# December 31, 2017

Shown below is the quarterly report on the status of the Montgomery County Consolidated Retiree Health Benefits Trust ("CRHBT") for the quarter ending December 31, 2017. This quarterly report is designed to assist you in understanding the current status of the CRHBT.

***History***

The Consolidated Retiree Health Benefits Trust was established in 2008 as a Section 115 Trust to provide funding for retiree health benefits for retirees and their dependents of Montgomery County and other

***Participating Agencies and Other Trust Participants***

Participating agencies include Montgomery County Government, Revenue Authority, Credit Union, Department of Assessment & Tax, Strathmore Hall Foundation, Housing and Opportunity Commission, Washington Suburban Transit Commission, and Village of Friendship Heights. Beginning in June 2012, funding for retiree health benefits for Montgomery County Public Schools ("MCPS") and Montgomery College were also contributed to the CRHBT.

***Board of Trustees***

The Board of Trustees consists of 19 members: The Montgomery County Directors of Management and Budget, Finance, and Human Resources; the Council Administrator; a Police Bargaining Unit Representative; a Fire & Rescue Bargaining Unit Representative; an Office, Professional, and Technical (OPT) and Service, Labor and Trades (SLT) Bargaining Unit Representative; a Non-Bargaining Unit Representative; a Retired Employees Representative; two persons recommended by the Council who are knowledgeable in pensions, investments, or financial matters; two individuals knowledgeable in pensions, investments, or financial matters appointed by the County Executive; three members nominated by the Montgomery County Board of Education including a designee of the Superintendent, a Bargaining Unit Representative and retiree of MCPS; and 3 members nominated by the Board of Trustees of Montgomery College including a designee of the President, a Bargaining Unit Representative, and a retiree of Montgomery College.

***Performance Results***

The total return for the quarter was a gain of 4.34%, 25 basis points (bps) ahead of the 4.09% gain recorded by the policy benchmark. For the one year ending December 31, 2017, the gain of 16.56% was 243 bps ahead of the 14.13% gain recorded by the policy benchmark. The one-year gross return places the CRHBT's performance in the top quartile of the universe of comparable funds constructed by the Board's consultant, Wilshire Associates. Our annualized performance of 7.14% for the three-year period and 7.95% for the five-year period each ranked slightly below the median of the universe.

The total market value of trust assets at December 31, 2017 was $924.0 million. The CRHBT's asset allocation was: Domestic Equities 22.3%, International Equities 19.4%, Global Equities 4.2%, Fixed Income 24.6%, Inflation Linked Bonds 11.5%, Public Real Assets 8.8%, Private Real Assets 2.9%, Private Equity 5.0%, Private Debt 0.5%, and 0.9% Cash.

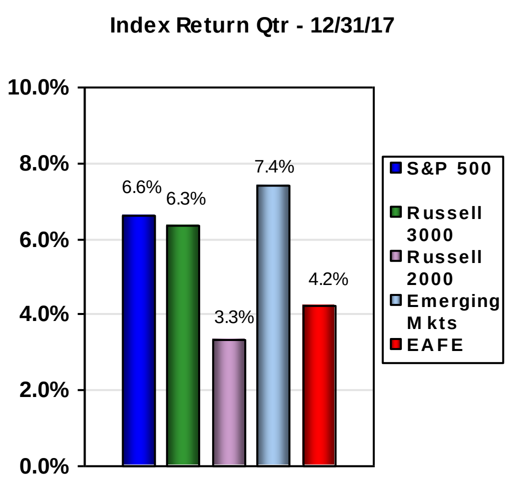
***Major Initiatives/Changes***

During the quarter, the following commitments were made: $6 million to Clearlake Capital Partners V, LP, a distressed restructuring private equity fund, $5 million to Thoma Bravo Discover II, LP, a lower-mid market buyout private equity fund, and $2 million to Magna Hotel Fund VI, LP, a hospitality-focused private real asset fund. In addition, Morgan Stanley Investment Management Inc. was hired to manage a global listed infrastructure mandate.

***Capital Markets and Economic Conditions***

Economic data reflected that GDP increased at an annualized rate of 2.6% rate in the fourth quarter of 2017, falling short of market expectations of 3.0%. The biggest driver of the disappointing GDP report was a surge in imports, which is subtracted from the GDP figure. Imports grew at a 13.9% pace, which represents the fastest rate since 2010. Consumer spending, which accounts for more than two-thirds of the U.S. economy, grew at a 3.8% rate, which points to a growing and strong economy. The economy added 647,000 jobs during the quarter, an increase from Q3's 425,000 gain. The U.S. unemployment rate held steady at 4.1%, which is a 17-year low. Inflation came in below expectations as CPI decreased from 2.2% to 2.1% during the quarter amid a slowdown in gasoline and fuel prices. Core CPI, which excludes the costs of food and energy, slightly increased from 1.7% to 1.8% during the quarter due to rising medical care costs. The housing market continues to recover as new housing starts averaged 1.25M in Q4 relative to 1.17M in Q3. However, housing starts are still 50% below their levels seen before the bursting of the housing bubble in 2007.

**Public Equity Markets:** U.S. equities continued their strong performance in Q4, advancing to all-time highs following robust corporate earnings as well as hopes for tax reform. The low volatility environment that had been present in the first three quarters persisted into the end of the year, with the VIX, a measure of equity market volatility, reaching all-time lows during Q4. Equities were supported by positive macroeconomic data, included a strong Q3 GDP report as well as strength in the employment data. The top performing sectors for the quarter were the more cyclical sectors of Consumer Discretionary, Technology, and Financials while the defensive sectors of Utilities, Telecom, and Health Care lagged. During the quarter large cap outperformed small cap and value outperformed growth. Our combined domestic equity performance was a gain of 5.52%, underperforming the 6.34% gain of the Russell 3000 Index. The underperformance was driven by active management underperformance in the large cap space.

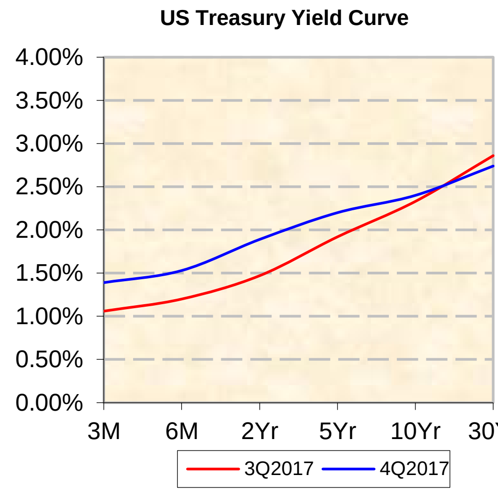



Developed international and emerging equity markets took divergent paths in Q4 as emerging market equities outperformed developed international markets lagged. Within developed markets, Asia was a standout performer driven by Japan and Australia while Europe underperformed due to weakness in France, Switzerland, and Germany. European weakness was attributed to strength in the currency impacting exporters as well as disappointing corporate earnings within Health Care, Telecom, and Financials. Japan rallied sharply as it became clear that Shinzo Abe's Liberal Democratic Party would regain their electoral majority, indicating continued monetary and fiscal stimulus. Much like the U.S., the top performing sectors in Q4 were cyclicals, particularly Energy, Materials, and Consumer Discretionary. The more defensive Utilities, Health Care, and Telecom sectors failed to participate in the rally. Emerging markets continued to rally in the quarter led by India and China. India performed well as the government announced plans to inject capital into the struggling state-owned banks. China performed well due to a favorable Q3 GDP report. Latin America underperformed for the quarter, primarily due to currency weakness in Mexico and Brazil. Our combined international equity performance was a gain of 5.76%, outperforming the 5.12% gain recorded by the benchmark index. Our global equity allocation returned 5.06%, underperforming the 5.73% gain of the MSCI ACWI benchmark.

**Private Equity:** Private equity funds raised $453 billion globally in 2017, the largest amount of capital raised in any year. 2017 also marks as the second consecutive year in which annual fundraising has surpassed $400 billion, a landmark that has only been achieved in 2007-2008. Even though fewer funds closed in 2017 than in 2016, 50% of the funds exceeded their target and 21% achieved 125% or more of their fundraising goal. Fundraising in North America reached a new high in 2017 with the $272 billion aggregate capital raised representing a 23% increase versus 2016, and 60% share of all capital raised during the year. Buyout funds in North America raised $176 billion, a 12% increase from 2016. With $24.7 billion, Apollo IX was the largest private equity fund ever raised. Venture capital deals competed globally reached $182 billion, which was 28% higher than 2016 and reached the highest level in record – the rise in value was driven by over $1 billion transactions. On the other hand, the number of deals completed represented a four-year low. VC deal flow continued to shift from the North American markets towards European and emerging markets such as China and India, with these two emerging regions raising 75% more capital in 2017 than in 2016, securing $28 billion through 56 funds.

During the quarter, our private equity managers called a combined $5.7 million and paid distributions of $1.9 million. Our current allocation to private equity is 5.0%, with a market value of $45.8 million. From its 2013 inception through September 30, 2017, the private equity program has generated a net internal rate of return of 17.6% versus a 15.9% return for the dollar-weighted public market equivalent (the Russell 3000 Index plus 300 bps).

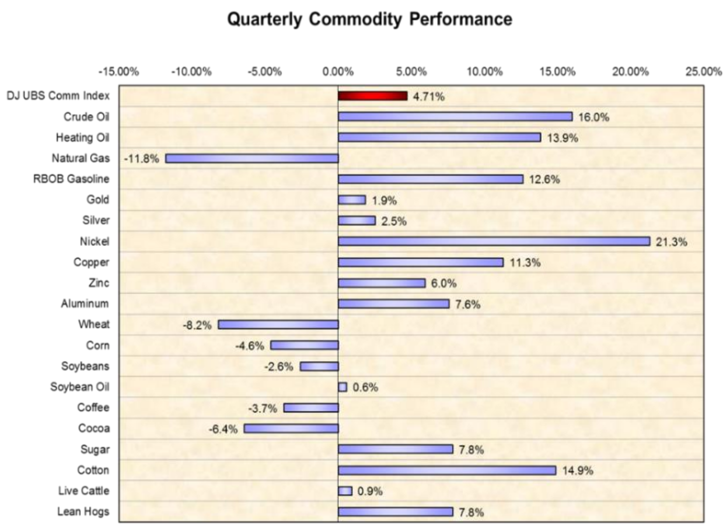
**Fixed Income:** The yield curve flattened during the fourth quarter driven primary by a rise in short and intermediate bond yields. The increase in shorter-term yields is attributed to the transition away from years of accomodative monetary policy by the Fed. While Treasury yields have moved up, credit speads remain suppressed, leading to the outperformance of corporate bonds relative to Treasuries. The yield on the 30-year bond decreased by 12 bps during the quarter, and ended the period at 2.74%. The spread between 2-year and 10-year Treasuries, the main gauge of the yield curve, narrowed by 35 bps to 51 bps. For the quarter, the 2-year Treasury yield ended at 1.89%, up by 42 bps from the prior period, while the 10-year Treasury yield rose by 28 bps to 2.40%. For the quarter, the Merrill Lynch High Yield II Constrained Index rose by 0.41%, the Barclays Aggregate was up 0.39%, and the Barclays Long Govt/Credit Index recorded a gain of 2.84%. The fixed income performance for the quarter was a gain of 1.89%, outperforming the custom benchmark by 17 bps. Our global inflation-linked bond portfolio, combined with a portable alpha overlay, recorded a gain of 5.61% for the quarter, outperforming the custom benchmark's gain of 4.26%.




**Private Debt:** Private debt fundraising in the fourth quarter saw 36 funds reach a final close, securing a total of $35 billion in capital commitments from investors. The majority of the funds that closed (57%) were direct lending, with mezzanine, distressed/special situations, and venture debt funds rounding out the remainder of the fundraising. The largest close was a €4.2 billion direct lending fund focused on providing senior secured loans to European corporate borrowers. Geographically, of the 36 funds that closed, 26 were North American focused. During the quarter, our private debt managers called a combined $1.6 million and paid distributions of $0.5 million. Our current allocation to private debt is 0.53%, with a market value of $4.9 million. Due to the young age of the portfolio, performance data is not relevant.

**Private Real Assets:** The NCREIF Property Index (NPI), a measure of private commercial real estate properties in the U.S., gained 1.8% in the fourth quarter 2017, slightly up from 1.7% from the previous quarter. For the calendar year 2017, the NPI returned 7.0%. The Industrial sector continued to lead performance by property type with total returns of 3.3% in the fourth quarter. Office experienced the second strongest quarterly return by property sector at 1.7%. Apartments, Retail and Hotel returned 1.6%, 1.3% and 1.0%, respectively. Hotels were also the lowest performing property type during 2017, as increasing supply weighed on the industry's ability to push higher average daily rates. Within the U.S. upstream oil and gas sector, there was an uptick in the number of deals announced in the fourth quarter 2017 versus the same period one-year ago; however, total deal value declined by 47%. As oil prices have moved up and stabilized, upstream operators are taking the opportunity to re-invest in core assets and strengthen balance sheets rather than focus on deal making. During the quarter, our private real assets managers called a combined $4.9 million and paid distributions of $0.8 million. Our current allocation to private real assets is 2.9%, with a market value of $26.4 million. Due to the young age of the portfolio, performance data is not relevant.

**Public Real Assets:** The Bloomberg Commodity Index gained 4.7% due to strength in the energy and industrial metal sectors. Energy prices rallied on voluntary OPEC and Russian production cuts and US crude oil supply declines. Industrial metals appreciated on global growth in manufacturing and greater than expected economic expansion in China. Nickel led the sector advance on expectations for increased battery demand for electric vehicles. Grain prices fell on abundant global supplies. Precious metals advanced due to US dollar weakness. Livestock prices appreciated on strong demand for US meat.




Global listed real estate securities as measured by the FTSE EPRA/NAREIT Developed Index advanced 3.6%, led by strong performance in the German listed residential sector, the French and London office sectors and Hong Kong developers. The German listed residential sector benefited from strong underlying residential market fundamentals and low German Bund rates. The French office sector profited from recovering business sentiment and improving rental growth. In comparison the London office sector rebounded after weak third quarter performance and low valuations. Hong Kong real estate continues to do well as developers are benefitting from farmland conversions and receiving strong demand for their condo projects. Japanese real estate was mixed with Japanese developers outperforming JREITs. U.S. REITs were positive but underperformed the index due to the rising interest rate environment and decelerating growth in the core real estate sectors. The US regional mall sector outperformed due to robust M&A activity.

Master Limited Partners (MLPs), as measured by the Alerian MLP Total Return Index, declined 1.0% due to weak investor sentiment.

For the quarter, the public real asset portfolio increased 4.21%, outperforming the custom benchmark by 77 bps due to outperformance by our active commodities, MLP and global REIT managers.

***Outlook***

In a widely anticipated move, the U.S. Federal Reserve ("Fed") voted to raise short-term interest rates by a quarter point at their most recent December policy meeting. The Fed's benchmark interest rate is now targeted between a range of 1.25% - 1.50%. Additionally, the Fed also increased their GDP growth expectations for 2018 – raising the estimate from 2.1% to 2.4%, as new accommodative fiscal policies were passed through Congress. Presently, the U.S. economy has been growing at a slightly higher rate than the revised estimates, turning in two consecutive quarters of growth in excess of 3%. The Fed also boosted their 2018 inflation forecast by 0.1% to 1.7% - still below their long-term target rate of 2%. The expected unemployment rate was further cut to 3.9% for 2018 and 2019, reflecting the positive outlook for overall growth.

The European Central Bank ("ECB") continued to leave its benchmark interest rate unchanged at 0%. The ECB's monetary policy path is slightly behind that of the U.S. Fed, as the ECB is expected to continue purchasing €30 billion of assets each month through their quantitative easing program until at least September 2018. Even with much uncertainty remaining related to Brexit, the Bank of England's ("BoE") policy committee raised interest rates by a quarter point to 0.50%. This represents the first increase since 2007, and was largely in response to inflation breaching the upper band of the BoE's target range. The outlook for the Japanese economy remains strong after current PM Abe's snap general election victory in October. Major economic metrics such as the unemployment rate, declined to a cyclical low of 2.7%. Inflation, retail sales, and industrial production data were also all reported ahead of expectations. A survey record by the Bank of Japan indicated the strongest sentiment by large manufacturing companies in more than 11 years which could provide a future boost for corporate expenditures and business investment.

**Sources: BlackRock, Bloomberg, Bridgewater, Eagle, FRM, Gryphon, JP Morgan MSCI, NCREIF, Northern Trust, Oil & Gas Investor, PE Hub, Private Equity Analyst, Pitchbook, Preqin, PwC Deals, Real Capital Analytics, RE Alert, S&P Schroders, T. Rowe Price, U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Wilshire Associates.**

***Risk Profile***

The risk/return statistics for the CRHBT for the 1, 3 and 5-year periods ending December 31, 2017 are shown below:

| 1 Year | | | | | |
|---|---|---|---|---|---|
| | Total Return | Risk | Sharpe Ratio | Sortino Ratio | Return/Risk |
| CRHBT - Net of Fees | 16.07 | 1.23 | 12.09 | 17.04 | 13.07 |
| CRHBT Benchmark | 14.13 | 1.30 | 9.77 | 13.09 | 10.87 |

| 3 Year | | | | | |
|---|---|---|---|---|---|
| | Total Return | Risk | Sharpe Ratio | Sortino Ratio | Return/Risk |
| CRHBT - Net of Fees | 6.71 | 6.06 | 0.99 | 1.16 | 1.11 |
| CRHBT Benchmark | 6.55 | 5.64 | 1.03 | 1.17 | 1.16 |

| 5 Year | | | | | |
|---|---|---|---|---|---|
| | Total Return | Risk | Sharpe Ratio | Sortino Ratio | Return/Risk |
| CRHBT - Net of Fees | 7.58 | 5.90 | 1.20 | 1.42 | 1.28 |
| CRHBT Benchmark | 7.41 | 5.63 | 1.22 | 1.44 | 1.32 |

***Participating Agency Allocation***

| | 10/1/2017 | | 10/1/2017 - 12/31/2017 | | | 12/31/2017 | |
|---|---|---|---|---|---|---|---|
| Agency | Balance $ | Balance % | Contributions | Expenses | Investment Gain/Loss | Balance $ | Balance % |
| Montgomery County Govt | $432,448,969 | 48.84% | $1,404,270 | ($794,989) | $18,932,115 | $451,990,366 | 48.90% |
| MontCo Revenue Authority | $2,658,077 | 0.30% | $38,450 | ($4,904) | $116,815 | $2,808,437 | 0.30% |
| Strathmore Hall Foundation | $1,234,675 | 0.14% | $15,700 | ($2,277) | $54,228 | $1,302,326 | 0.14% |
| Credit Union | $1,102,594 | 0.12% | $7,850 | ($2,029) | $48,334 | $1,156,749 | 0.13% |
| Dept of Assessments & Tax | $12,477 | 0.00% | $0 | ($23) | $546 | $13,000 | 0.00% |
| District Court of Maryland | $0 | 0.00% | $0 | $0 | $0 | $0 | 0.00% |
| HOC | $14,282,546 | 1.61% | $267,350 | ($26,388) | $628,589 | $15,152,097 | 1.64% |
| WSTC | $98,118 | 0.01% | $0 | ($180) | $4,291 | $102,228 | 0.01% |
| Village of Friendship Heights | $337,961 | 0.04% | $6,730 | ($625) | $14,880 | $358,947 | 0.04% |
| Montg. Cty. Public Schools | $382,785,181 | 43.23% | $0 | ($694,679) | $16,739,363 | $398,829,865 | 43.15% |
| Montgomery College | $50,552,691 | 5.71% | $0 | ($91,743) | $2,210,691 | $52,671,639 | 5.70% |
| **Total** | **$885,513,289** | **100.00%** | **$1,740,350** | **($1,617,837)** | **$38,749,852** | **$924,385,654** | **100.00%** |