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PENSION FUND COMMITTEE

Minutes of Meeting

November 16, 2015

The Sussex County Pension Fund Committee met on November 16, 2015, at 10:00 a.m. in the County Council Chambers, Georgetown, Delaware. Those in attendance included members: Gina Jennings, Todd Lawson, Karen Brewington, Jeffrey James, David Baker, Hugh Leahy, and Kathleen Ryan. Also in attendance was Michael Shone of Peirce Park Group, the County's Pension Investment Consultant.

On November 6, 2015, 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 August 20, 2015 meeting were approved by consent.

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

Mr. Shone distributed copies of a booklet entitled, "Sussex County Investment Performance Report, September 30, 2015". The Investment Performance Report includes information regarding the market environment for the third quarter of 2015, as well as quarterly and annual performances of the Pension and OPEB Plans. Although the report should be referenced for a more detailed analysis, discussion highlights include:

Mr. Shone referred members to Market Environment – 3rd Quarter of 2015 (Tab 1).

The Year-Over-Year Real Gross Domestic Product (GDP) Growth has seen reasonably steady growth (inflation adjusted) of 1-1/2 to 2 percent, with a slight reverse in the third quarter both internationally and domestically. Although, historically over a 30 to 80 year timeframe, inflation has averaged approximately 3 percent, the 10-year breakeven inflation is projected to be 1.5 percent. The decline seen in the world economy has been primarily driven by China. Over the last 20 years, the year-over-year world trade volume has grown at approximately 5 percent, but the last two years has seen a significant decrease. In an effort to combat their sluggish economy, China took action to devalue their currency, which allows their goods to be less expensive and more attractive to buyers.

Equities, for the quarter and year, all saw negative returns; U.S. Equities: -7.2 for the quarter and -5.4 for year-to-date; international equities: -10.2 for the quarter and -5.3 for the year-to-date; and emerging market equities: -17.9 for the quarter and -15.5 for year-to-date. U.S. bonds were slightly positive for the quarter (1.2 percent) and for the year-to-date (1.1 percent). Commodities have performed extremely poorly for the third quarter (-11.8) and -17.2 for year-to-date. Within U.S. Equity returns, growth stocks continued to outperform their value counterparts among large-caps, but value was the better performer within small-caps. Large caps fared well amid mid and small caps for the quarter, although they were the worst performers during August.

Mr. Shone directed members to the Pension Fund Performance Report (Tab II).

As of September 30, 2015, the ending market value of the Pension Plan was $70.7 million and realized a third quarter loss of $3.5 million, and a 1 year (October 1, 2014 thru September 30, 2015) loss of $296,000. The quarterly performance was in line with the Policy Index; underperformance by DuPont was offset by outperformance by the State Investment Pool. Looking ahead, the Committee will be discussing possible changes to the Pension Investment Policy Statement, as well as a possible increase in the international allocation [add new international or global manager(s)].

The ending market value of $70,739,340 included: DuPont Capital Investment: $13,152,500, Operating Account: $112,474, State of Delaware Investment Pool: $44,086,218, Vanguard Extended Market Index: $2,724,804, Vanguard Mid Cap Value: $2,373,239, Wilmington Trust Bonds: $8,290,105, and Wilmington Trust Short Term: $0. Over the last 3 years, the pension fund saw an investment gain of $14.6 million, or an 8.1 percent return.

As of September 30, 2015, Sussex County's Pension Asset Allocation included: State of Delaware Investment Pool: 62.3 percent; Cash: 0.2 percent; Domestic Fixed Income: 11.7 percent; and Domestic Equity: 25.8 percent; these percentages have remained very consistent over time.

Year-to-date, the Pension Fund realized a -2.2 percent return and ranked in the top 30th percentile nationwide (250 public funds); -0.2 percent return for 1 year (top 36th percent); top 19 percent for 3 years; and in the top 25 percent for 5 years. For the quarter, the fund realized a negative return of 4.7 percent (top 36th percent), which was above the policy index of -4.6 percent. Mr. Shone noted Peirce Park likes to see their clients within the top 20th to 30th percentile, which allows for more consistent returns overall. Over the last 5 years, the County's pension plan has realized a return of 8.4 percent, which is above the 7.8 percent policy index. Mr. Shone noted that the County's overall fees are more expensive due to the State's fee of .68, but their returns justify the added cost.

Portfolio summary for the third quarter include: DuPont Capital Investment: -7.4 percent return; Vanguard Extended Market Index (added October 2014): -10.5 percent; Vanguard Mid Cap Value (added December 2014): -6.7; Wilmington Trust Bonds: 1.2 percent; and State of Delaware Investment Pool: -4.4 percent.

Mr. Shone referred members to the OPEB Fund Performance Report (Tab III).

As of September 30, 2015, the ending market value of the OPEB Plan was $30 million ($31.3 million as of October 31, 2015) and realized a first quarter loss of $1.3 million,

and a one year (October 1, 2014 thru September 30, 2015) loss of $55,000. The OPEB Plan outperformed its policy index by approximately 0.9 percent due to strong quarter performance from active equity managers and very low investment fees of .26 percent. Looking ahead: Investment Policy Statement review.

Since its inception (March 1, 2011), at which time the market value was $22,982,102, the OPEB has realized a 4.7 percent return. For the quarter, the plan was down 4.2 percent and ranked in the top 19th percentile; year-to-date: -2.5 percent (top 39th percent), and 1 year: 0.2 percent (top 27 percent); two years: top 42nd percent; and 3 years: top 50th percent.

Mr. Shone reported that he would be recommending one fund to go on their watch list even though they had outperformed their benchmarks by 10 percentage points per year for the last three years, ranking them in the top 2 percent of global equity managers. PPG's heightened concern regarding Thornburg is due to their significant decrease in international equity assets and several portfolio manager changes.

When questioned, Mr. Shone noted that Peirce Park's expectations are that returns, over the next ten years, will be below historic norms for two reasons: fixed income (expected returns of 2.5 percent) and the overvalue of domestic equities.

3. **Review and Modify Pension and OPEB Investment Policy Statements**

Committee members were provided with copies of a report prepared by Peirce Park entitled, "Sussex County Pension & OPEB Investment Policy Statements – November 2015". Also included were two additional documents, "Sussex County OPEB Fund Investment Policy Statement – November 2015" and "ADDENDUM – The Sussex County, Delaware Employee Pension Plan Investment Policy Statement Dated June 24, 2014". Today's information is being presented as a result of discussion held at the Committee's August 20, 2015 meeting and the goals include: updating the investment guidelines and restrictions, making the statements easier to read, removing unnecessary or redundant language, and providing consistency between the Pension and OBEP.

OPEB

The existing OPEB Investment Policy Statement was signed almost 5 years ago (December 2010) and has been amended three times (April 2013, September 2014, and December 2014). The proposed revisions would improve consistency with the Pension's guidelines (pending approval of the Pension's IPS Addendum). Mr. Shone stated that he had contacted Mr. D'Eramo, fixed income manager with Wilmington Trust, to ensure his agreement with the suggested revisions. Mr. Shone and the Committee reviewed and discussed the following:

SUSSEX OPEB IPS COMPARISON

Section	Existing IPS	New IPS
Investment Objectives	States that the target return of the fund is an annualized 8%.	**States that the target return is the Plan's actuarially assumed rate of return.**
Investment Guidelines	Investment Manager(s) shall report immediately to the Committee or its designees any shift between or decrease in market value of asset classes	**Removed.**

Investment Guidelines (Con't.)	during any calendar quarter which equal or exceeds ten (10) percent of the market value of the assets assigned to the Investment Manager(s).	
	Investment Manager(s) should exceed their assigned benchmarks, post fees, on an annualized basis over periods of three (3) years or more.	**Increased to five (5) years, net of fees.**
Equity Guidelines	Limits investment manager(s) to a 5% position in any one security.	Limits investment manager(s) to the greater of: 1. Five (5) percent **or 2. 1.5 times the weighting** of a security within an Investment Manager's bench-mark.
	No limit.	**5% limit on convertible securities and ADRs.**
International/Global Equity Investment Guidelines		**Removed.** International/Global is included within Equity Guidelines.
Fixed Income Investment Guidelines	No less than 50% of the total fixed income portfolio shall be invested in U.S. Government securities.	**Removed.**
	Average credit quality shall exceed A2 as determined by Moody's.	Average credit quality shall exceed **A**/A2 as determined by **S & P**/Moody's.
	Investment grade bonds rated BBB/Baa	**Added a limit of 35%.**
	Single issuer limited to 30%.	Single issuer limited to **25%.**
	Federal Agencies limited to 50%.	**Removed.**
	Zero coupon treasuries limited to 10%.	**Removed.**
Cash Investment Guidelines		**Removed. Included new guidelines within fixed income.**
Review Procedures	All investment managers will rank above agreed upon peer group medians over periods of three (3) or more years.	All investment managers will rank above agreed upon peer group medians over periods of **five (5)** or more years.

Mr. Baker questioned "single issuer limited to **25%**" under Fixed Income Investment Guidelines, and whether this included U. S. Government/Corporate Bonds. Mr. Shone noted that this should read "single issuer of agency bonds limited to 25%".

PENSION

The existing Investment Policy Statement was signed in June 2014. The current IPS was reviewed and redlined to make it consistent with the new OPEB IPS, and Peirce Park is recommending approval of the IPS Addendum. A review of the changes include:

SUSSEX PENSION IPS COMPARISON

Section	Existing Sussex Pension IPS	New Sussex OPEB IPS/Pension IPS Addendum
Investment Guidelines	Investment Manager(s) shall report immediately to the Committee or its designees any shift between or decrease in	**Removed.**

	market value of asset classes during any calendar quart which equal or exceeds ten (10) percent of the market value of the assets assigned to the Investment Manager(s).	
Equity Guidelines	5% limit on REITS	**Removed.**
	Limits investment managers(s) to a 5% position in any one security.	Limits investment manager(s) to the greater of 1) Five (5) percent **or 2) 1.5 times the weighting of a security within an Investment Manager's benchmark.**
	Limits access to liquidity.	Modified to give investment manager's more latitude to find liquidity.
Fixed Income Investment Guidelines	Average credit quality shall exceed A2 as determined by Moody's.	Average credit quality shall exceed **A**/A2 as determined by **S&P**/Moody's.
	Allows non-investment grade bonds up to 20%.	**Prohibits non-investment grade bonds.**
	Investment grade bonds rated BBB/Baa	**Added a limit of 35%.**
	The effective duration … shall be no more than twenty-five (25) percent greater or less than the effective duration of the policy benchmark.	The effective duration … shall be no more than twenty-five (25) percent greater **or fifty (50) percent less than** the effective duration of the policy benchmark.
	Single issuer limited to 30%.	Single issuer limited to **25%.**
	Zero coupon treasuries limited to 10%.	**Removed.**
	Federal Agencies limited to 50%.	**Removed.**
	No guidelines for cash.	**Added guidelines for cash (section 2G).**
Asset Allocation	International Equity Benchmark: MSCI EAFE (net).	**Changed to: MSCI ACWI ex U.S. (net)**
	Fixed Income Benchmark: Barclay's Intermediate Government Index	**Changed to: Barclay's Intermediate Government/Credit Index.**

Note: As was noted for the OPEB, the above "Single Issuer limited to 25%" under Fixed Income Guidelines should read, "Single issuer of agency bonds limited to 25%".

When questioned, although not included in the summary, Mr. Shone confirmed that changes were made and included in the Pension IPS revisions pertaining to cash guidelines, REITS, and duration, as was done for the OPEB.

Ms. Jennings thanked Mr. Shone for the tremendous amount of work required by Peirce Park in presenting their comparisons and recommendations to the Committee.

A Motion was made by Mr. Baker, seconded by Mr. Leahy, to recommend to the Sussex County Council to amend both the OPEB and Pension Investment Policy Statements as recommended and presented by Peirce Park Group.

Before passage of the motion, Mr. Shone suggested that discussion would need to take place to define the international equity targets and allow inclusion in the Committee's recommendations to County Council.

Mr. Baker and Mr. Leahy withdrew their motion to allow discussion on the international targets for both Investment Policy Statements (next item on the agenda).

4. **Pension and OPEB Manager Recommendations**

Committee members were presented with copies of a report entitled, "Sussex County Global/Int'l Equity Manager Search – November 2015". At the August 2015 meeting, the Committee had expressed an interest in increasing the allocation of international equities for both the Pension and the OPEB. At the present time, the Pension's exposure to International Equities is approximately 12 percent thru the Delaware State Pool. The OPEB's allocation is 14 percent thru two global managers (MFS and Thornburg) and one international manager (American Funds). Given the potential allocation size, Peirce Park recommends the use of an international passive option should the Committee decide not to use global equity managers. Mr. Shone noted that the OPEB can also allocate more assets to existing managers.

Mr. Shone reviewed the following Summary and Manager information for the 4 noted managers (as well as Fund Comparisons – Regional and Sector Distributions, and Market Capitalization):

SUMMARY

Artisan Global Opportunities	- Five portfolio managers supported by a team of research analysts - Aims to find companies experiencing accelerating profit cycles - Invests in developed (U.S. and international) and emerging markets - Guidelines for total exposure to industry, market capitalizations, countries, and individual positions
MFS Low Volatility Global Equity	- Four portfolio managers who use both fundamental and quantitative metrics - Targets 30% less risk than the MSCI ACWI - Invests in developed (U.S. and international) and emerging markets - The strategy has a shorter track record and limited assets
Vanguard Total World Stock Index	- Seeks to track the performance of the FTSE Global All Cap Index - Passively managed, using index sampling - Broad exposure across non-U.S. developed and emerging markets around the world, including the U.S.
Vanguard FTSE All-World ex-US Index	- Seeks to track the performance of the FTSE All-World ex US Index - Employs a passively managed, full-replication strategy - Broad exposure across non-U.S. developed and emerging markets around the world

MANAGER INFORMATION – AS OF SEPTEMBER 30, 2015

	Artisan Global Opportunities	**MFS Low Volatility Global Equity**	**Vanguard Total World Stock Index**	**Vanguard FTSE All-World ex-US Index**
Location	Milwaukee, WI	Boston, MA	Malvern, PA	Malvern, PA
Firm Inception	1994	1924	1975	1975
Firm Assets ($B)	97	403	3,105	3,105

Style	Fundamental, Bottom-up	Combined, Bottom-Up	Index	Index
Strategy Inception	2007	November 2011	2008	2007
Strategy Assets ($B)	6.5	0.1	7.1	23.0
Expense Ratio	0.97%	0.95%	0.27*	0.14%*
Vehicle	Mutual Fund (Ticker: APHRX)	Mutual Fund (Ticker: MVGNX)	Mutual Fund (Ticker: VTWSX)	Mutual Fund (Ticker: VFWSX)
Preferred Benchmark	MSCI ACWI	MSCI ACWI	FTSE Global All Cap	FTSE All-World ex US Index
# of Holdings	46	95	7,424	2,510

*The strategy also has an institutional share class with an expense ratio of 0.15%. The minimum for this vehicle is $5 million. There is also an ETF, which has an expense ratio of 0.17%.

	Artisan Global Opportunities	**MFS Low Volatility Global Equity**
Portfolio Management:	- 5 portfolio managers on the strategy - Supported by 11 research analysts	- Two portfolio managers on the strategy - Global research platform – fundamental research, sector teams, quantitative research, etc. (supports the portfolio managers)
Looking for stocks with:	- Franchise companies that exhibit financial strength, high industry position, revenue growth, and strong margins - An accelerating profit cycle - Attractive valuations that sell at a discount to private market value	- Volatility (as measured by standard deviation) below the highest 40% within universe - High quality of products and services, strong growth rate versus its industry, strong management, and solid financial strength - Attractive valuations that have an investment catalyst
Managers risk in absolute terms and relative to benchmark:	- Max of 35% in any single country other than the U.S. - Max of 25% in any industry - Market capitalization greater than $3B at initiation of position	- 4% position maximum - Sector, industry, and region weights within 5% of benchmark 50 year average - Use MSCI Barra in daily risk monitoring and optimization process

YEARLY RETURNS

	2015 YTD	**2014**	**2013**	**2012**	**2011**	**2010**	**2009**	**2008**
Artisan	-1.2	2.6	24.6	30.2	-6.6	28.2	47.9	-44.7
MFS	-4.5	10.0	26.0	16.3				
Vanguard Total World	-7.9	3.9	22.8	16.9	-7.9	14.5	37.1	-42.4
ACWI	-8.8	4.2	22.8	16.1	-7.4	12.7	34.6	-42.2

CUMULATIVE RETURNS ANNUALIZED (%) – AS OF OCTOBER 2015

	YTD	1 Year	3 Year	5 Year	Since Oct. 2007
Artisan	-1.2	-0.2	10.0	12.0	6.7
MFS*	-4.5	0.3	10.8	11.6	6.2
Vanguard Total World	-7.9	-5.9	7.23	7.1	2.3
ACWI	-8.8	-6.7	7.0	6.8	1.9

*The MFS strategy incepted in November 2011. Prior to that, Peirce Park used the MSCI ACWI Minimum Volatility Index as a proxy.

PENSION IMPLEMENTATION

(possible portfolio structure)

	Current	14% Int'l	14% Intl v2	16% Int'l	16% Int'l v2
DuPont Large Cap Structured Equity	19.2	**17.2**	**16.2**	**16.2**	**13.2**
Vanguard Extended Market Index	2.7	2.7	2.7	2.7	2.7
Vanguard Mid Cap Value Index	4.8	4.8	**3.8**	**3.8**	**2.8**
Wilmington Trust FI	11.1	11.1	11.1	11.1	11.1
Cash	0.2	0.2	0.2	0.2	0.2
DE State Pool	62.0	62.0	62.0	62.0	62.0
New Global Manager(s)	-	-	**4.0**	-	**8.0**
New International Manager	-	**2.0**	-	**4.0**	-

Contributing
Withdrawing

OPEB IMPLEMENTATION

(possible portfolio structure)

	Current	16% International	18% International
Vanguard Institutional Index	35.1	**32.1**	**29.1**
Vanguard Mid Cap Value Index	6.3	6.3	6.3
Vanguard Small Cap Value Index	2.9	2.9	2.9
MFS Low Volatility Global Index	6.4	**7.4**	**9.4**
Thornburg Global Opportunities	6.3	6.2	6.2
American Funds Int'l Growth & Income	6.9	**8.9**	**9.9**
Wilmington Trust FI	35.1	35.1	35.1
Cash	1.0	1.0	1.0

Contributing
Withdrawing

Ms. Ryan inquired as to the impact of recent events in Europe (made in reference to the November 12, 2015 violence in France by ISIS) to international performance going forward; she also questioned the timing and appearance for the Committee to recommend international target changes to the Council considering recent events. Ms. Jennings noted her agreement with Ms. Ryan's concerns.

A Motion was made by Ms. Ryan, seconded by Mr. Leahy, to table discussion on increasing international equity targets until the first quarter of 2016.

Motion Adopted: 7 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Ms. Ryan, Yea; Mr. Leahy, Yea; Mr. Baker, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea.

A Motion was made by Mr. Baker, seconded by Mr. James, that the Pension Committee recommend to the Sussex County Council to approve the changes to the OPEB and Pension Investment Policy Statements as recommended and presented by Peirce Park Group.

Motion Adopted: 7 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Ms. Ryan, Yea; Mr. Leahy, Yea; Mr. Baker, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea.

Ms. Jennings, again, thanked Mr. Shone for his time in preparing the information presented today. (Note: The Committee's recommendations will be brought before Council at their December 8, 2015 meeting, with Mr. Shone in attendance).

5. **Committee Member Replacement**

In addition to Mr. James' upcoming retirement on December 31, 2015, Ms. Jennings reported that terms of two additional committee members – Mr. Baker and Mr. Leahy – would expire on January 17, 2016. Ms. Jennings requested Mr. Baker and Mr. Leahy to let her know if they would consider serving an additional 4-year term, and for the committee to consider a replacement for Mr. James' who serves as the County employee representative on the Committee. Mr. Baker and the Committee congratulated Mr. James and thanked him for his valuable service and expertise on the Committee. Mr. James expressed his appreciation and pleasure in being able to serve as a member on the Committee.

6. **2016 Meeting Dates**

Ms. Jennings announced the quarterly meetings for 2016:

February 18, 2016
May 19, 2016
August 18, 2016
November 17, 2016

All meetings begin at 10:00 a.m. and are held in the Sussex County Council Chambers. Members were asked to review the suggested dates and notify Ms. Jennings of any conflicts.

7. **Additional Business**

Ms. Jennings presented Committee members with two documents prepared by Aon (the County's Actuary), "Actuarial Valuation Report – Sussex County Employee Pension

Plan for the Fiscal Year Ending June 30, 2015" and "Sussex County Actuarial Report for OPEB Benefits (GASB 43 and 45). She specifically mentioned the Funding Ratio for both plans and noted that the new mortality tables were implemented, which has resulted in a decrease in the funding ratio. A RFP will be issued in early 2016 to hire an actuary to review the assumptions, the sustainability of the County's pension plan with the current allocations, possible changes to the plans, and to make recommendations. The Actuary's two documents will be discussed at the February 2016 meeting.

Mr. Leahy inquired as to public disclosure/reporting of pensions. Ms. Jennings stated that the Pension Plan will show the unfunded portion on the financial statements as of June 30; the funding mechanism has not changed, only the reporting method. For the OPEB, changes in reporting are not expected until 2017. The unfunded pension liability will be a new line item to be noted in the financial statements. Ms. Jennings noted that she will have the opportunity to explain these changes and the County's ranking in relation to other plans when the County's Comprehensive Annual Financial Report is prepared.

8. **Adjourn**

At 11:20 a.m., a Motion was made by Mr. Leahy, seconded by Ms. Ryan, to adjourn.

Motion Adopted: 7 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Ms. Ryan, Yea; Mr. Leahy, Yea; Mr. Baker, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea

The next meeting of the Pension Fund Committee is scheduled for February 18, 2016, at 10:00 a.m. in the Sussex County Council Chambers.

Respectfully submitted,

Nancy Cordrey

Nancy J. Cordrey
Administrative Secretary