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# **Board of Investment Trustees**



## **Montgomery County Employee Retirement Plans**

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Annual Report

Fiscal Year ending June 30, 2017

# Overview

November 1, 2017

To: Employees, Retirees, and Beneficiaries

From: Board of Investment Trustees

The mission of the Board of Investment Trustees is to manage prudent investment programs for the members of the Employee Retirement Plans and their beneficiaries. The County's Chief Administrative Officer is responsible for overseeing the day-to-day administration of the retirement plans.

We are pleased to present this annual report for the fiscal year ending June 30, 2017 on the three investment programs established for the retirement plans.

- The Employees' Retirement System (ERS) is a defined benefit pension plan with net assets of \$3,933.5 million, established in 1965 and closed to employees hired on or after October 1, 1994, except public safety bargaining unit employees and employees electing to participate in the Guaranteed Retirement Income Plan (GRIP). As of June 30, 2017 the ERS had 5,738 active participants and 6,516 retirees and beneficiaries receiving benefits.
- The Retirement Savings Plan (RSP) was established in 1994 as a defined contribution plan providing benefits to all non-public safety and certain public safety employees hired on or after October 1, 1994. As of June 30, 2017 the RSP had \$394.2 million in net assets and 4,584 (3,577 active and 1,007 inactive) participants.
- The County Deferred Compensation Plan (DCP) is a voluntary plan established pursuant to Section 457 of the Internal Revenue Code. As of June 30, 2017 the DCP had \$390.4 million in net assets and 3,411 participants.

Shown below is a condensed presentation of the Plan Net Position and Changes in Plan Net Position from the Comprehensive Annual Financial Report for the retirement plans for the period ending June 30, 2017:

Net Position (Millions)							Change in Net Position (Millions)						
	ERS		RSP		DCP			ERS		RSP		DCP	
	2017	2016	2017	2016	2017	2016		2017	2016	2017	2016	2017	2016
<b>Assets:</b>							<b>Additions:</b>						
Cash and investments	\$ 4,123.6	\$ 3,829.6	\$ 392.3	\$ 334.3	\$ 389.4	\$ 348.1	Employer contributions	\$ 95.5	\$ 134.8	\$ 19.8	\$ 19.7	\$ -	\$ -
Receivables	21.1	41.7	1.9	1.7	1.0	0.9	Member contributions	27.9	27.0	10.3	10.7	19.5	18.8
Capital Assets	-	0.3	-	-	-	-	Net investment income (loss)	413.3	57.7	43.6	0.5	47.6	(0.1)
<b>Total assets</b>	<b>4,144.7</b>	<b>3,871.6</b>	<b>394.2</b>	<b>336.0</b>	<b>390.4</b>	<b>349.0</b>	<b>Total additions</b>	<b>536.7</b>	<b>219.5</b>	<b>73.7</b>	<b>30.9</b>	<b>67.1</b>	<b>18.7</b>
<b>Liabilities</b>	<b>211.2</b>	<b>230.0</b>	<b>0.0</b>	<b>0.0</b>	<b>-</b>	<b>-</b>	<b>Deductions:</b>						
<b>Total net position</b>	<b>\$ 3,933.5</b>	<b>\$ 3,641.6</b>	<b>\$ 394.2</b>	<b>\$ 336.0</b>	<b>\$ 390.4</b>	<b>\$ 349.0</b>	Benefits	235.1	230.7	-	-	-	-
							Refunds	6.5	5.9	15.2	10.0	25.7	22.3
							Administrative expenses	3.2	3.0	0.3	0.2	-	-
							<b>Total deductions</b>	<b>244.8</b>	<b>239.6</b>	<b>15.5</b>	<b>10.2</b>	<b>25.7</b>	<b>22.3</b>
							<b>Total change in net position</b>	<b>\$ 291.9</b>	<b>\$ (20.1)</b>	<b>\$ 58.2</b>	<b>\$ 20.7</b>	<b>\$ 41.4</b>	<b>\$ (3.6)</b>

For detailed information on the investment programs for all three retirement plans, please visit the Board's web site at [www.montgomerycountymd.gov/retirement](http://www.montgomerycountymd.gov/retirement). For questions, please call the Board office at 240-777-8220.

## Board of Investment Trustees

**Gino Renne**  
Chair  
OPT/SLT Bargaining Unit Designee

**Brad Stelzer**  
Vice Chair  
Montgomery County Council Representative  
Term Expires March 2018

**Shawn Stokes**  
Montgomery County Director of  
Human Resources  
Ex-Officio Member

**Jeffrey D. Buddle**  
Fire & Rescue Bargaining Unit Designee

**Jennifer A. Hughes**  
Montgomery County Director of  
Management and Budget  
Ex-Officio Member

**Jennifer E. Barrett**  
Retired Employees Representative  
Term Expires March 2018

**George Willie**  
Public Representative  
Term Expires March 2020

**Diane Wurdeman**  
Secretary  
Non-Bargaining Unit Representative  
Term Expires March 2020

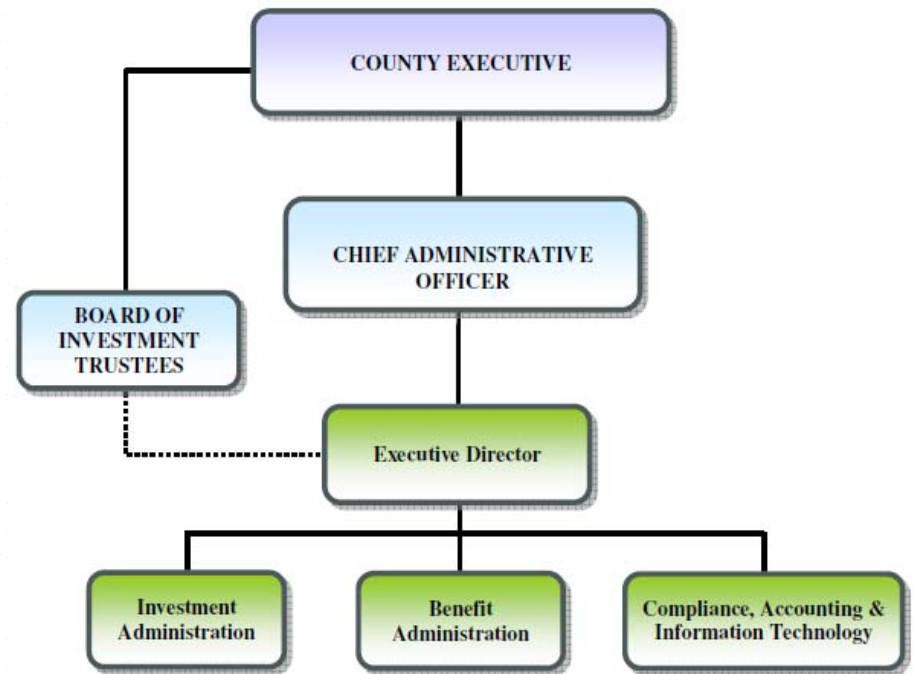
**Alexandre A. Espinosa**  
Montgomery County Director of Finance  
Ex-Officio Member

**Stephen B. Farber**  
Montgomery County Council Administrator  
Ex-Officio Member

**David J. Locke**  
Montgomery County Council Representative  
Term Expires March 2020

**Kelda J.C. Simpson**  
Police Bargaining Unit Designee

## Retirement Plans Administrative Organization



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## **Board Actions**

### ■ ***Employees' Retirement System (includes GRIP)***

- *Continued to add new investments in the following sectors to further diversify the portfolio and manage risk: public equities, private equity, private real assets, private debt, and public real assets.*
- *Prepared the annual comprehensive update describing the implementation and outcomes of the Board's Environmental, Social, and Governance (ESG) policy.*
- *Approved 2017 calendar year commitment pacing plans for the private equity, private real assets, and private debt asset classes.*

### ■ ***Retirement Savings Plan & Deferred Compensation Plan***

- *Transitioned to a flat dollar administrative and recordkeeping fee, which resulted in a significant reduction in overall fees paid by participants.*
- *Conducted annual benefit fair, as well as monthly "Retirement Open Houses" at various County locations, to provide a forum for participants to gain additional information about their retirement plan and the investment options available.*

## **Board Achievements**

### ■ ***Certificate of Achievement for Excellence in Financial Reporting***

- *The Government Finance Officers Association (GFOA) awarded the Certificate of Achievement to the Board for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2016. The certificate of achievement is a prestigious national award that recognizes conformance with the highest standards in government accounting and financial reporting. The Board has received this award for each of the seventeen years that it has published its own CAFR.*

### ■ ***Employees' Retirement System***

- *The investment return for the year ended June 30, 2017 was a gain of 12.16%. The return ranked slightly below median when compared to returns achieved by similar public pension funds reporting results for the one year period. For the longer time periods, five and ten years, the ERS' investment returns ranked median and in the top decile, or top 10%, when compared to peers.*

### ■ ***Retirement Savings Plan***

- *As of June 30, 2017, 92% of the funds offered through Fidelity were rated three stars or above by Morningstar (five star is the highest rating). The one year return for the Plan was a gain of 12.7%.*

### ■ ***Deferred Compensation Plan***

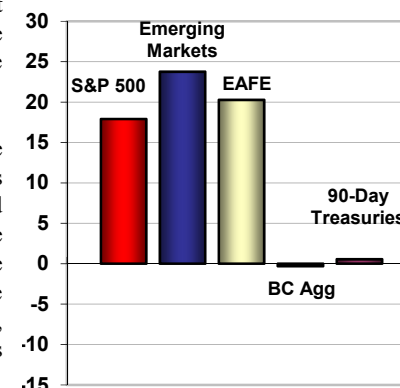
- *As of June 30, 2017, 92% of the funds offered through Fidelity were rated three stars or above by Morningstar (five star is the highest rating). The one year return for the Plan was a gain of 13.8%.*

## Market Highlights – ERS Investment Performance

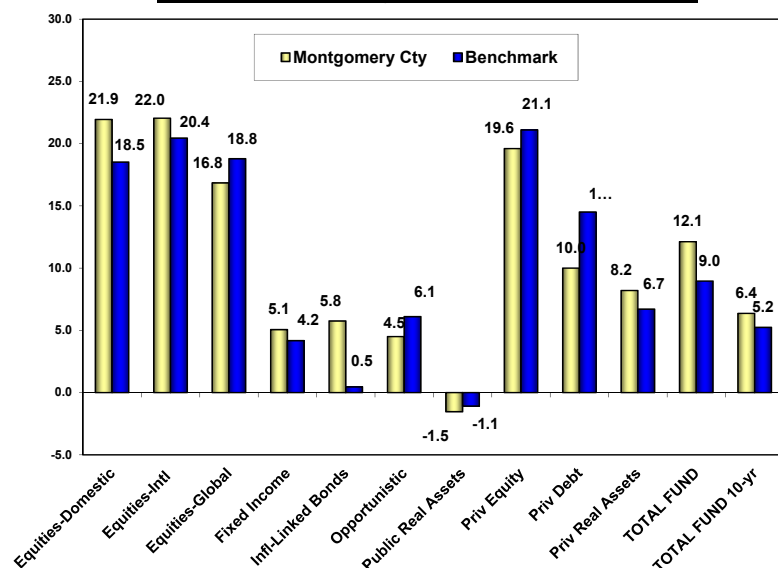
Economic data reflected that GDP increased at a 2.6% annual rate at the end of the second quarter of 2017, matching market expectations. GDP growth reflected increases in both consumer spending on goods and services as well as increases in business investment, exports, and federal government spending. Consumer spending was led by increases in housing, utilities, healthcare, recreational good and vehicles. The 8.2% increase in equipment spending was the fastest in nearly two years. The unemployment rate continued to decline during FY16 and reached 4.4%, a level not seen since pre-crisis 2007. Inflation remained muted, with the price index excluding food and energy increasing at a 0.9% rate, the slowest rise in more than two years. The Federal Reserve announced three interest rate hikes in December 2016, March 2017, and June 2017.

U.S. equity markets posted double digit gains during FY16, rallying post U.S. elections and reaching all-time highs during the second half of the fiscal year, driven by positive economic reports. Both the international developed and emerging markets outperformed the U.S. markets during the fiscal year posting over 20% gains (see chart to the right). The international developed market continued to benefit from global central banks' accommodative monetary policy. Returns for emerging markets were attributed to the strong performance of the Chinese market which generated over a 30% return. Commodities, as measured by the Bloomberg Futures Commodity Index, posted a 6.5% loss, led by the energy and agriculture sectors. Treasuries rose across the yield curve reflecting the increase in interest rates. The Barclay's Aggregate Bond Index declined 0.31% and long duration bonds, as measured by the Barclay's Capital U.S. Long Government/Credit Index, fell by 1.07%, while the high yield asset class, as measured by the Merrill Lynch High Yield II Constrained Index, posted a 12.74% gain during the fiscal year.

Index Returns  
Year Ending 6/30/17



Employees' Retirement System  
FY 2017 Returns by Asset Class-Gross of fees



The Board allocates ERS assets to a broad array of asset classes resulting in the following allocation as of June 30, 2017: domestic equities 19.2%, private equity 7.6%, international equities 16.2%, global equities 3.2%, public fixed income and cash 23.9%, private debt 1%, opportunistic 2.9%, global inflation indexed bonds 11.6%, public real assets 9.5%, and private real assets 4.9%. The chart to the left reflects the returns for the fiscal year ending June 30, 2017 achieved by ERS assets in each investment sector compared to the corresponding benchmark. The Board establishes benchmarks for each market sector, usually an index of securities that represent most of the available investment opportunities within that sector, to evaluate the performance of the investment managers within each sector.

In overseeing the management of ERS assets, the Board has developed sound and prudent investment policies. The Board works to control the risk to which the ERS is exposed while maximizing the potential for long term increases in the value of the assets. The Board's specific investment objectives are to:

- realize the actuarial assumed rate of return of 7.5% annually, over a long term time horizon (for the 2008-2017 fiscal year decade, the annual rate of return on the ERS' investments was 6.37% before fees);
- manage portfolio risk to limit potential downside fluctuations in the value of the total ERS assets; and
- realize as high a rate of total return as possible consistent with the above.

# Employees' Retirement System (ERS)

- **How do I know if I'm a participant in the ERS defined benefit plan?**

Employees who participate in the ERS have the following description on their pay stub next to the bi-weekly contribution amount: *RETIRE*

- **How do I know if I'm a participant in the GRIP?**

Employees who participate in the GRIP have the following description on their pay stub next to the bi-weekly contribution amount: *RET GRI*

- **How is my benefit calculated?**

If you are in the ERS (*RETIRE* on paystub), under County law your benefit is based on your salary, years of credited service, and age at retirement and is not based on the amount you contributed or the investment earnings of the ERS. If you are in the GRIP, your benefit is based on your account balance at time of retirement or separation of service from County.

- **How can I find more information on my benefit?**

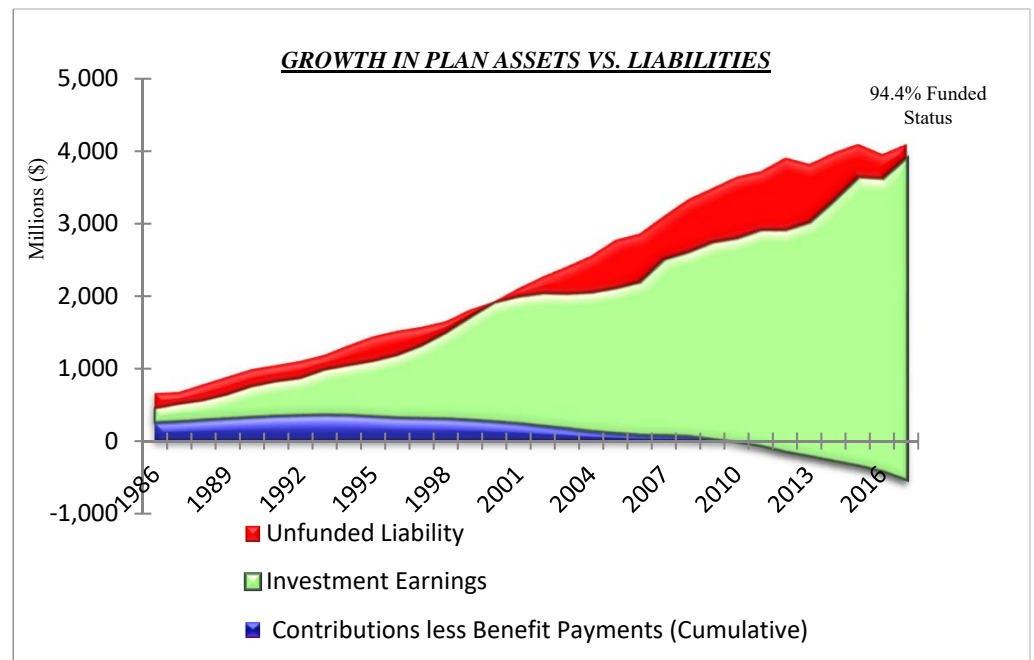
Contact the Montgomery County Employee Retirement Plans at 240-777-8230 or visit our website at [www.montgomerycountymd.gov/retirement](http://www.montgomerycountymd.gov/retirement).

- **How does the amount earned on invested assets impact the ERS?**

While your ERS benefit is paid in accordance with County law, you may be interested in knowing about the status of the assets and liabilities of the ERS. Please refer to the chart below for a 32-year history. Your contributions, along with the County's, are used primarily to make benefit payments to retirees and beneficiaries and pay other costs associated with the administration of the ERS (shown as the bottom layer in the chart).

The earnings (shown as the green middle layer in the chart) represent the bulk of the growth in assets over the years. In funding the ERS, the County currently assumes the assets will earn 7.5% per year. During the strong equity markets of the late 1990s, the assets grew at nearly double that amount, and the funded status of the ERS was strengthened.

As of June 30, 2000 the ERS was nearly fully-funded, but because of the difficult financial markets in 2000-2002 and 2008-2009, plus increased liabilities for higher future benefit payments, the funded status decreased. As of June 30, 2017, the ERS was 94.4% funded. The area shown as the top layer reflects the additional amount required (\$190.5 million) for the ERS to achieve fully-funded status. As noted earlier, the Board continues to implement sound and prudent investment policies that will maximize the potential for long-term increases in the value of the assets.



# Retirement Savings Plan (RSP)

The County established the Retirement Savings Plan for all non-public safety and certain public safety employees not represented by a collective bargaining agreement hired after October 1, 1994. The Plan requires employees to contribute 4% of regular earnings up to the Social Security wage base and 8% above the wage base and public safety employees to contribute 3% up to the Social Security wage base and 6% above the wage base. During FY17, the County contributed 8% and 10% of regular earnings for non-public safety and some public safety employees, respectively.

## How do I know if I'm a participant in this plan?

Employees who participate in the RSP have the following description on their pay stub next to the bi-weekly contribution amount: RET SAV.

## How is my retirement benefit calculated?

Your benefit is based on your account balance at the time of retirement or separation of service. The balance includes your contributions, the County's contributions (if you're vested) and investment earnings.

## How can I find out more information on my account balance and benefit eligibility?

Contact Fidelity's onsite representative at 240-777-8228 or stop by the Fidelity office located in the Executive Office Building, 101 Monroe St, 15<sup>th</sup> floor. Additional information is also available at the Fidelity website at <http://plan.fidelity.com/MCG> or by calling 1-800-343-0860.

The Board oversees the investment program, providing a variety of investment options for participants to choose from. The Board formally evaluates these options quarterly.

The Board also provides two hours of investment counseling annually to all RSP and DCP participants at no charge to encourage participants to expand their knowledge of investment products. Call 410-557-7300 to sign up or visit the Board's web site, <http://www.montgomerycountymd.gov/retirement>.

Shown to the right is a list of the investment funds offered, along with their Morningstar rating and annualized performance as of June 30, 2017.

Fidelity's web site, <http://plan.fidelity.com/MCG>, is an invaluable source of information. The web site contains:

- ✓ Your RSP account activity
- ✓ Analysis and performance information on all of the funds offered and information on investment markets
- ✓ Financial tools to assist you in determining the amount you'll need at retirement

Funds	Morningstar Rating	Rates of Return		
Stable Value Funds:		1 Year	3 Year	5 Year
Fidelity Managed Income	Not Rated	1.44	1.38	1.29
Income Funds:				
Fidelity Total Bond	★★★★	2.26	n/a	n/a
Fidelity Inflation-Protected Bond	★★★	(1.05)	0.22	(0.17)
SSgA U.S. Bond Index	Not Rated	(0.38)	2.46	2.18
PIMCO High Yield	★★★★	11.27	4.60	6.36
Target Date Funds:				
SSgA Target Retirement 2015	Not Rated	6.79	2.85	5.87
SSgA Target Retirement 2020	Not Rated	9.12	3.71	7.44
SSgA Target Retirement 2025	Not Rated	11.43	4.48	8.51
SSgA Target Retirement 2030	Not Rated	12.67	4.76	9.19
SSgA Target Retirement 2035	Not Rated	13.85	4.94	9.72
SSgA Target Retirement 2040	Not Rated	14.93	5.06	10.21
SSgA Target Retirement 2045	Not Rated	15.77	5.22	10.33
SSgA Target Retirement 2050	Not Rated	15.77	5.21	10.33
SSgA Target Retirement 2055	Not Rated	15.77	5.22	10.34
SSgA Target Retirement 2060	Not Rated	15.77	n/a	n/a
SSgA Target Retirement Income	Not Rated	5.40	2.39	4.32
Growth & Income Funds:				
Hartford Dividend & Growth	★★★★	17.96	8.18	13.72
SSgA S&P 500 Index	Not Rated	17.90	9.59	14.61
ClearBridge Appreciation Fund	★★★★	13.80	8.52	12.97
Growth Funds:				
ClearBridge Small Cap Growth	★★★	25.02	6.17	12.63
Fidelity Growth Company	★★★★★	33.28	13.92	n/a
Fidelity Low-Priced Stock	★★★	16.90	6.26	13.29
Fidelity Small Cap Value	★★★★★	18.57	7.97	14.61
SSgA Russell Small/Mid Cap Index	Not Rated	21.66	6.94	14.29
International Stock Funds:				
Harbor International	★★★	17.74	(0.04)	6.75
Oppenheimer Global	★★★★	31.28	7.27	13.77
SSgA Global All Cap Equity ex US Index	Not Rated	19.87	1.28	7.64
Specialty Funds:				
Fidelity Strategic Real Return	★★	1.32	(1.36)	0.84



# Deferred Compensation Plan (DCP)

The County established the Deferred Compensation Plan for employees in 1980. The Board formally evaluates the investment performance of the funds offered quarterly. Shown below is a list of the funds available as of June 30, 2017, along with their Morningstar rating and annualized performance as of June 30, 2017. Additional information on the investment program is available on the Plan web site at <http://plan.fidelity.com/MCG> and the Board's web site at <http://www.montgomerycountymd.gov/retirement>.

## ■ How do I know if I'm eligible to participate in this plan?

All non-represented employees hired after June 6, 2010 are automatically enrolled in the Plan 60 days after the date they are hired. Other non-represented employees are eligible to join the DCP at any time. Employees who are members of MCGEO, and were hired prior to March 1, 2005 and were not members of the DCP at that time, may also join the plan at any time. MCGEO members hired after March 1, 2005 and employees represented by the FOP or the IAFF, are not eligible to make contributions to the DCP.

## ■ How is my retirement benefit calculated?

Your benefit is based on your account balance at the time of retirement or separation of service. The balance includes your contributions and investment earnings.

## ■ How can I find out more information on my account balance and benefit eligibility?

Contact Fidelity's onsite representative, at 240-777-8228 or stop by the Fidelity office located in the Executive Office Building, 101 Monroe Street, 15<sup>th</sup> floor. Additional information is also available at the Fidelity website at

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Funds	Morningstar Rating	Rates of Return		
Stable Value Funds:		1 Year	3 Year	5 Year
Fidelity Managed Income	Not Rated	1.44	1.38	1.29
Income Funds:				
Fidelity Total Bond	★★★★	2.26	n/a	n/a
Fidelity Inflation-Protected Bond	★★★	(1.05)	0.22	(0.17)
SSgA U.S. Bond Index	Not Rated	(0.38)	2.46	2.18
PIMCO High Yield	★★★★	11.27	4.60	6.36
Target Date Funds:				
SSgA Target Retirement 2015	Not Rated	6.79	2.85	5.87
SSgA Target Retirement 2020	Not Rated	9.12	3.71	7.44
SSgA Target Retirement 2025	Not Rated	11.43	4.48	8.51
SSgA Target Retirement 2030	Not Rated	12.67	4.76	9.19
SSgA Target Retirement 2035	Not Rated	13.85	4.94	9.72
SSgA Target Retirement 2040	Not Rated	14.93	5.06	10.21
SSgA Target Retirement 2045	Not Rated	15.77	5.22	10.33
SSgA Target Retirement 2050	Not Rated	15.77	5.21	10.33
SSgA Target Retirement 2055	Not Rated	15.77	5.22	10.34
SSgA Target Retirement 2060	Not Rated	15.77	n/a	n/a
SSgA Target Retirement Income	Not Rated	5.40	2.39	4.32
Growth & Income Funds:				
Hartford Dividend & Growth	★★★★	17.96	8.18	13.72
SSgA S&P 500 Index	Not Rated	17.90	9.59	14.61
ClearBridge Appreciation Fund	★★★★	13.80	8.52	12.97
Growth Funds:				
ClearBridge Small Cap Growth	★★★	25.02	6.17	12.63
Fidelity Growth Company	★★★★★	33.28	13.92	n/a
Fidelity Low-Priced Stock	★★★	16.90	6.26	13.29
Fidelity Small Cap Value	★★★★★	18.57	7.97	14.61
SSgA Russell Small/Mid Cap Index	Not Rated	21.66	6.94	14.29
International Stock Funds:				
Harbor International	★★★	17.74	(0.04)	6.75
Oppenheimer Global	★★★★	31.28	7.27	13.77
SSgA Global All Cap Equity ex US Index	Not Rated	19.87	1.28	7.64
Specialty Funds:				
Fidelity Strategic Real Return	★★	1.32	(1.36)	0.84