IDAHO DEFERRED COMPENSATION BOARD

Minutes

May 23, 2022- 1:00pm-3:30pm Idaho State Controller's Office

700 West State Street, 4th floor Syringa Room, Boise

The following board members were all present in person: State Controller Brandon Woolf, Lisa Mason representing the Secretary of State's Office, Brian Kane representing the Attorney General's Office, and Ben Ysursa representing Office of the Governor.

Others present were: Jake O'Shaughnessy and Stuart Payment, SageView, via Microsoft Teams video; John Steggell, Nationwide via Microsoft Teams Video; in person were John Lamm and Stephanie Blackwood, Nationwide, Renee Holt and Rachel Grove, State Controller's Office, and Jackie McCleve, State Controller's Office via Microsoft Teams video.

State Controller Brandon Woolf called the meeting to order at 1:02 p.m.

1. **Committee Questions or Additions to Agenda- Action Item**

Resolution: None

2. **Minutes- Action Item**

Resolution: Mr. Kane moved to approve minutes from February 28, 2022 meeting. Ms. Mason seconded the motion. The motion carried on a unanimous voice vote.

3. **Q1 Quarterly Performance Review and Market Recap – Jake O'Shaughnessy - Action Item**

Mr. O'Shaughnessy reported that stocks have been off and that it has been a bear market. He also stated that overall, the fiduciary funds have held up quite well through March. Mr. O'Shaughnessy reminded everyone that February was when Russia invaded Ukraine, so some of the items seen today (either from an equity standpoint or price of goods standpoint) are somewhat due to the incursion of Ukraine by Russia, but some of the issues had still existed beforehand. He mentioned supply chain issues as an example. Mr. O'Shaughnessy reports that there were indeed inflationary pressures prior to the invasion of Ukraine, but that the incursion exacerbated these concerns. Mr. O'Shaughnessy also stated that he doesn't believe that all of the inflationary pressures have materialized as of yet, particularly around grain, oil factors, and even geopolitical permutations. He reported that geopolitically, these inflationary pressures are most likely going to percolate first in the United States, and then possibly spread into other countries.

Mr. O'Shaughnessy began looking from an equity standpoint, stating that equities entitle people to no more than a share of future earnings of a company. He then continued, that as analysts look at companies and stock prices, they factor in two things when they look at future value, the first is the magnitude of earnings and the second is growing revenue. Mr. O'Shaughnessy reported that over the last ten years up until the last few months, Americans do a very good job of taking that profit margin up 10-20%. However, Mr. O'Shaughnessy stated that these profit margins are likely to be squeezed, possibly due to wage growth and costing more to ship goods across the country. The second factor that Mr. O'Shaughnessy mentioned was growing revenue. This is being affected by the top line pressure, which is revenue growth being squeezed and the bottom line pressure, which is profit margin being squeezed. He reported that these factors are negatively impacting equity holders. Mr. O'Shaughnessy argued that as analysts look at future earnings, they are looking not into the next couple years but earnings into perpetuity, which is possibly a reason why they are entering into bear market territories. Mr. O'Shaughnessy continued that when money is cheap and/or free, people tend to invest in things in a different fashion than when interest rates are high and money is tight. He also stated that right now is an adjustment period, where not only are they battling inflation but interest rates are normalizing. Mr. O'Shaughnessy mentioned that these are the highest inflation rates that anyone has seen in decades. Mr. O'Shaughnessy stated that people are not going to dump stock altogether, but they are going to rejigger the valuations that they put on future earnings, which will impact growth companies.

Mr. O'Shaughnessy reported that from a US economic standpoint, it is important to watch employment because the Federal Reserve of the United States is trying to slow down the labor market. This is because businesses aren't able to hire people due to the difficulty of negotiating wages or wage rises. He also stated that housing is another item to keep an eye on. Interest rates are rising, which directly impacts mortgage rates. Mortgage rates have gone from 3.1% to 4.67% just in the first quarter, nearly a 50% rise in interest rates in a three-month period. Mr. O'Shaughnessy also pointed out the "wealth effect," which also impacts people's spending. He stated that the benefits of the wealth effects start to slow some of the other spending points in the economy, which is currently what the Federal government is trying to slow down.

Mr. O'Shaughnessy mentioned that growth stocks are very popular post-COVID. The Russell 2000 growth names were down 12.8% for the quarter and the small Russell 2000 value was down only 2.4%, indicating that the value stocks held up much better (about 10%) as opposed to their growth counterparts. Mr. O'Shaughnessy also stated that as fiduciary investors, when there is volatility, it is important to point out that this type of a sell off this proverbial bear market is just simply 20% sell off from the high, which was January 20th of this year. However, he also stated that when looking at the S&P 500 is that there are a number of years, nearly every two to three years, that the market sells off around 18-20% and then pops back. Mr. O'Shaughnessy stated that this is a natural process of a healthy market, where bear markets can be seen and clears out growth names that don't have a clear future. He also stated history has shown that this is one of the best times to be an investor, considering that they are coming on seven weeks in a row of negative returns for the S&P 500.

Mr. O'Shaughnessy then began talking about bonds and fixed income. He stated that fixed income and bond markets can be more powerful and more predictive of what the future economy may hold. He also stated the inversion in rates means that there is likely an economic slowdown in the future, but that a recession isn't going to happen right away, likely 12-18 months after the inversion.

Congress introduced a bill called the Secure 2.0 Act, which includes provisions such as retirement lost and found, easier access to student loan repayment, increasing catch-up contributions, and required minimum distribution ages as well as making changes to in service withdrawals. He also began discussing cryptocurrency, stating that they are very volatile and discourages putting a cryptocurrency fund into a retirement plan.

Mr. Kane then asked Mr. O'Shaughnessy, how as a board do they fulfill their responsibility when evaluating cryptocurrency to protect their plan holders. Mr. O'Shaughnessy replied by saying to not offer it and to inquire with Nationwide. He explained that Charles Schwab runs a self-directed brokerage option that the participants could access, so it would be beneficial to inquire with the agent and ask them if there are already Bitcoin products available in the brokerage window. Mr. Kane explained that from the board perspective he wants to make sure that they have the right disclosures and waivers in place to mitigate responsibility, since the crypto market does not have the same level of oversight and regulation as more traditional investments. Mr.

Steggell said that he reached out to Schwab and they said that they don't specifically have any Bitcoin sector funds available, but crypto-related investments can fall into different asset classes.

Mr. O'Shaughnessy continued with his presentation and began discussing litigation. He reported that a lot of lawsuits around fees really subside. Mr. O'Shaughnessy also stated that Fidelity launched what are called K6 share classes, which are a little less expensive than their K share class. He stated that over time the tracking error for these funds has been mitigated, so it would be beneficial to potentially consider moving to the less expensive K6 shares for Contrafund.

4. Recent Developments (regulatory or market place) – Jake O'Shaughnessy – Action Item

Mr. O'Shaughnessy started off by saying that through the end of March, there continues to be very strong growth in the plan. There is a total of $641,380,764.43 in the program through the end of March 2022. Investors continue to earn the amount of investment they have made in the product plus the return they are given there. The American Century Ultra and the Contrafund have benefitted from growth over the last 5-10 years. The Vanguard 500 Index, American Funds Income Fund of America, Calvert, and Dodge & Cox have weathered the storm quite well. The Vanguard Target Retirement 2065 Fund was added and a small amount of money is trickling its way into that product. Mr. Steggell reported that the Vanguard 2070 fund has been approved and can be administered by August 2022.

Mr. O'Shaughnessy reported that the retiree fixed account is at a rate of 3.2%, which is a very healthy rate. This is one of the fixed account rates, both the fixed and traditional that they have seen across their book. Mr. O'Shaughnessy then asked Mr. Steggell what the current rate is and what the outlook will be on these two accounts (retiree fixed and Nationwide fixed) for the remainder of the year. Mr. Steggell reported that that retiree fixed is 3.25% and Nationwide fixed is 3%, reporting that they came down nine basis points from last quarter. Mr. O'Shaughnessy replied by saying that these are still very healthy rates. Mr. O'Shaughnessy continued by stating that the expense ratio was reduced dramatically by moving to the K6 share classes. Overall, performance has been doing well in both large cap and small cap growth managers. The Vanguard 2015 fund is the only fund that is below the median performance, but it is still doing quite well.

Mr. O' Shaughnessy stated that in the previous meeting, the Fidelity Contrafund was in the third quartile, meaning it was below median performance. Mr. O'Shaughnessy reported that it is now in the second quartile, but it should still be kept on watch. This is the same with the American Funds Income Fund, which followed a similar trend where they were below median for a few quarters and are only recently improving. The hope is that by next quarter each fund will stay above the median and then consider removing them from watch at that time.

Mr. O'Shaughnessy concluded his report and asked if there were any questions or if Mr. Steggell had any thoughts. Mr. Steggell mentioned the Dodge & Cox Stock is coming out with a zero-revenue share class that went live earlier this month. He said that this might be something that is worth exploring in the future. Mr. Woolf then asked the room if there were any additional questions or comments, and then thanked Mr. O'Shaughnessy for his presentation.

5. Quarterly Board Report – John Steggell – Action Item

Mr. Woolf introduced John Steggell and John Lamm with Nationwide to speak about the Quarterly report. Mr. Steggell stated he has a couple items on the agenda today for this meeting. The first will be the Board Report, the second will be the revisit to incentive plan.

Mr. Steggell stated that the balance sheet shows that the first quarter 2022 ended with a balance of $650.4 million of total plan assets, which included adding in Schwab and loans. For the first three months of 2022 the plan received about $7 million in cash flow in and $4.8 million went out for withdrawals. Additionally, there were almost $1.7 million enrollments. Mr. Steggell also reported that Nationwide received $5.4 million in new cash flow. For new loan activity, the first quarter was a little bit less than previous quarters, showing that $258,000 are new loans. The average new loan was lower this last quarter as well, showing at around $8,605. There are 476 current loans outstanding, 30 loans were paid off in the first quarter, and the total balance of loans is just under $3 million.

Mr. Steggell then spoke regarding demographics, stating that this last quarter there were 10,096 total participants: 4,561 actively contributing, 4,247 inactive, and then over 1,200 in a payout phase. The largest category of participants by age group is the 60 and over, with 3,787 and the second largest is 50-59 with 2,461. The average balance of the plan is around $64,476, which is a slight dip from the fourth quarter due to market fluctuation, but is still overall a strong number. The average contributing participant puts in $8,316 per year from their paychecks. Mr. Steggell shared that compared to other places in the country, Idaho is doing very well with their employees contributing as much as possible.

Mr. Steggell stated that when the money is flowing into Nationwide, around 29% is going into target dates, 24% is large cap stock, and 21% is going into short-term. $29.2 million are going into Roth money type with a total of 2,697 participants, with the expectation that Roth will continue to expand since it is very popular.

Mr. Steggell then talked about quarterly onsite activity, with 726 individual meetings, 604 virtual meetings, and 122 in-person meetings with group attendance of 16. Mr. Lamm added that post-COVID allowed for them to shift to part-virtual and part in-person. Mr. Lamm asked Ms. Blackwood to speak on her county visits, and she replied that there were a lot of people in the counties that wanted to sign up but she needed to create more time on her calendar to meet with them. Mr. Lamm stated that this model of both in-person and virtual appears to be working really well.

Mr. Steggell then reported that 137 participants logged into the app in the first quarter, which has continued positive feedback from its users. Mr. Woolf pointed out that the documentation he presented has different number values regarding app usage. Mr. Steggell clarified that the numbers he is speaking to are correct, that the numbers Mr. Woolf are referring to are from the old report, but is planning on checking with his reports team for accurate data.

Mr. Steggell continued by reporting over 21,000 logins, where most people are looking at a balance with a few making an exchange. There were 1,077 calls that came in at the call center in the first quarter, indicating increased productivity. Mr. Woolf inquired about the increased number of calls abandoned at 150, and Mr. Steggell said that he hasn’t heard much about that in particular but will check with their call center manager to see exactly why. Mr. Steggell also reported on reconciliation, stating that the beginning balance as of 12/31/2021 was $200,340.21 and the ending balance as of 3/31/2022 was $215,765.69. Mr. Steggell and Mr. Lamm both spoke about new pay centers that were added – Bingham County Fire and Rescue, Nampa Fire, and City of Victor.

6. Revisit to Incentive Plan – John Steggell – Action Item

Mr. Steggell began talking about the incentive program. In the first quarter there was a total bonus paid of $46,600, which is less than the fourth quarter but falls back in line with quarters before that. There were 276 total receiving incentives as current participants, 103 total receiving incentives as new enrollees, and 173 receiving the incentive for increasing. Mr. Lamm stated that word got out that the bonus was going to be going away, so he projects that there is going to be a significant enrollment or increase during this second quarter. He also stated to be prepared for a little more money going out to pay for this incentive program, which will be discontinued after March 31st for current participants but still remain for the new enrollees.

Mr. Woolf asked if anyone had any updates or changes to the incentive plan. Mr. Lamm responded and suggested to leave it alone and see what happens, stating that he is hesitant to jump into something different right away. Ms. Blackwood stated that a lot of the participants are okay with riding things out, with the possible exception of those who are within a couple years of retirement. She also said that she has seen a lot of younger people sign up for the plan and suggests that the board wait and let the dust settle so that there isn't a lot of confusion about who does and doesn't benefit from the incentive. Mr. Steggell asked if the budget was sufficient to pay for the incentives and what the expected expenses will be. Mr. Lamm responded that most of the quarter was running in the red, but going forward without the incentive for increases it'll probably change to running in the black. He then suggested that the board lets this incentive plan continue for a few quarters to see what happens and make an adjustment from there.

7. Updated & Enhanced Participants Statement – John Steggell

Mr. Steggell showed the board the reconfigured participant statement starting the second quarter in the State of Idaho. The front page shows the logo as well as information about the plan broken up into six tiles. The top left will be the balance and performance information section, showing both a quarterly and 1-year return. The top right will be quarterly activity, which will show priority balance, withdrawals and deposits, and vested balance. The middle-left tile is for current investments by asset class, broken up into different percentages. The middle-right tile shows a four-year balanced history. The bottom two tiles indicate retirement readiness, showing how much a person will receive monthly during retirement as well as how much a person might need to continue to save depending on income, expenses, and other retirement plans.

Mr. Steggell also reported additional information on page two of the new statement. The top of page two includes a section for custom messaging, providing information for each individual based on their needs or preferences. Overall, Mr. Steggell reported that the new statement has a better look and better experience. Mr. Woolf asked when this statement will roll out, to which Mr. Steggell replied that it would be the June 30th statement. Mr. Woolf also asked what the percentage breakdown is of those who receive statements electronically vs. those who still receive a paper copy. Mr. Steggell replied that he wasn't sure of the exact numbers but that he can provide that information for him. Mr. Kane asked if there was an area on the form that showed fee assessed for the plan charges. Mr. Steggell replied that it would be on the upper right tile under quarterly activity, specifically the line item entitled fees and charges.

8. Recap – Action Items

a) American Funds Income Fund of America and Contrafund will remain on watchlist for another quarter even though they performed better this last quarter.
b) Next board meeting will be held August 29, 2022 at 1:00 pm.

The meeting adjourned at 2:18 p.m.