

State Board of Education Committee on School Finance/Permanent School Fund

&

School Land Board

Annual Joint Meeting

10:00 AM, June 4, 2020

AGENDA

- 1) SBOE Committee on School Finance/Permanent School Fund (Committee)
Call to Order by Chair Maynard
- 2) SBOE Committee Roll Call
- 3) SLB Call to Order by Commissioner Bush
- 4) SLB Roll Call and possible vote to excuse any absent SLB members
- 5) SBOE Committee Chair Maynard calls on SBOE Chair Ellis for brief opening
 - a. Purpose of Meeting
 - b. Statutory directive:

The boards are meeting pursuant to Section 32.0161, Natural Resources Code, which requires the boards to hold an annual joint meeting to discuss the allocation of the assets and the investment of the money in the PSF. *(Enacted by SB 608, 86th Leg., R.S.)*
- 6) SBOE Member introductions
- 7) SLB Commissioner Bush brief opening
- 8) SLB Member introductions
- 9) Presentation from SLB
 - a. Rusty Martin, Chief Investment Officer, General Land Office
 - b. Questions
- 10) Presentation from SBOE
 - a. Holland Timmins, Chief Investment Officer, Texas Education Agency
 - b. Questions
- 11) Discussion about next year's meeting
- 12) Summary of meeting
- 13) Adjourn

Annual Joint Meeting of School Land Board and State Board of Education

As Required by Section 32.0161(a), Natural Resources Code

June 4, 2020

PRESENTATION BY: RUSTY MARTIN, CHIEF INVESTMENT OFFICER, TXGLO



Annual Joint Meeting of
School Land Board and
State Board of Education
June 4, 2020

TXGLO PSF Investment Portfolio Asset Types and Target Weightings

*(100% Private-Markets Real Assets
Investments Only)*

TXGLO PSF ASSET TYPES AND TARGET WEIGHTINGS

Energy/Minerals/Other Real Assets - 35% of Total Net Asset Value ("NAV")

The Energy/Minerals/Other Real Assets allocation will primarily target oil and natural gas investments in the upstream and oilfield services sectors, as well as various renewable energy assets and projects. The Energy allocation will focus primarily on oil and natural gas investments, but will be diversified by strategy and sector.

Infrastructure - 32% of Total Net Asset Value ("NAV")

The Infrastructure allocation will primarily target long-lived assets that provide essential services (e.g., toll roads and bridges; airports; seaports; rail facilities; power plants; and midstream oil and natural gas assets, such as pipelines and associated processing, storage, and transportation facilities). The Infrastructure allocation will be diversified by strategy and sector.

Real Estate - 33% of Total Net Asset Value ("NAV")

The Real Estate allocation will primarily target a collection of commercial real estate assets that is diversified across the main real estate sectors (i.e., office; multifamily; hotel; retail; and industrial) with a focus on niche opportunities that may arise within the main sectors (e.g., senior living or student housing opportunities within the multifamily sector). The Real Estate allocation will be diversified by strategy and sector and will generally pursue a target mix of 25% Core assets and 75% Non-Core assets (i.e., value-added or opportunistic investments).

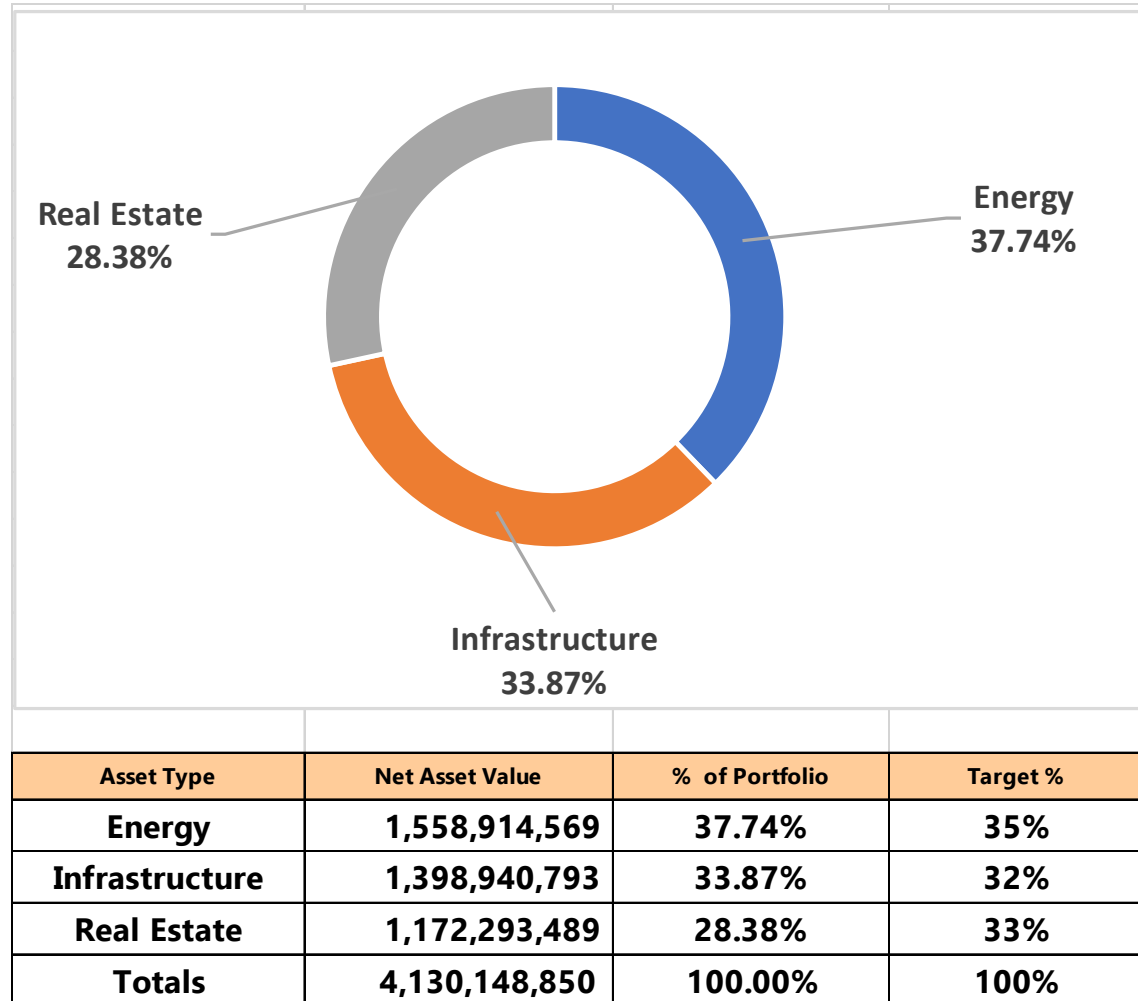
Annual Joint Meeting of
School Land Board and
State Board of Education
June 4, 2020

TXGLO PSF Investment Portfolio Actual Asset Allocations

(Based on NAV)

TXGLO PSF ACTUAL ASSET ALLOCATIONS

at December 31, 2019



**Annual Joint Meeting of
School Land Board and
State Board of Education
June 4, 2020**

Procedures for the Release of Funds from the RESFA to the ASF or to SBOE for Investment in the PSF

*Section 151.6, Title 31, Chapter 4,
Texas Administrative Code*

PROCEDURES FOR DETERMINING RELEASES FROM RESFA TO SBOE OR ASF

The School Land Board (SLB) determines the dates that releases will be made and the amounts of money that will be released from the Real Estate Special Fund Account (RESFA) to either the Available School Fund (ASF) or the State Board of Education (SBOE) for investment in the Permanent School Fund (PSF) according to the rules required by Section 51.413(b), Texas Natural Resources Code summarized below:

- Not later than July 31 of each even-numbered year, the TXGLO Chief Investment Officer (CIO) will perform an analysis to determine an amount equal to 6% of the average market value of the TXGLO PSF Investment Portfolio over the trailing sixteen-quarter measurement period.
- Not later than September 1 of each even-numbered year, the CIO will provide the SLB with the results of the analysis performed above and present options regarding the possible release of funds from the RESFA. The SLB will adopt a resolution detailing any actual amounts to be released to either the ASF or the SBOE for investment in the PSF in each of the individual years of the next-approaching fiscal biennium and the actual dates of the releases.
- Also not later than September 1 of each even-numbered year, the SLB, in consultation with the CIO, will submit a report to the Legislature, Comptroller, SBOE, and Legislative Budget Board that states the dates and amounts approved by the SLB for release from the RESFA to either the ASF or SBOE for investment in the PSF during the next-approaching fiscal biennium.

Annual Joint Meeting of
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June 4, 2020

History of TXGLO PSF Releases from Real Estate Special Fund Account (RESFA) to State Board of Education or Available School Fund (ASF)

(\$ millions)

HISTORY OF RELEASES FROM RESFA TO SBOE OR ASF *(\$ millions)*

Fiscal Year	Amounts Released	Amounts Released	Total Amounts Released
	to SBOE for Investment	Directly to ASF	to SBOE or ASF
	<i>(\$ millions)</i>	<i>(\$ millions)</i>	<i>(\$ millions)</i>
2002	-		
2003	95		95
2004	132		132
2005	261		261
2006	78		78
2007	78		78
2008	100		100
2009	100		100
2010	100		100
2011	100		100
2012	250		250
2013	250	300	550
2014	130		130
2015	150		150
2016	175		175
2017	200		200
2018	235		235
2019	255	300	555
2020	10	300	310
2021	45	300	345
	2,744	1,200	3,944

¹ Source: TXGLO Financial Reporting Division Reconciliation to RESFA Activity

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TEXAS PERMANENT SCHOOL FUND

State Board of Education & School Land Board
2020 Annual Joint Meeting
June 4, 2020

TEXAS PERMANENT SCHOOL FUND

State Board of Education

Committee on Instruction

Sue Melton-Malone, chair

Pam Little, vice chair

Aicha Davis

Georgina C. Pérez, *SBOE secretary*

Marty Rowley, *SBOE vice chair*

Committee on School Finance / Permanent School Fund

Tom Maynard, chair

Lawrence A. Allen, Jr., vice chair

Patricia Hardy

Ken Mercer

Donna Bahorich

Committee on School Initiatives

Barbara Cargill, chair

Marisa B. Perez-Diaz, vice chair

Ruben Cortez, Jr.

Keven Ellis, *SBOE chair*

Matt Robinson

School Land Board

Commissioner George P. Bush, chair

Gilbert Burciaga

Scott Rohrman

Michael A. Neill

Todd Williams

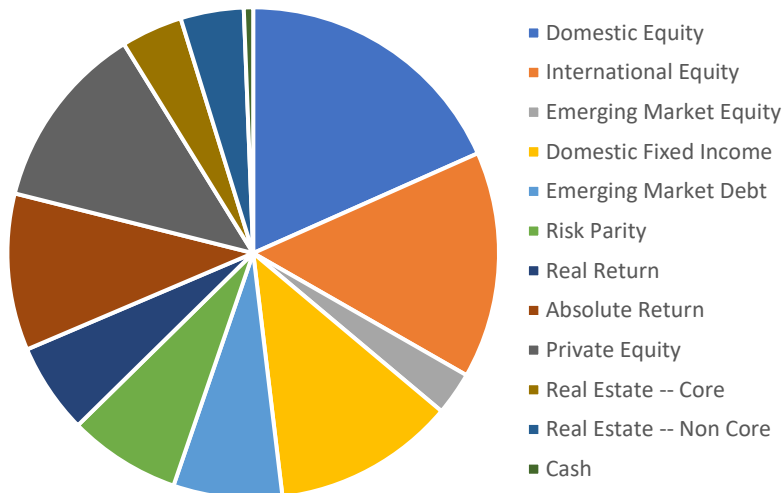
TPSF – ASSET ALLOCATION BY BOARD

December 31, 2019

State Board of Education

Asset Class	Amount	Percent*
Domestic Equity	\$ 6,581,155,749	18%
International Equity	\$ 5,357,143,110	15%
Emerging Market Equity	\$ 1,018,836,288	3%
Domestic Fixed Income	\$ 4,297,940,271	12%
Emerging Market Debt	\$ 2,569,806,767	7%
Risk Parity	\$ 2,649,793,818	7%
Real Return	\$ 2,135,546,450	6%
Absolute Return	\$ 3,700,046,973	10%
Private Equity	\$ 4,405,280,378	12%
Real Estate – Core	\$ 1,451,533,838	4%
Real Estate – Non Core	\$ 1,490,634,579	4%
Cash	\$ 220,133,885	0.6%
SBOE Total	\$ 35,877,852,106	100%

Total PSF	\$ 48,312,317,792	74%
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School Land Board

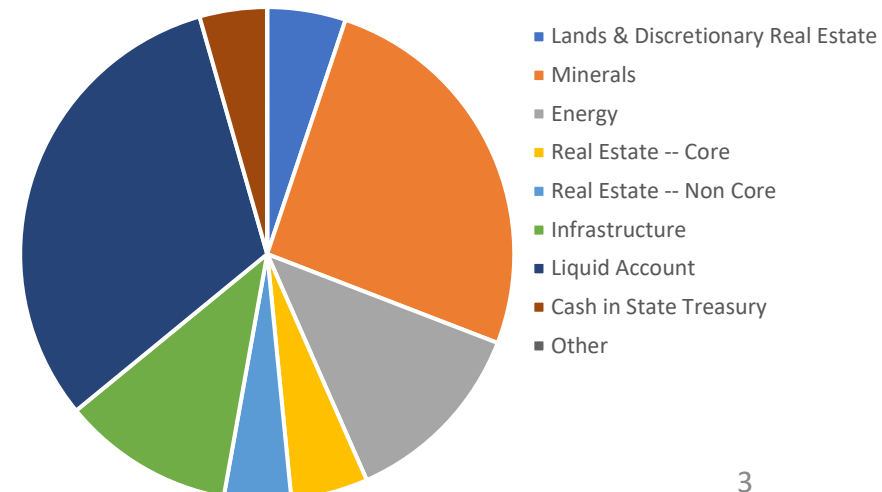
Asset Class	Amount	Percent*
Lands & Discretionary Real Estate ⁺	\$ 638,943,445	5%
Minerals [#]	\$ 3,198,174,631	26%
Energy	\$ 1,558,914,569	13%
Real Estate – Core	\$ 626,304,912	5%
Real Estate – Non Core	\$ 545,988,577	4%
Infrastructure	\$ 1,398,940,793	11%
Liquid Account	\$ 3,917,799,058	31%
Cash in State Treasury ⁺	\$ 548,614,340	4%
Other ⁺	\$ 785,361	0%
SLB Total	\$ 12,434,425,686	100%

Total PSF	\$ 48,312,317,792	26%
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*Numbers may not add to 100% due to rounding.

+ Values as of November 30, 2019.

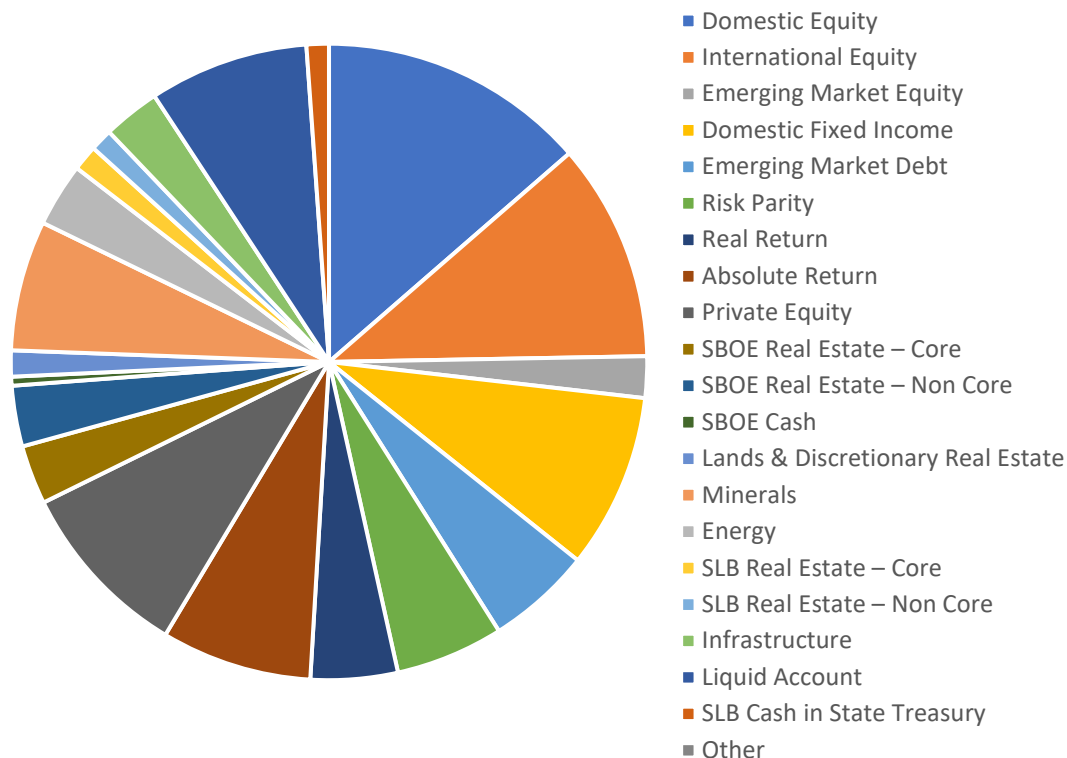
Value as of August 31, 2019.



TPSF – ASSET ALLOCATION OF TOTAL FUND

December 31, 2019

Total PSF		
Asset Class	Amount	Percent*
Domestic Equity	\$ 6,581,155,749	14%
International Equity	\$ 5,357,143,110	11%
Emerging Market Equity	\$ 1,018,836,288	2%
Domestic Fixed Income	\$ 4,297,940,271	9%
Emerging Market Debt	\$ 2,569,806,767	5%
Risk Parity	\$ 2,649,793,818	5%
Real Return	\$ 2,135,546,450	4%
Absolute Return	\$ 3,700,046,973	8%
Private Equity	\$ 4,405,280,378	9%
SBOE Real Estate – Core	\$ 1,451,533,838	3%
SBOE Real Estate – Non Core	\$ 1,490,634,579	3%
SBOE Cash	\$ 220,133,885	0.5%
Lands & Discretionary Real Estate ⁺	\$ 638,943,445	1%
Minerals [#]	\$ 3,198,174,631	7%
Energy	\$ 1,558,914,569	3%
SLB Real Estate – Core	\$ 626,304,912	1%
SLB Real Estate – Non Core	\$ 545,988,577	1%
Infrastructure	\$ 1,398,940,793	3%
Liquid Account	\$ 3,917,799,058	8%
SLB Cash in State Treasury ⁺	\$ 548,614,340	1.1%
Other ⁺	\$ 785,361	0%
Total PSF	\$ 48,312,317,792	100%



**Numbers may not add to 100% due to rounding.*

+ Values as of November 30, 2019.

Value as of August 31, 2019.

TPSF – LIQUID ACCOUNT¹

Liquid Account Implementation

- The SBOE, working with PSF staff and NEPC, the board's general investment consultant, adopted an asset allocation framework for the Liquid Account and has begun to implement the plan within two timeframes.
 - **Near-term horizon** (2019 & 2020)
 - ✓ Obtain exposures that will outperform cash in the near term.
 - ✓ Purchase short duration fixed income assets.
 - **Long-term horizon** (2020 & 2021)
 - ✓ Construct a diversified, liquid portfolio that exceeds the return of a dynamically-weighted allocation index.
 - ✓ Current and future PSF (SBOE) asset allocation targets will serve as a base for formulating the Liquid Account targets and utilize existing internal and external investment managers and vehicles.
 - ✓ Implementation speed of the ultimate asset allocation should be done in light of the market environment.

1. The PSF Liquid Account was created by HB 4388, 86th Legislature, Regular Session.

TPSF – LIQUID ACCOUNT

Liquid Account Summary as of April 2020

Transfers from SLB ¹		
September 3, 2019	\$ 3,900,000,000	
January 16, 2020	\$ 145,000,000	
Total Transferred from SLB		\$ 4,045,000,000
Liquid Account Investments		
Investments	\$ 1,658,105,645	
Cash at State Treasury	\$ 2,404,965,251	
Fair Value of Investments		\$ 4,063,070,896

1. On May 19, 2020, the SLB approved moving an additional \$200 million to the Liquid Account.

- Since the initial transfer of funds from the SLB to the Liquid Account:
 - ✓ Over \$52 million in income and realized gains have been earned.
 - ✓ Over \$30 million has been released from the Liquid Account to the PSF (SBOE).

TPSF – LIQUID ACCOUNT

Historical Yields

Month End	U.S. Treasury 3 year	State of Texas Treasury	Liquid Account¹
September 2019	1.56%	2.29%	2.52%
October 2019	1.52%	2.22%	2.28%
November 2019	1.61%	2.15%	2.39%
December 2019	1.62%	2.07%	2.23%
January 2020	1.30%	2.00%	2.06%
February 2020	0.85%	1.93%	1.95%
March 2020	0.29%	1.54%	2.69%
April 2020	0.24%	1.19%	1.86%
May 2020	0.19%	1.09%	1.55%
<i>Average</i>	<i>1.02%</i>	<i>1.83%</i>	<i>2.17%</i>

1. The Liquid Account yield is for the invested portion of the account.

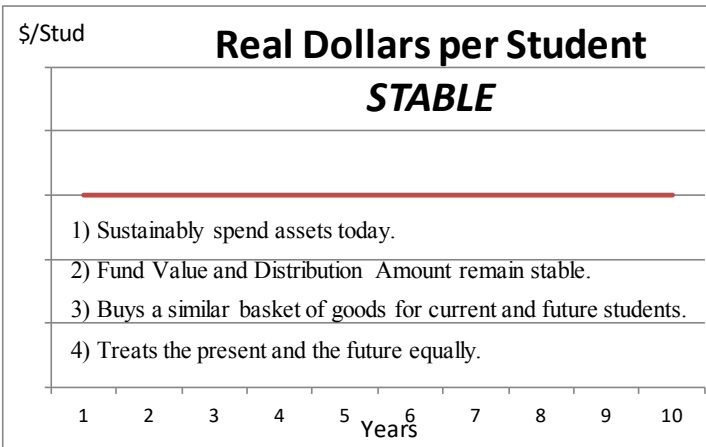
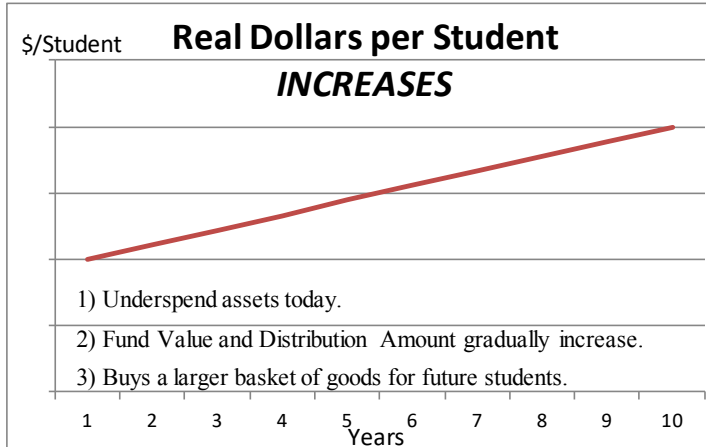
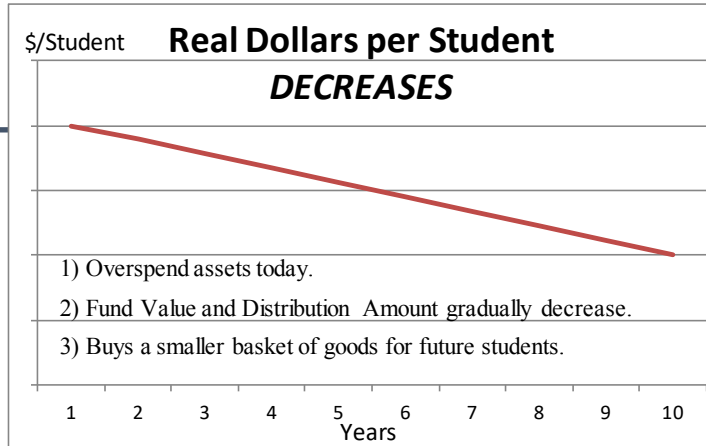
TPSF – SBOE DISTRIBUTIONS

Hypothetical Endowment Spending Options

- In 1974, James Tobin, Nobel prize recipient and former Federal Reserve Board governor, provided an influential, normative principle for endowment management and distributions:

“The trustees of endowed institutions are the guardians of the future against claims of the present. Their task is to preserve equity among generations. . . . [which] means in principle that the existing endowment can continue to support the same set of activities that it is now supporting.”¹

1. Tobin, James. 1974. “What is Permanent Endowment Income?” *American Economic Review*, 64:2, p427.



TPSF – SBOE DISTRIBUTIONS

Spending Rate Structure

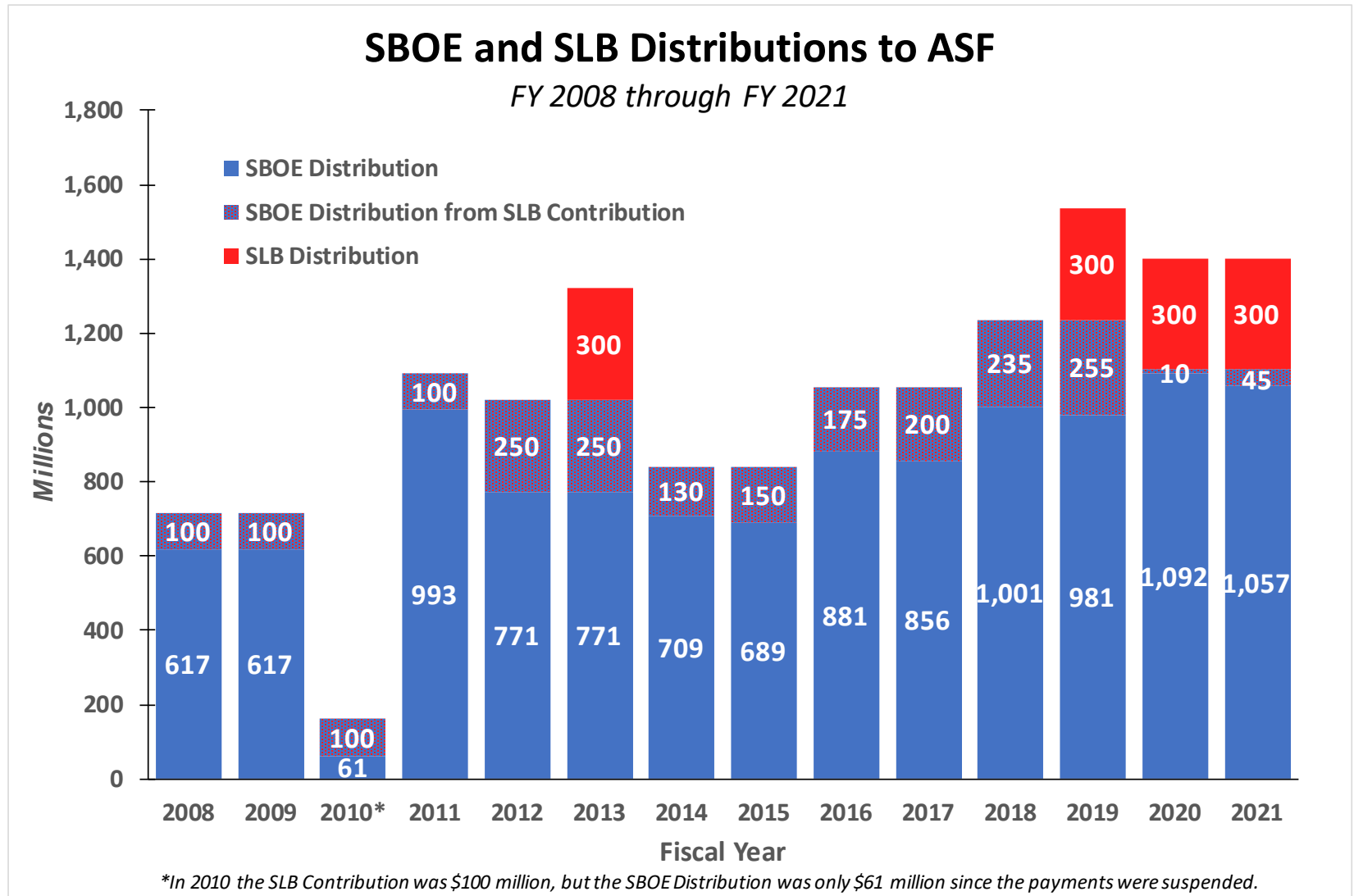
used by SBOE to balance the needs of current and future students

<i>HYPOTHETICAL FIGURES</i>	
Expected Total Return (+)	7.00%
Rate of Inflation (CPI) (-)	2.00%
Student Population Growth (-)	1.50%
Administrative Expenses (-)	0.10%
School Land Board Contribution ¹ (+)	0.50%
Sustainable Spending Rate (=)	3.90%
Real Growth Rate of Endowment	0.00%

1. SLB contributions have ranged from 0.07% to 1.26% of the PSF (SBOE) market value since FY 2004.

- The Spending Rate is applied to the 16-quarter average fair value of the PSF (SBOE) and PSF (SLB) assets, except sovereign lands and minerals, to arrive at the annual dollar amount distributed. *(See Texas Constitution, Article VII, Section 5(a).)*

TPSF – DISTRIBUTIONS TO ASF



TPSF – BOND GUARANTEE PROGRAM

The PSF also benefits public education by guaranteeing most of the debt issued by school districts and charter schools through the Bond Guarantee Program.

- Bonds with a PSF guarantee receive a AAA credit rating.
- Since its creation in 1983, the Fund has guaranteed almost 7,400 school district bond issues valued at over \$184 billion, saving schools **billions of dollars** in interest expense.
- The assets of the Fund have never been called on to pay debt service on a defaulted bond.
- At the end of FY 2019, the BGP capacity was just over \$117 billion.

TPSF – BOND GUARANTEE PROGRAM

Amounts Guaranteed & Credit Rating

- At the end of FY 2019, the PSF guaranteed:
 - ~3,300 school district debt issues with a balance of \$82.5 billion; and,
 - 49 charter school debt issues with a balance of about \$1.9 billion.
 - ❖ The Charter District Bond Guarantee Reserve Fund provides additional financial backing for charter school guaranteed bonds.
- To ensure sustainability of this critical program, the SBOE continually evaluates the impact Fund management decisions could have on the BGP's credit rating.
 - Moody's Credit Opinion, February 2019: “[C]onstitutional amendments permitting greater distribution of fund assets for non-guarantee purposes” was listed as a factor that could lead to a downgrade in credit rating.
 - Standard & Poor's report, June 2019: “The stable outlook reflects our expectation that strong fund oversight, coupled with sufficient liquidity levels, will continue.”
 - Fitch Rating's report, November 2019: “Deterioration in the aggregate credit quality of the participants [in the BGP], substantial reductions in the market value of the fund assets, a move toward less liquid asset types, or a significant increase in program leverage could put negative pressure on the rating.”