AD HOC COMMITTEE ON ACTUARIAL ECONOMIC ASSUMPTIONS MEETING MINUTES
BOARD OF TRUSTEES
MARYLAND STATE RETIREMENT AND PENSION SYSTEM

June 17, 2019

The Ad Hoc Committee on Actuarial Economic Assumptions for the Maryland State Retirement and Pension System convened at the Board Room of the SunTrust Building, 120 East Baltimore Street, 16th Floor Board Room, Baltimore, Maryland beginning at 10:00 a.m.

The Committee Members present included:

Eric Brotman, Chairman, presiding	Linda Herman
Michael Barry (via phone)	F. Patrick Hughes
David Brinkley	Douglas Prouty
	Michael Stafford

Agency Staff members attending included: R. Dean Kenderdine, Executive Director/Board Secretary

Melody Countess	Anne Gawthrop	Andrew Palmer
Patricia Fitzhugh	Angie Jenkins	Janet Sirkis

Assistant Attorneys General present included: Rachel Cohen and Kathleen Wherthey

Other attendees included: Treasurer Nancy Kopp, Brad Armstrong, and Brian Murphy of GRS, and Frank Benham of Meketa (via phone).

Minutes

Treasurer Kopp, while not a committee member, questioned several entries on page 2 of the committee meeting minutes and asked for clarification. Specifically on the following comments:

- “Mr. Palmer responded that from 2001-2017 the S&P 500 was at 7.15%, when the System was assuming an 8% return back then.”

After discussion Mr. Palmer’s response was amended to reflect “that from 2001-2017 the S&P 500 was at 7.15%, when the System was assuming a higher return during that time.”

- “Jeff Tebeau from GRS responded that salary increases result in higher liability, but gains on returns result in lower cost-of-living increases for retirees and beneficiaries.”

After discussion Mr. Tebeau’s response was amended to reflect “that salary increases result in higher liability, but gains on returns result in lower unfunded liabilities and possible higher cost-of-living increases.”

- “Mr. Armstrong responded yes, to the extent the GRS is aware of such changes. Mr. Armstrong further commented that GRS will take all such information under advisement.

After discussion Mr. Armstrong’s response was modified to remove the phrase “to the extent the GRS is aware of such changes."

On a motion made by Mr. Prouty and seconded by Mr. Hughes, the Ad Hoc Committee approved the May 10, 2019 open session meeting minutes, as amended.

Ms. Herman asked if Meketa was able to prepare the information she requested at the last meeting.
Mr. Benham responded that scenarios were presented at the May Investment Committee meeting. Mr. Palmer further responded that the scenarios could be found on the Board portal.

Ms. Herman asked if Meketa would revise the assumptions in the 2019 numbers.

Mr. Benham responded that Meketa will revise the numbers in December of next year, consistent with its standing schedule.

Mr. Armstrong responded that Trustee Herman had requested a report from Wilshire Associates on funded status and return assumptions for state plans. He had searched for the report but found that the latest update was for fiscal year 2017 and was not as current as the NASRA report provided in the last meeting.

Ms. Herman confirmed that the 2017 report was the latest available.

Charge to Committee

Mr. Brotman, Chairman of the Committee, reminded the members that as established by the Board of Trustees, the Committee was charged with examining the System's current actuarial economic assumption for the System's Investment Rate of Return and possibly make recommendations to the Board as to whether changes in the rate or its components should be implemented, and if implemented, where that assumption should be set. Mr. Brotman further reminded the Committee that it may make more than one recommendation and that the Committee should consider alternative Investment Rate of Return assumptions within a range of acceptable rates provided by the System's actuary based upon statistics from the set of investment consultants that the actuary monitors.

Presentation by Gabriel Roeder Smith & Company on the Assumed Rate of Investment Return

The Committee was provided with a PowerPoint document presented by Brian Murphy and Brad Armstrong from Gabriel Roeder Smith & Company (GRS), which responded to the committee's request at its May 10 meeting, regarding economic and inflation assumptions.

Mr. Murphy presented information on inflation, which affects projections in the following ways:

- future benefit payout for reformed service;
- initial benefits for future retirees because wages are assumed to grow at least at the inflation rate;
- total payroll which affects the amortization payment for UAAL; and
- investment return assumptions because Investment return assumption is developed as "Inflation Plus Real Return."

Mr. Murphy indicated that GRS surveyed 14 investment consultants and based on the results, the average inflation expectation of those consultants is 2.18%, while the Social Security inflation rate is currently 2.6%.

Ms. Herman asked how GRS came up with the 14 consultants to survey, as she feels that there are only 5-6 investment consultant firms that deal with comparable public pension funds.

Mr. Murphy responded that the 14 consultants surveyed are not all consultants that deal with public pension funds.

Ms. Herman commented that maybe GRS should focus only on such public pension consultants.

Mr. Murphy presented a chart showing that 57% of the present value of benefits will be paid out over the next 15 years.

Mr. Stafford asked how the figures in the chart would compare with those available 15 or more years ago.

Mr. Murphy responded that 15, 20 or 30 years ago the chart would have appeared flatter than it does at present, largely due to the retirement of the baby-boom generation and that the same would be true for most public retirement systems.

Mr. Armstrong also commented that the System's cash flow is better than our peers at 2%.

Messrs. Murphy and Armstrong presented slides pertaining to economic assumptions.

Ms. Herman asked over the last 10 years, what the System's record has been for meeting the assumed rate of return.

Mr. Kenderdine responded that in 6 out of the past 10 years, the System has exceeded the assumed rate of return.

Mr. Palmer commented that the Social Security inflation projection is largely a backwards looking statistic, reflecting the inflation experience over the last two full economic cycles.

Ms. Herman asked where the $50m in projected liability reductions is coming from.

Mr. Armstrong responded that it is resulting from demographic changes in all five state plans.

Review of the Asset Allocation Approved by the Board on May 21, 2019

Mr. Hughes asked if the assumed rate of return was lowered to 6.75% how that would affect the asset allocation.

Mr. Palmer stated that that the a lower assumption with the same asset allocation would improve the probability of achieving the assumption and that moving to something higher than 50/50 would be recommended if it could be done with in the System's risk tolerance.

Mr. Benham responded that the 7.66% projected rate of return for the plan is based on the asset allocation approved by the Board in May.

Mr. Brotman asked how much how much the market move since the beginning of the year would reduce the projected return.
Mr. Benham responded that it was about 40 basis points.

Ms. Herman asked if Meketa's projected return included alpha.

Mr. Benham responded that it does not include alpha.

Ms. Gawthrop also commented that these projections do not include the additional $75m contributed to the trust from reinvested savings and a potential $50m from the "sweeper" amendment.

Discussion

Mr. Brotman commented that, based on discussion, there seems to be two potential recommendations, the first being to keep the inflation rate at 2.6% and reduce the rate of return to 7.4% and the second being to reduce the inflation rate to 2.5% and the rate of return to 7.3%. Mr. Brotman asked if the Committee was opposed to having GRS produce projections that would show the effects of both scenarios. The committee agreed.

Treasurer Kopp commented that she felt the Committee should be looking at market return projections for a period longer than 10 years. She expressed the concern that keeping the Board's current 2.6% inflation rate assumption will require a clear explanation for the System's stakeholders.

After further discussion, GRS was asked to produce projections that show the effects of the 7.4%/2.6% and 7.3%/2.5% scenarios, to be discussed at the next Ad Hoc Committee meeting, which will be held by conference call, once a date has been determined.

Adjournment

There being no further business before the Committee, on a motion made by Mr. Stafford and seconded by Mr. Hughes, the meeting adjourned at 12:43 p.m.

Respectfully submitted,

R. Dean Kenderdine
Secretary to the Board