detracted from performance, and the fund's overweight to equities added to returns.

The Pension Fund had an investment gain of \$5.25 million year-to-date that was a byproduct of the strong equity market, and a five-year gain of \$29 million. It was noted the fund was within investment policy ranges for each asset class.

Distribution of returns for various time periods were discussed. The total fund composite for the second quarter was 2.6 percent versus a median return of 2.8



percent, with a policy index of 2.7 percent. The fund has a higher proportion allocation to U. S. equities versus non-U.S. equities than to its peers. Year-to-date, the fund increased 6.6 percent versus a policy index of 7.1 percent; this underperformance was mostly due to the State Pool. For the past one-year, Mr. Wing noted that the fund has had good returns and is ahead of its assumed rate of return of 7.25 percent.

The total equity composite is weighted toward index funds with the Vanguard large cap index fund added in October 2016 as part of the portfolio restructuring. DuPont Capital realized a 2.8 percent return (net of fees) versus a 3.1 percent policy index for the last three months of the quarter, or lagging by 30 basis points. For the past 7 years, returns also lagged by 30 basis points, or 15.1 percent versus a 15.4 percent policy index. Mr. Wing reported that although DuPont ranked in the top third within their peer group, they have not outperformed. He noted that this was indicative of how difficult it is for U. S. large cap equity managers to add value. It was noted that the State comprises 50 percent of the pension fund.

Mr. Wing referred members to Exhibit III - Sussex Post-Employment Benefit Plan. As of June 30, 2017, the ending market value of the OPEB Plan was \$35.5 million and realized a second quarter gain of approximately \$900,000. The Plan realized a return of 2.6 percent (net of investment management fees) versus a policy index of 2.7 percent. The portfolio underperformed its policy index by 10 basis points. Although the portfolio's value tilt detracted from the fund's performance, its overweight to equities added to returns.

Regarding the summary of cash flows, Mr. Wing reported that it had been a good environment for capital markets in general. The OPEB Fund realized an investment gain of \$11.5 million over the last five years. Year-to-date, the OPEB fund performed slightly better than the Pension Fund due to the State Pool; the fund lagged behind its policy index due to investment management fees.

Mr. Wing reported on the annualized returns, specifically noting two new global equity managers, Artisan Global Opportunities Fund (growth manager) and Dodge & Cox (value manager), both of whom have added value to the portfolio during the second quarter.

Mr. Wing discussed two handouts for the Pension and OPEB Fund showing their performance as of July 31, 2017. The Pension Fund, for the quarter, was up 1.6 percent, which is in line with its policy index; international equities outperformed U. S. equities during July. Year-to-date, the total fund composite of 8.4 percent slightly lagged its policy index due to DuPont and the State, but ahead of the assumed rate of return of 7.25 percent. The market value of the Pension Fund at the end of July was \$84.1 million. Value managers for the OPEB Plan have lagged slightly for July, and global managers have performed well. Year-to-date, the OPEB Plan increased by 8.6 percent, which is also ahead of the 7.25 percent assumed rate of return.

### 3. **Additional Fund Contributions & Allocation**

Mr. Wing distributed copies of a booklet entitled, "Equity Manager Search – Sussex County Pension Plan – August 17, 2017". At May's meeting, the Pension Committee requested Marquette to present possible replacements for DuPont Capital as a result of

their underperformance. Currently, the Pension Fund has two U. S. large cap equity managers – DuPont Capital and Vanguard. He noted that Vanguard was added in October 2016 and DuPont has slightly lagged its benchmark (net of fees) overall in both the short- and long-term periods. In performing a search, Marquette Associates considers both quantitative and qualitative aspects, i.e. firms that have stable portfolio management teams, consistent execution of investment process, and downside protection.

Marquette presented three portfolio managers for the Committee’s consideration: Atlanta Capital (High Quality Select Equity); Coho Partners (Relative Value Equity), and Vanguard (S & P 500 Index Fund). One similarity between Atlanta and Coho is that both look for high quality companies. Included in the presentation were Manager Information as of June 30, 2017 (Portfolio Management, Investment Process, and Risk Management), Top 10 Holding Percentages, Strategy Comparisons (Sector Distribution and Market Capitalization), Cumulative Returns Annualized Percentages (over various time periods), Yearly Returns Percentages, Up/Down Market Participation – 10 years as of June 2017 (including downside protection), Risk Statistics as of June 2017, and Pros and Cons.

Mr. Wing reported that although Atlanta’s stated fees are 70 basis points on the first \$50 million, they reduced their fee to 50 basis point assuming a portfolio value of \$10 million. Coho’s stated fee is 60 basis points, but is negotiable and, most likely, 50 basis point would be acceptable. Both Atlanta and Coho are concentrated managers, having only 27 holdings.

Concern and questions were expressed by the Committee, with Mr. Wing giving further explanation as to the manager’s high investment fees, their concentrated/limited number of holdings, what was involved with a separately managed account, the Russell 1000 versus S & P 500, and downside protection.

The question was raised as to what was included in the State’s 46 percent equity portfolio/holdings. After discussion, it was the consensus of the Committee that this information was needed prior to the Committee making possible manager changes; this information will be provided at the November meeting.

Mr. Wing distributed booklets entitled, “Asset Allocation Update & Portfolio Options – Sussex County – August 17, 2017”. He explained that, each year, Marquette performs capital market projections across the major asset classes that their clients are invested in; for the County, this would include fixed income, as well as U. S. and non-U.S. equities. Currents yields for fixed income are 2.1 percent, which is a reasonable return to expect over the next 5 years. Interest rates are expected to rise slightly, which should result in years 6 to 10 realizing a better performance, possibly seeing 2.5 percent over the next 10 years. He further explained that over the next ten years, a return of 6 to 7 percent for U. S. equities was expected. For Non-U.S. stocks, average returns are expected for the next 10 years. Portfolio options and projections for the Pension fund were discussed reflecting a target allocation increase of 2 percent (12 to 14 percent) to Non-U.S./international equities from U. S. equities. Similar information was presented for the OPEB Fund; it was noted that the OPEB Fund is already at a target allocation of 14 percent in international equities.

Mr. Jennings reiterated that the County is contributing an additional \$5,000,000 to both the Pension and OPEB Funds. With the additional contribution to the Pension Fund, it is estimated that the fund would be 84 percent funded.

A Motion was made by Ms. Ryan, seconded by Ms. Roth, to recommend to the Sussex County Council to increase the international target allocation for the Pension Fund from 12 to 14 percent.

Motion Adopted: 5 Yeas.

Vote by Roll Call: Ms. Brewington, Yea; Ms. Roth, Yea;  
Mr. Leahy, Yea; Ms. Ryan, Yea;  
Ms. Jennings, Yea

A Motion was made by Mr. Leahy, seconded by Ms. Ryan, to recommend to the Sussex County Council to approve Option 4 for the Pension Plan, which includes moving funds from Dupont Capital to an index fund, with the additional \$5,000,000 contribution, to reflect: DuPont Capital – 0 percent; Vanguard S&P 500 Index – 21.9 percent; Vanguard Mid Cap Value Index – 5.2 percent; Vanguard Extended Mkt Index – 5.2 percent; Vanguard Total Int'l Stock Mkt Index – 4.0 percent; Wilmington Trust Fixed Income – 12.4 percent; Cash – 1.8 percent; and DE State Pool – 49.5 percent.

Vote by Roll Call: 5 Yeas.

Vote by Roll Call: Ms. Brewington, Yea; Ms. Roth, Yea;  
Mr. Leahy, Yea; Ms. Ryan, Yea;  
Ms. Jennings, Yea

A Motion was made by Mr. Leahy, seconded by Ms. Ryan, to recommend to the Sussex County Council to approve Option 1 for the OPEB Plan, which will the rebalance the Plan without increasing the international target allocation, to reflect: Vanguard S&P 500 Index – 34.2 percent; Vanguard Small Cap Value Index – 6.7 percent; Vanguard Small Cap Value Index – 3.1 percent; Artisan Global Opportunities – 3.8 percent; Dodge & Cox Global – 3.6 percent; MFS Low Volatility Global – 6.4 percent; Vanguard Total Int'l Stock Index – 7.1 percent; Wilmington Trust FI – 34.1 percent; and Cash – 0.9 percent.

Motion Adopted: 5 Yeas.

Vote by Roll Call: Ms. Brewington, Yea; Ms. Roth, Yea;  
Mr. Leahy, Yea; Ms. Ryan, Yea;  
Ms. Jennings, Yea

Ms. Jennings and the Committee thanked Mr. Wing for his time in preparing the information presented today.

4. **Additional Business**

No additional business.

5. **Adjourn**

At 11:39 a.m., a Motion was made by Mr. Leahy, seconded by Ms. Roth, to adjourn.

Motion Adopted: 5 Yeas.

Vote by Roll Call: Ms. Brewington, Yea; Ms. Roth, Yea;  
Mr. Leahy, Yea; Ms. Ryan, Yea;  
Ms. Jennings, Yea

The next meeting of the Pension Committee is scheduled for November 16, 2017, at 10:00 a.m., in the Sussex County Council Chambers.

Respectfully submitted,

Nancy J. Cordrey  
Administrative Secretary