
Board of Investment Trustees



Montgomery County Employee Retirement Plans

Annual Report

Fiscal Year ending June 30, 2018

Overview

October 31, 2018

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, 2018 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 \$4,149.3 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, 2018 the ERS had 6,004 active participants and 6,615 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, 2018 the RSP had \$446.2 million in net assets and 4,529 (3,516 active and 1,013 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, 2018 the DCP had \$431.4 million in net assets and 3,391 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, 2018:

Net Position (Millions)						
	ERS		RSP		DCP	
	2018	2017	2018	2017	2018	2017
Assets:						
Cash and investments	\$ 4,283.2	\$ 4,123.6	\$ 444.5	\$ 392.3	\$ 430.3	\$ 389.4
Receivables	24.2	21.1	1.7	1.9	1.1	1.0
Total assets	4,307.4	4,144.7	446.2	394.2	431.4	390.4
Liabilities	158.1	211.2	0.0	0.0	-	-
Total net position	\$ 4,149.3	\$ 3,933.5	\$ 446.2	\$ 394.2	\$ 431.4	\$ 390.4

Change in Net Position (Millions)						
	ERS		RSP		DCP	
	2018	2017	2018	2017	2018	2017
Additions:						
Employer contributions	\$ 93.1	\$ 95.5	\$ 20.3	\$ 19.8	\$ -	\$ -
Member contributions	29.0	27.9	10.8	10.3	20.6	19.5
Net investment income	340.1	413.3	36.6	43.6	43.1	47.6
Total additions	462.2	536.7	67.7	73.7	63.7	67.1
Deductions:						
Benefits	238.9	235.1	-	-	-	-
Refunds	4.6	6.5	15.4	15.2	22.7	25.7
Administrative expenses	2.9	3.2	0.3	0.3	-	-
Total deductions	246.4	244.8	15.7	15.5	22.7	25.7
Total change in net position	\$ 215.8	\$ 291.9	\$ 52.0	\$ 58.2	\$ 41.0	\$ 41.4

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

Board of Investment Trustees

BOARD OF INVESTMENT TRUSTEES

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Chair

Montgomery County Council Representative
Term Expires March 2021

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Vice Chair
Non-Bargaining Unit Representative
Term Expires March 2020

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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

Deborah Snead

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Representative Term Expires
March 2021

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Public Representative
Term Expires March 2020

Alexandre A. Espinosa

Secretary
Montgomery County Director of Finance
Ex-Officio Member

Joseph F. Beach

Public Representative
Term Expires March 2021

Marlene Michaelson

Montgomery County Council Administrator
Ex-Officio Member

David J. Locke

Montgomery County Council
Representative Term Expires March 2020

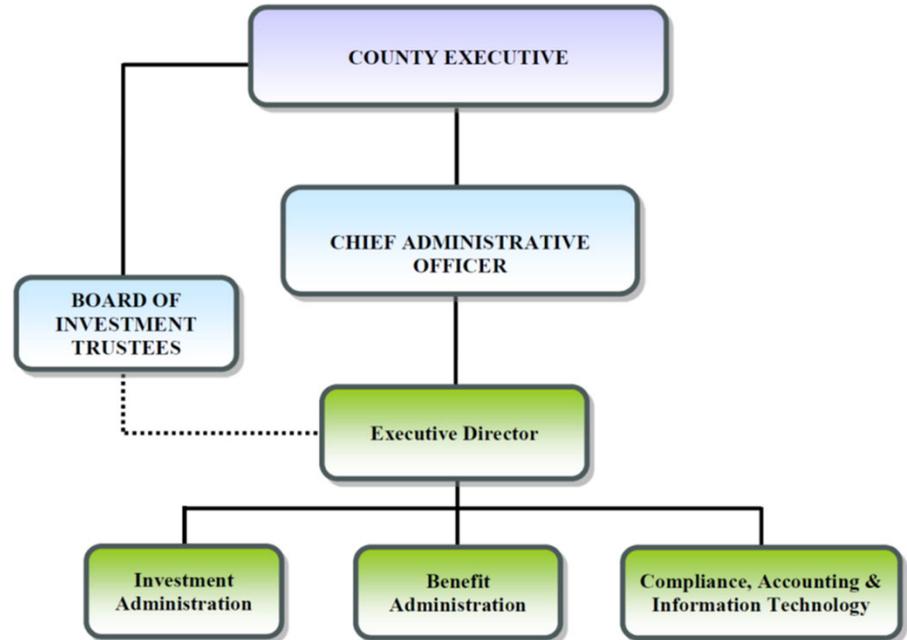
Kelda J.C. Simpson

Police Bargaining Unit Designee

Geno Renne

OPT/SLT Bargaining Unit Designee

Retirement Plans Administrative Organization



Board Actions

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

- *Implemented an integrated approach to asset allocation classifying investments as growth, risk mitigation, and real assets, resulting in a better method to evaluate risk factor exposures.*
- *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. In addition, launched co-investment programs within private equity, private debt, and private real assets to expand the investment opportunities within these sectors.*
- *Expanded ESG efforts to target exposure and evaluate risk and return attributes. Conducted carbon footprint and green revenue analyses to identify the exposures and enhance monitoring efforts. Joined CERES, which is an investor network on climate risk and sustainability, to gain a better understanding of climate risk within the portfolio and the efforts being undertaken by other entities.*

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

- *Transitioned SSgA Target Date funds from K to W share class, which resulted in a reduction in fees paid by participants.*
- *Continued to conduct an 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, 2018. 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 eighteen years that it has published its own CAFR.*

■ ***Employees' Retirement System***

- *The investment return for the year ended June 30, 2018 was a gain of 9.07%. The return ranked above 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 above median and in the top decile, or top 10%, when compared to peers.*

■ ***Retirement Savings Plan***

- *As of June 30, 2018, 83% 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 9.3%.*

■ ***Deferred Compensation Plan***

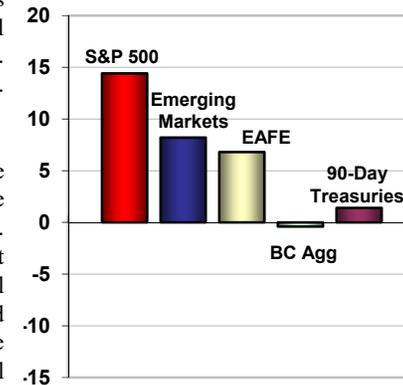
- *As of June 30, 2018, 83% of the funds offered through Fidelity were rated three stars or above by Morningstar (five star is the highest rating). The one-year return for the Plan was a gain of 11.1%.*

Market Highlights – ERS Investment Performance

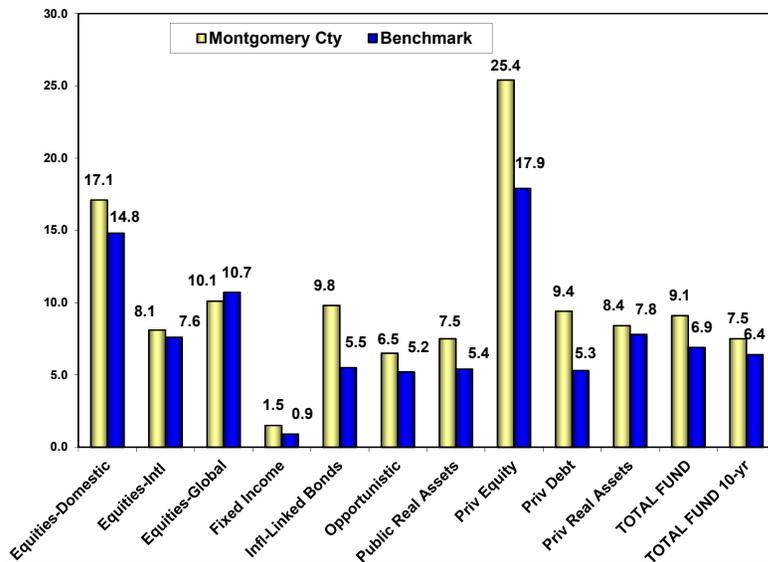
Economic data reflected that GDP increased at a 4.1% annual rate at the end of the second quarter of 2018, matching market expectations and the fastest rate since late 2014. GDP growth reflected increases in both consumer spending on goods and services as well as increases in business investment, exports, and federal government spending. Household purchases, which account for about 70 percent of the economy, remained the main driver of growth and contributed 2.6%. A robust job market and tax cuts supported consumer spending. Nonresidential fixed investment, which includes spending on equipment, structures and intellectual property, increased 8.7%. The unemployment rate ended FY18 at 4.0%, lower than the 4.4% rate at the beginning of the year. Inflation rose in FY18 with the price index excluding food and energy increasing at a 2.3% rate, meeting economists expectations. The Federal Reserve announced three interest rate hikes during the fiscal year in December 2017, March 2018, and June 2018.

U.S. equity markets posted double digit gains during FY18, led by growth oriented sectors such as technology. Both the international developed and emerging markets underperformed the U.S. markets during the fiscal year (see chart to the right). The international developed market returns were muted due to political concerns around Brexit and the impact of tariffs on growth. Similarly, returns for emerging markets were also lower than the domestic markets due to tariff concerns and rising U.S. interest rates. Commodities, as measured by the Bloomberg Futures Commodity Index, posted a 7.4% gain, led by strong gains in crude oil prices. Treasuries rose across the yield curve reflecting the increase in interest rates. The Barclay’s Aggregate Bond Index declined 0.4% and long duration bonds, as measured by the Barclay’s Capital U.S. Long Government/Credit Index, fell by 0.8%, while the high yield asset class, as measured by the Merrill Lynch High Yield II Constrained Index, posted a 2.5% gain during the fiscal year.

Index Returns
Year Ending 6/30/18



Employees' Retirement System
FY 2018 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, 2018: domestic equities 18.3%, private equity 8.7%, international equities 14.3%, global equities 3.1%, public fixed income and cash 23.3%, private debt 1.3%, opportunistic 3.1%, global inflation indexed bonds 12.1%, public real assets 11.0%, and private real assets 4.8%. The chart to the left reflects the returns for the fiscal year ending June 30, 2018 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 2009-2018 fiscal year decade, the annual rate of return on the ERS’ investments was 7.53% 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?**

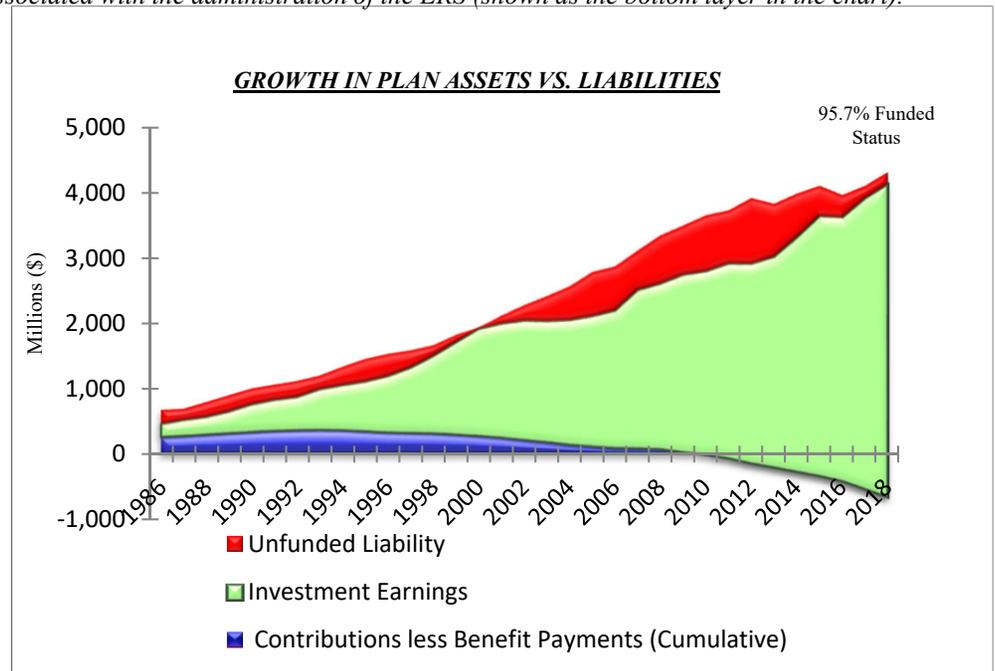
Contact the Montgomery County Employee Retirement Plans at 240-777-8230 or visit our website at www.montgomerycountymd.gov/retirement.

- **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 33-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, 2018, the ERS was 95.7% funded. The area shown as the top layer reflects the additional amount required (\$184.9 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 FY18, 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, 15th floor. Additional information is also available at the Fidelity website at <https://nb.fidelity.com/public/nb/mcg/home> 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, 2018.

Fidelity's web site <https://nb.fidelity.com/public/nb/mcg/home>, 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		
		1 Year	3 Year	5 Year
Stable Value Funds:				
Fidelity Managed Income	Not Rated	1.60	1.49	1.37
Income Funds:				
Fidelity Total Bond	★★★★	0.32	N/A	N/A
Fidelity Inflation-Protected Bond	★★★★	1.72	1.58	1.26
SSgA U.S. Bond Index	Not Rated	(0.48)	1.67	2.24
PIMCO High Yield	★★★	1.19	4.69	4.95
Target Date Funds:				
SSgA Target Retirement 2015	Not Rated	4.69	4.27	5.16
SSgA Target Retirement 2020	Not Rated	6.14	5.39	6.49
SSgA Target Retirement 2025	Not Rated	7.70	6.46	7.57
SSgA Target Retirement 2030	Not Rated	8.55	6.96	8.16
SSgA Target Retirement 2035	Not Rated	9.40	7.42	8.65
SSgA Target Retirement 2040	Not Rated	10.07	7.78	9.06
SSgA Target Retirement 2045	Not Rated	10.73	8.14	9.31
SSgA Target Retirement 2050	Not Rated	10.72	8.13	9.30
SSgA Target Retirement 2055	Not Rated	10.73	8.25	9.51
SSgA Target Retirement 2060	Not Rated	10.73	8.25	N/A
SSgA Target Retirement Income	Not Rated	3.98	3.66	3.98
Growth & Income Funds:				
Hartford Dividend & Growth	★★★★	9.92	10.07	11.44
SSgA S&P 500 Index	Not Rated	14.34	11.91	13.39
ClearBridge Appreciation Fund	★★★★	11.79	10.19	11.55
Growth Funds:				
ClearBridge Small Cap Growth	★★★★	33.30	14.28	14.25
Fidelity Growth Company	★★★★★	28.67	18.53	N/A
Fidelity Low-Priced Stock	★★★★	13.07	8.18	10.66
Fidelity Small Cap Value	★★★★	9.64	9.54	11.05
SSgA Russell Small/Mid Cap Index	Not Rated	16.76	10.40	12.69
International Stock Funds:				
Harbor International	★★	4.47	2.87	4.87
Oppenheimer Global	★★★★	15.94	9.82	11.90
SSgA Global All Cap Equity ex US Index	Not Rated	7.85	5.61	6.54
Specialty Funds:				
Fidelity Strategic Real Return	★	4.99	2.19	1.60

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, 2018, along with their Morningstar rating and annualized performance as of June 30, 2018. Additional information on the investment program is available on the Plan web site at <https://nb.fidelity.com/public/nb/mcg/home> 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, 15th floor. Additional information is also available at the Fidelity website at

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Funds	Morningstar Rating	Rates of Return		
		1 Year	3 Year	5 Year
Stable Value Funds:				
Fidelity Managed Income	Not Rated	1.60	1.49	1.37
Income Funds:				
Fidelity Total Bond	★★★★	0.32	N/A	N/A
Fidelity Inflation-Protected Bond	★★★★	1.72	1.58	1.26
SSgA U.S. Bond Index	Not Rated	(0.48)	1.67	2.24
PIMCO High Yield	★★★	1.19	4.69	4.95
Target Date Funds:				
SSgA Target Retirement 2015	Not Rated	4.69	4.27	5.16
SSgA Target Retirement 2020	Not Rated	6.14	5.39	6.49
SSgA Target Retirement 2025	Not Rated	7.70	6.46	7.57
SSgA Target Retirement 2030	Not Rated	8.55	6.96	8.16
SSgA Target Retirement 2035	Not Rated	9.40	7.42	8.65
SSgA Target Retirement 2040	Not Rated	10.07	7.78	9.06
SSgA Target Retirement 2045	Not Rated	10.73	8.14	9.31
SSgA Target Retirement 2050	Not Rated	10.72	8.13	9.30
SSgA Target Retirement 2055	Not Rated	10.73	8.25	9.51
SSgA Target Retirement 2060	Not Rated	10.73	8.25	N/A
SSgA Target Retirement Income	Not Rated	3.98	3.66	3.98
Growth & Income Funds:				
Hartford Dividend & Growth	★★★★	9.92	10.07	11.44
SSgA S&P 500 Index	Not Rated	14.34	11.91	13.39
ClearBridge Appreciation Fund	★★★★	11.79	10.19	11.55
Growth Funds:				
ClearBridge Small Cap Growth	★★★★	33.30	14.28	14.25
Fidelity Growth Company	★★★★★	28.67	18.53	N/A
Fidelity Low-Priced Stock	★★★★	13.07	8.18	10.66
Fidelity Small Cap Value	★★★★	9.64	9.54	11.05
SSgA Russell Small/Mid Cap Index	Not Rated	16.76	10.40	12.69
International Stock Funds:				
Harbor International	★★	4.47	2.87	4.87
Oppenheimer Global	★★★★	15.94	9.82	11.90
SSgA Global All Cap Equity ex US Index	Not Rated	7.85	5.61	6.54
Specialty Funds:				
Fidelity Strategic Real Return	★	4.99	2.19	1.60