The Education Trust Board of New Mexico

Approved
Vera Lyons
Board Secretary
11/5/20

Meeting Minutes of August 6, 2020
1516 Paseo de Peralta
Santa Fe, New Mexico 87501

Board Members

Sandra Liggett, Chair
Robert Desiderio, Vice-Chair (remotely)
Lawton Davis, Member
Mont Green, Member (remotely)

ETB Staff

Ted Miller, Executive Director
Carolyn Fittipaldi, Director of Marketing (remotely)
Vera Lyons, Board Secretary

Meketa Investment Group

Kay Ceserani, Managing Principal (remotely)
Eric White, Principal (remotely)

HoganLovells

Helen Atkeson, Partner (remotely)

SommerUdall

Kurt Sommer, Partner (remotely)

Morton Accounting Services

Janet Pacheco-Morton, CPA (remotely)

Ascensus

Tom Hewitt, VP Relationship Management (remotely)
Tom Lowe, VP Investment Management (remotely)

Principal

Paul Schieber, Managing Director, 529 Distribution (remotely)
Randy Welch, Managing Director, Portfolio Manager (remotely)
James Fennessey, Portfolio Manager, Director of Research (remotely)
Tracy Bollin, Managing Director – Fund Operations (remotely)
Jori Horn, 529 Marketing Director (remotely)

Esparza Advertising

Del Esparza, President (remotely)
Jamie Rushad-Gros, VP, Experience and Digital (remotely)

Sunny505

Joanie Griffin, CEO (remotely)
Jerry Matthews, Senior Account Manager (remotely)

1) **CALL TO ORDER**
The meeting was called to order at 8:34 AM. There was a quorum and four board members were present.

2) **APPROVAL OF AGENDA**
Ms. Liggett called for a motion to approve the agenda. Vice-Chair Desiderio so moved. Mr. Davis seconded. The vote to approve the motion was unanimous.

3) **APPROVAL OF MINUTES**
Ms. Liggett called for a motion to approve the minutes of the June 4, 2020 board meeting. Vice-Chair Desiderio so moved. Mr. Davis seconded the motion. The vote to approve the minutes was unanimous.

4) **PUBLIC COMMENT**
The Chair then called for any public comment. There being none, she moved to the next item.

5) **FY2020 Q4 FINANCIAL REPORT AND REVISED FY 2021BUDGET PROPOSAL**
Ms. Liggett asked Ms. Pacheco-Morton to give the quarterly financial report. She first reviewed the Board's program administrative fund and the budget. She noted that revenue for the year had come in ahead of budget by $257,000. This was largely the result of higher than anticipated payments received from OppenheimerFunds/Invesco at termination of the old program manager contract. Expenses had come in less than expected primarily due to less spending on contractual services than anticipated and less compensation expense due to the marketing director position not being filled for a portion of the year. The change in net position for the year was $786, 735. The net position of the administrative fund at the end of the year was increased to $10,915,842 as a result. She noted that spending was in line with or under budget for all major categories in the budget.

Ms. Pacheco-Morton then reviewed the fiduciary funds. She noted that at the end of the quarter Scholar'sEdge had $1.84 billion in assets and The Education Plan had $580 million in assets. She noted that in SE net position decreased by $58 million as a result of redemptions exceeding income. In TEP there was an increase in net position of $3.5 million. Year over year for the trust funds there was a decrease in net position of $63.5 million.

Ms. Liggett called for a motion to accept the financial report. Mr. Davis so moved. Mr. Green seconded the motion. The vote to approve the motion was unanimous.

Mr. Miller then addressed the proposal to revise the already approved FY21 budget. He noted that in discussions with the DFA cabinet secretary he had been told that it would be best if all state agencies showed an effort to reduce expenses during this difficult year. Even though ETB does not rely on state appropriations, she thought it prudent that ETB reduce its budget as well. He then reviewed several areas where the current budget could be cut without affecting the core functions of the program. The proposed budget reduction under the proposal is 6.7%. Mr. Davis asked if the elimination of a contract provision for a marketing assistant would have an adverse impact on sales efforts. Mr. Miller thought it would not because the position is a back office administrative role.

Ms. Liggett asked for a motion to approve the budget proposal. Mr. Davis so moved. Vice Chair Desiderio seconded the motion. The vote to approve the motion was unanimous.

6) THE EDUCATION PLAN QUARTERLY MARKETING UPDATE

The Chair then asked Ms. Griffin to begin the TEP marketing update for the quarter. Ms. Griffin First noted the PR activity for the quarter, including both the local and national media. She also noted the connection between PR activity and activity on the TEP website. Releases were picked up in national outlets such as Yahoo Finance, Market Insider, Morningstar and the international Business Times.

Mr. Matthews then reviewed breakout of traditional media activity for the quarter as well as the budget spend. He noted the efforts on commercial TV, rural radio and billboards. He noted that traditional media drives visits to the TEP website by design. He then turned the presentation over to Esparza.

Mr. Esparza who gave an executive summary of activities for the quarter. He noted the 51% increase in new accounts for the first six months of 2020 compared to the first six months of 2019. He found this especially notable in the current COVID environment.

He then noted the increased activity on the website. Up 300% in page views over the same period in 2019. Web searches on financial matters is up 60% over a normal year. TEP has benefitted from that interest. The plan is already at 64% of new account growth for the calendar year at the end of July.

He then asked Mr. Gros to continue. Mr. Gros reviewed the changes to the current website made during the last quarter. The home page is being update more frequently with new content and a search functionality has been added. A media page was added. All pages has been optimized for search engines to increase traffic to the site. The number of key words that bring up the site in online searches has increased from 1,000 to 1,800. This has nearly doubled traffic coming to the site frog Google as an example.

He also noted the efforts with regard to launching employee payroll deposit at Sandia Labs, including a dedicated landing page for employees as well as an available online presentation for them. He then reviewed a number of web statistics.

He also looked forward to the next quarter including enhancements for employers, updating content and increasing presence on social media. Outbound emails have been very successful, with a 50% open rate. These will be continued and enhanced.

Ms. Fittipaldi then gave an update on outreach efforts in the CVOID setting. She noted how employers are adapting to the environment with more online outreach to employees. She noted the increase in new accounts at Dona Ana County. She also noted the contacts with Lovelace Health Systems, the Bernalillo county Water Authority and the City of Albuquerque.

She also noted that Morningstar had agreed to review and rate The Education Plan for the first time in the plan's 20 year history.

Ms. Liggett asked if there was any progress on adding the state as an employer to the plan. Ms.

Fittipaldi said that contact had been made but not much forward progress. Ms. Liggett noted that the secretary of SPO was now tasked with a lot of projects by the governor and may have little time for other matters. Ms. Liggett said that she would send a note to the secretary.

Mr. Green asked if the plan had contact with PNM. He offered to reach out to an individual know to him at PNM.

7) SCHOLAR'S EDGE QUARTERLY MARKETING UPDATE

Ms. Horn then reviewed the SE marketing efforts for the past quarter as well as a look ahead for the next quarter. There were two active campaigns running during the quarter – an evergreen campaign originally conceived at launch as well as a National 529 Day campaign which is on May 29th of each year. Principal targets of the campaigns were the brokerage firms strategically important to SE such as Ameriprise, the Principal Advisors Network and several others. Tactics included social media advertising, paid search and paid emails. Programmatic ads generated the highest number of clicks. Trade publications and outlets such as Saving for College, Investing Channel, Think advisor and Asset TV were a significant focus.

She also noted activities with Saving for College as well as a new infographic for the SE website. A new video page was launched on the website. She then reviewed the statistics for a variety of web activities.

She then reviewed the new "Dream, Learn and Save" presentation designed to educate investors about all aspects of education savings. The piece is designed both for general use and for use by financial advisors with their clients. This forms the basis for a new interactive section of the SE website

From a budget perspective she noted that the entire budget allocated to the quarter was committed.

She then reviewed some future activities such as the "529 Playbook" designed for use by financial advisors, email templates for advisors to use as conversation starters and a new SE presentation builder for use by advisors. Webinars are in development for specific brokerage firms strategic to the program. In addition a literacy library is being created to help families involve children in college savings. She noted that all materials for SE had been updated for compliance with the new Reg BI.

A back to school campaign is being finalized with the theme "Great Journeys Begin with a Few Small Steps". She then showed examples of some creative pieces used in conjunction with this theme.

8) SCHOLAR'S EDGE DISTRIBUTION UPDATE

Mr. Schieber then gave the Se distribution update. He began by noting that the industry has had to adopt to a virtually selling model due to COVID. The sales team has finished training on the new system. The team will be judged on the number of their virtual efforts and on virtual sales. He noted that the sales team has been closely engaged with the Principal internal wholesalers. These wholesalers are now asking for 529 information from their contacts. This information can then be accessed by the 529 sales team. Calendaring software will soon rollout that gives advisors a range of times available for a virtual engagement. He also outlined efforts to reacquire business from advisors that have moved away from SE.

He then moved on to discuss methods for improving the technology experience for firms doing 529 business with the program. A priority list of firms has been developed from both current firms as well as firms where Principal it may have an advantage.

He then asked Mr. Bollin to address some recent changes to the program. Mr. Bollin noted the expansion of the rights of accumulation for Principal Funds held by account owners. Previously only 529 assets had counted. In addition rollover activity will be encouraged by having Principal support a financial incentive for brokers to rollover to the SE program. Finally the commission schedule is being adjusted to lower the amount of assets needed to waive commissions on A shares.

Another component still in development is a lump sum incentive designed to remove commission charges from purchases of $75,000 or more.

Mr. Davis asked if it was common to see a contribution of $75,000 or above. Mr. Miller observed that it was not that common. Mr. Davis thought that it might be a good incentive to encourage larger contributions. Mr. Miller agreed. Mr. Schieber noted that the $75,000 figure was designed to correlate with the maximum amount that can be forward gifted into a 529 account without triggering gift tax consequences.

Mr. Sommer observed that this new feature was a great encouragement to generational planning.

Mr. Miller asked the Chair to call for a motion to amend Exhibit C of the program management agreement to accommodate these new fee arrangements. The chair called for the motion. Mr. Davis so moved. MR. Desiderio seconded the motion. The vote to approve the motion was unanimous.

9) PROGRAM MANAGER'S QUARTERLY OPERATIONS UPDATE AND INVESTMENT REPORT

Mr. Hewitt gave the program manager's operations report. He started with general observations on 529 account owner activity at Ascensus. There has been a reduction in qualified withdrawals although activity is picking up as fall approaches. Non-recurring contributions are down significantly and recurring contribution amounts have been reduced. Towards the end of the quarter these numbers began to increase as well. Call volumes for the New Mexico plans are down for the quarter although also showing a recent increase.

Asset levels for TEP improved for the quarter from $530 million to $580 million. Net accounts were added to TEP in the quarter and so far for the year. Cash flow for the quarter was positive.

Mr. Miller noted that both plans have large numbers of accounts and assets approaching distribution this year and over the next several years. This is a great challenge for both plans, but TEP so far has been holding its own, and growing slightly. SE is in net distribution by both measures.

Mr. Hewitt continued with SE. He noted that the plan recovered value during the quarter from about

$1.3 billion to $1.8 billion. Cash flow was negative by about $4 million. He noted that the proposed changes to accommodate rollovers should help to reduce rollover outflows from SE to other plans.

Mr. Lowe then reviewed the investment performance for the quarter. He noted that the performance improved compared to the first quarter. Most portfolios performed as expected net of fees. Passive portfolios met their benchmarks and active portfolios outperformed or were in line with benchmarks. He noted that the several static passive portfolios showed negative variance from their benchmarks, but that was not unexpected given the small size of the portfolios and the related cash flow. The static active portfolios by and large beat their benchmarks. The year of enrollment portfolios are passive, and showed some variance from benchmarks in the developed and emerging markets. He said this was the result of timing of cash flows and the ability of the managers to get the cash into the markets.

He then reviewed the underling funds that make up the various investment portfolios – noting outperformance and underperformance against benchmarks. In particular he noted the DFA developed and emerging markets funds. These have a small cap and value orientation. Neither asset class has done well in the recent past, but the funds did make up some ground in the quarter. He expressed the hope that reversion to the mean would aid performance over time. He also noted the strong outperformance of the TIAA-CREF and PGIM funds.

He then went over the ranking of the year of enrollment portfolios and underlying funds against their Morningstar categories. He observed that the fund lineup is new, and the markets have been very volatile. In the longer term the funds show better performance.

Mr. welch then reviewed the performance of the SE portfolios. He noted the swift downward movement in the first quarter and the swift recovery in the second quarter. For the quarter all the year of enrollment portfolios exceeded their benchmarks.

Mr. Miller reminded the board that the review of performance was against the R Share class which does not have commissions and trailers. Those costs would weigh down performance in other share classes.

Mr. Welch then noted that the static asset allocation portfolios also had a good quarter and exceeded their benchmarks.

Mr. Fennessey then reviewed the qualitative and quantitative assessments of the SE funds prepared by the Principal manager research team. These include one-, three- and five-year peer rankings, as well as three- and five-year performance ranking against benchmarks. Information and capture ratios are also part of the evaluation. The quantitative rankings for all funds were favorable for the quarter. He also noted the current asset allocations for year of enrollment portfolios.

Mr. Welch observed that the inclusion of the Diversified International Fund with its slightly higher fees was offset by a small increase in the US passive component of the portfolios to offset any overall fee increase foe the portfolios.
(At this point a break was taken from 11:46 AM until 12:09 PM.)

10) INVESTMENT CONSULTANT'S QUARTERLY REPORT

a) Report on GIA carriers

b) Underlying Funds Credit Quality Report

c) Quarterly Investment Report and Watch List Recommendations

Mr. White led off with an update on the GIA carriers. He noted that this is a quarterly report that began last quarter and will be updated as needed in the future. Both providers, NYL and Principal, noted that the quick action by the federal government had stabilized markets after the March disruption. He stated the general accounts of both firms were doing well. Some credit downgrades had occurred but there was no widespread deterioration in the portfolios. In fact the increase in cash flows into the general account had allowed both firms to take advantage of mispriced valuations to add value to the portfolios.

The longer term concern for both carriers was the collapse in interest rates, and the effect that a long period (multiyear) of depressed rates could have on their businesses. Both firms indicated that they were cautious about reaching for yield or materially reducing the credit quality of their portfolios for return.

Ms. Ceserani noted that these meetings are over an hour in length, and the carriers provide detailed information about the nature of their portfolios. Meketa and ETB staff attend as well as high level personnel from each firm. Levels of detail are available in these calls that are not provided in the general materials produced by these companies.

Mr. Miller observed, and Mr. White confirmed that the greatest challenge remains a multiyear period of low interest rates. Mr. Miller also thanked Meketa, and Mr. White in particular, for his suggestion that the board build in a floor return of 1% on its GIA contracts. He noted that this floor protection came at a small cost in yield but was welcome in this low interest environment. Mr. Miller also noted that even with the 1% floor, the C share class at Principal could be at risk of dropping below zero. To forestall that Principal is supporting the portfolio to the extent necessary.

Ms. Ceserani then moved on to the underlying funds credit quality review. She noted that this was an update of the report first prepared last quarter as a result of the market disruption. The review encompasses ten funds in TEP and five funds in SE. She reminded the board of the demarcation line between the lowest investment grade securities (BBB) and the below investment grade market. Moving over that line for a security can cause a significant decrease in value as the market demands higher interest rate to accommodate the increased risk. In addition many funds are restricted to holding investment grade securities. Any security that falls below the line must be sold – often at a loss.

She noted that for the quarter overall investment grade securities holdings increased, but this included an increase in BBB holding as well. Overall there has been an influx if investment into taxable bonds. She noted that the PGIM fund and the Vanguard short-term fund had increased these holding in particular. The Vanguard fund additions were primarily due to holding money market securities to provide some liquidity to the fund.

Mr. Miller asked Ms. Ceserani to explain the various shadings of red assigned to funds in the portfolios. In particular he noted the TIAA-CREF Core Plus Fund, the PGIM Total Return Fund, the Vanguard Ultra Short-Term Fund and the Principal Core Fixed Income Fund. Ms. Ceserani noted that even though these funds were shaded in dark red, they were all actively managed funds with experienced teams, and as a result Meketa was not concerned about the current level of holdings.

Ms. Ceserani then turned to the quarterly report and watch list memorandum. She asked Mr. White to give a brief update on current market conditions. Mr. White observed that the current swings in the market are remarkable for their speed, both down and up. He also noted that Meketa expects a second or even a third wave of COVID infection in the fall. After a vaccine is available (next spring or summer at the earliest) he expected a significant economic rebound based on the increased savings rate of consumers and the pent up demand for goods and services.

He expects the stock market to grind higher over time. Mr. Miller noted that Mr. White had talked in the past about the low interest rate environment for risk free debt securities and the resultant strength in the stock markets as the only alternative for achieving real returns. He asked if Mr. White still held that view. Mr. White said that he did, and that it is a strong driving force behind the stock markets.

Mr. Davis stated that in his view the current interest rate environment was a strong support for the markets, even in the face of renewed outbreaks of COVID. He did express his concern over whether this outperformance could be maintained if corporate earnings did not meet expectations in the longer term.

Ms. Ceserani then proceeded with her review. She began by noting that Morningstar had final agreed to rate the TEP plan. Mr. Miller observed that Morningstar had issued an RFI to 529 plans, and that the RFI response and subsequent Morningstar meeting were critically important for the program. The RFI and the meeting involved ETB staff, Meketa, Ascensus and Principal.

Ms. Ceserani then reviewed the newly released 529 rating system from Morningstar. In particular she noted the reduction in Pillars from 5 to 4, and the inclusion off all plans (direct and advisor-sold) into one overall rating system. This may well result in downgrades for some advisor-sold plans. She also noted the Morningstar bias in favor of 529 plans that use a high proportion of analyst-rated funds.
She then turned to underlying fund performance for the quarter. She noted that TEP funds by and large produced positive results for the quarter against their benchmarks. The exceptions being the American Funds fund and the Vanguard high-yield corporate fund. The Vanguard fund was held back by the high quality restrictions imposed on the fund.

She then turned to SE and noted the overall good performance or outperformance of nearly all the funds. Even the few underperforming funds had 50 bps or less of underperformance.

Turning to the watch criteria. For TEP 15 of the 20 funds were rated either positive or acceptable. For SE all funds were rated positive or acceptable. There were no funds in either plan for which action was recommended.

Ms. Liggett asked a question in reference to the steep decline in the energy sector. Mr. White stated that over the last year as of June 30, the sector had decline 37%. Even a 32% rebound in the last quarter was not sufficient to make up for the overall loss in value. He expected that the sector would continue to suffer due to the sharp drop in fossil fuel use as a result of the CVOVID crisis.

Ms. Ceserani then stated that no funds in the program qualified for watch status for the quarter. Mr. Miller observed that the board would need to vote to accept that recommendation. The Chair called for a motion to accept the consultant's watch list recommendation. Mr. Davis so moved. Mr. Green seconded the motion. The vote to approve the motion was unanimous.

11) ADJOURNMENT

At this point the Chair called for a motion to adjourn. Mr. Davis so moved. Mr. Desiderio seconded the motion. The vote to approve the motion was unanimous.

The meeting adjourned at 1:05 PM.