OKLAHOMA STATE PENSION COMMISSION
Minutes
November 15, 2022

1. Call to Order

A meeting of the Oklahoma State Pension Commission convened on November 15, 2022 at 10:00 a.m. at the Oklahoma State Capitol. Written notice was sent to Commission members and interested parties, posted 24 hours prior to the meeting, and filed with the Secretary of State in compliance with the Open Meeting Law. The meeting was called to order once quorum was made.

Members Present: Commissioner Randy McDaniel – State Treasurer; Commissioner Cindy Byrd – State Auditor; Commissioner John Suter – Director, OMES; and Commissioners James Ward and DeWayne McAnally – Governor Appointees.

Others: Ruth Ann Chicoine – Administrator; Jason Samansky and Kyle Hagmeier - RVK; Maria Maule – Legal Counsel office of the Attorney General; Joe Fox and Brad Tillberg – Oklahoma Public Employees Retirement System; Chase; Sarah Green, Kirk Stebbins, and Joseph Cappello – Oklahoma Teachers Retirement System; Ginger Sigler and Sean Ruark – Oklahoma Police Pension and Retirement System; Duane Michael – Oklahoma Law Enforcement Retirement System; Chase Rankin and Timothy Van Horn – Oklahoma Firefighters Pension and Retirement System; Jennifer Grigsby – Cabinet Secretary; Paul Pustmueller and Evan Walter – Bank of Oklahoma;and Shawn Ashley - Quorum call.

2. Approval of Minutes dated August 16

A motion was made by Commissioner Webb to accept the minutes of the February 22, 2022, meeting with a second from Commissioner McAnally: all approved, there were no minutes to approve for the June 12 meeting, quorum was not met.

3. Investment Performance and Public Pension Plans Analysis – Jason Samansky and Kyle Hagmeier- RVK, Inc.

Chairman McDaniel turned the meeting over to Jason Samansky of RVK. From August 25th to the end of the quarter, yields on the 2-year Treasury increased 0.87% and US equities declined -14.6%. For the quarter, global equities fell -6.8% as measured by the MSCI ACWI Index, with non-US markets underperforming as the US Dollar soared to multi-decade highs. Fixed income markets suffered significant losses as inflationary dynamics forced global central banks into further tightening monetary policy, and commodity markets priced lower as well due to cyclical dynamics related to a potential global growth slowdown weighing on sentiment for raw materials.

Despite changes in interest rates and tighter financial conditions, the United States' economic activity proved resilient. Labor markets cooled but continue to remain tight. The unemployment rate ended the quarter at 3.5%, while non-farm payroll growth averaged 372,000 per month. Various official measures of aggregate wage growth continued to show annual rates of change in the range of 5% to 6%. Total job openings trended lower through the quarter, with August data indicating job openings down 1.8 million from the record levels in March.

During the 3rd Quarter of 2022 and for the fiscal year ended June 30th, the State funds produced negative returns, ranging between -3.8% to -6.4% net of fees. Relative to policy benchmarks, performance mostly underperformed over the trailing 12-month period, with only two out of seven plans outperforming its respective policy benchmark net of fees.

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The Pension Plans have a higher than median allocation, when compared to their peers, to growth-oriented assets. This remains appropriate given the Plans' extended time horizons, healthy funded statuses, cash needs, and tolerance for risk. However, such risk posturing can lead to meaningful drawdowns that the plans have experienced thus far in 2022.

In general, the Pension Plans are invested more heavily in US equities. International equities have fallen more than their US counterparts year-to-date as recessionary pressures, political changes, and geopolitical pressures have weighed more heavily on non-US stocks; the strategic tilt has benefited the plans over the longer-term as US stocks continue to outpace international over the trailing 10-year time period.

Institutional investors are constantly approached with marketing pitches on new investment strategies. Many of these strategies are largely unproven over multiple market cycles. They may add portfolio complexity and higher costs without providing commensurate benefits or tend to shift into new asset classes after an increase in their performance. The Oklahoma Pension Plans have resisted the temptation to invest in these products, which have kept fees low and avoided the unnecessary dilution of returns.

When evaluating the potential benefits and costs of active management, it is often the case that the costs outweigh the benefits. The relative magnitude of these gap varies by asset class and the unique attributes of the investors themselves. In general, the Oklahoma State Pension Plans have employed active management strategies in a manner that extracted benefits that have exceeded the associated costs. This has enhanced absolute returns and performance relative to peers.

Asset class returns varied during the third quarter but hovered mostly in negative territory. US equity returns remained in negative territory during the quarter. Relative to benchmarks with four out of six plans outperforming their respective benchmarks. US equity returns ranged from approximately -5.2% (Teachers) to -3.8% (Firefighters).

International equity returns were negative on an absolute basis, with underlying plans generally keeping pace or underperforming their asset class benchmark during the third quarter. Returns for the quarter ranged from approximately -11.1% (Teachers) to -7.0% (Firefighters). The use of active management in this asset class has yielded mixed results over long time periods. Three out of six plans with dedicated international equity buckets outperformed their respective indices over the 10-year trailing period. The Police plan measures total domestic and international equity against a broad, global benchmark of equities, and has outperformed almost all trailing periods.

Fixed income absolute returns were negative in the third quarter, though five out seven plans outperformed their respective asset class benchmarks. Returns ranged from approximately -6.5% (Firefighters) to -3.3% (Police). Over longer periods of time, as measured by 7- and 10-year periods, most plans are exceeding or roughly flat against their respective benchmarks.

Real estate returns are largely reported on a lagged basis and were mostly positive for the quarter and the trailing year. For the quarter, the NFI-ODCE Index (Net) delivered a return of 0.3%, comprised of 0.6% income and -0.3% appreciation as valuations are slowly decreasing to reflect higher interest rates and a slowing of economic activity.

Hedge funds returns were mixed in the third quarter. Returns ranged from a low of approximately -1.2% (Police) to a high of 26.1%. (Firefighters). Longer-term returns for Oklahoma Plans' hedge fund allocations have been challenged, providing negative or low single-digit positive returns over the trailing 7- and 10-year time periods.

Private equity produced mostly negative returns over the quarter, but the level of performance varied across the different pension plans. This variability is consistent with expectations given that each plan has different exposures by investment strategy and vintage year. Further, performance versus benchmarks varied considerably, but this is primarily because one plan uses a public equity benchmark, while the others use a private benchmark.

For the fiscal year ending June 30, 2022, the funded status of the plans increased by 1.8% based on the actuarial value of assets, based on the market value of assets, the funded status of the plans decreased by 13.9%: An increase of approximately $1.8 billion in the actuarial value of assets was the primary driver of improved funded status of the plans. Market results in the second half of FY 2022 were challenged, with both equity and fixed income assets experiencing double digit losses. The market value of assets fell by approximately $5.6 billion. Liabilities increased by approximately $1.1 billion over the last year partially offset the increase in the actuarial value of assets.

In FY 2022, pension plan contributions exceeded the actuarially required contributions, offsetting a portion of market value losses. The total contributions for the fiscal year were approximately $2.05 billion, an increase of 15.1% relative to the prior fiscal year. For the past fiscal year, the actual contribution exceeded the actuarially required contribution.

Beginning in 2019, many statehouses started acting to either promote or restrict ESG considerations in the investment decision making process mostly relating to their views on fossil fuel and firearm/ammunitions companies. Many state bills are focused on large, publicly traded banks that have pledged to reduce funding new fossil fuel projects in the United States. Most proposed legislation currently excludes asset management firms.

The scope of these bills is limited to ceasing direct business with banks that have publicly committed to reducing or eliminating financing to fossil fuel companies. In the future, it is expected to include the divestment of these firms' common stock in asset management accounts. In some states, new legislation indicates that a consideration of ESG factors when managing state portfolios should be prohibited under the view that ESG integration is non-pecuniary and investment decision making should be limited to pecuniary interests alone.

Several states have moved in the opposite direction and have frozen or divested holdings of fossil fuel companies within their portfolios and have memorialized the use of ESG factors in portfolio construction as a risk mitigant. Banks making public pledges to reach net zero greenhouse gas emissions can be easily identified. Determining to what extent and with what intention integrating ESG factors in portfolio decisions is much less clear and open to interpretation.

ESG investing continues to trend within the plan sponsor community. The conversations include climate eclipsing governance and social issues at the top of the ESG agenda for institutional investors; large conglomerates pushing their suppliers to become net-emission zero; private companies being evaluated for their carbon-intensity; states continue to discuss and plan their direction with ESG investing. Through it all, renewable energy and investing is increasing across all the states Oklahoma is a leader in providing wind energy.

No other discussion by the Commission.

4. <u>Approval of 2023 Meeting Dates</u>

Because of a scheduling conflict, a motion was made by Commissioner Byrd to move the August 15th date to August 8th with all in agreement, the motion was approved by the Commission. A motion to approve the meeting dates for 2023 was made by Commissioner Byrd, a 2nd by Commissioner Ward, all in favor.

5. <u>Adjournment</u>

A motion to adjourn was made with all in favor, meeting adjourned.

*Respectfully Submitted:*___________________________________
Ruth Ann Chicoine, Administrator