



November 15, 2018

## City of Fort Pierce

### Third Quarter Performance Review

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# Market Environment 3Q18: Global Economy

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*At the head of the pack, the U.S. economy continued to feel the shot of adrenaline provided by early 2018 tax cuts and fiscal stimulus, recording +4.2% real GDP growth in the second quarter and an estimated +3.6% in the third quarter. Overseas, the economic picture was less bright with trade headwinds and several idiosyncratic stories weighing on growth.*

- Labor market strong
  - Unemployment at 3.7% in October; lowest since 1969
  - Job gains averaged just over 185,000 for past three months
  - Wages inching up +2.8% (y/y) in September
- Inflation remained well-behaved
  - Headline CPI was 2.7% in September (y/y); Core CPI was 2.2% (y/y)
  - Rising oil prices, tariffs, tight labor market conditions could become headwinds
  - Core PCE in line with Fed's 2% target
- Consumer confidence soars
  - Conference Board Consumer Confidence Index highest since September 2000
  - Retail spending slowed in August, but up 6.6% y/y; a multi-year high
- The Fed raised rates as expected
  - A 25 bp hike in September brought target to 2.00% –2.25%; “accommodative” dropped from language
  - The Fed expects one more rate hike this year and three in 2019
  - Markets have priced in fewer but are moving closer to Fed projections
- Euro Zone
  - Core inflation for the EMU unchanged at 1.1%
  - Euro zone manufacturing sank to a 2-year low in September on slowing exports
  - ECB affirmed plan to cut asset purchases in half from October through December and likely halting altogether at year-end
  - Left benchmark rate unchanged at -0.4%
  - Politics and fiscal woes in Italy worried investors, causing yields on Italian bonds to surge
  - ECB lowered 2018 growth forecast to 2.0% from 2.1%
- Brexit negotiations are thorny, prospect of a “hard” Brexit remains
  - Rates unchanged at 0.75% in spite of a surprise spike in inflation (2.7% in August)
- Japan's economy gained traction; 2<sup>nd</sup> quarter GDP of 3% was the fastest since 2016
  - Capital expenditures was a key driver
  - Demographic woes pushed jobless rate to lowest in more than 25 years
- China / U.S. trade “wars” continue
  - Trump imposed a 10% tariff on \$200 bn in goods - rising to 25% on January 1<sup>st</sup> – and on top of \$50 billion earlier this year
  - China responded with \$60 bn in tariffs and cancelled trade talks

# Market Environment 3Q18: Global Equity

The U.S. equity market posted broad-based gains in the third quarter fueled by strong economic growth, soaring corporate profits, and record-breaking stock buybacks. Several major indices hit record levels during the quarter, and the S&P 500 Index's 7.7% gain was its biggest since the fourth quarter of 2013. Non-U.S. developed markets underperformed the U.S. and emerging market equities fared the worst, posting modest losses for the quarter.

## U.S. Equity

- S&P 500 Index rose 7.7%
  - Bringing y-t-d return to 10.6%
  - Best quarterly result since 4Q 2013
  - All sectors were positive, but differences were sharp
  - Health Care (+14.5), Industrials (+10.0%), Technology (+8.8%), and the new Communication Services (+9.9%) sectors were the top performers
  - Materials, Energy, and Real Estate returned less than 1% for the quarter
- Growth continued to outperform Value, widening y-t-d divergence
  - R1000 Growth: +9.2%; +17.1% y-t-d
  - R1000 Value: +5.7%; +3.9% y-t-d
- Large caps outperformed small caps and pulled ahead y-t-d
  - R1000: +7.4%; +10.5% y-t-d
  - R2000: +3.6%; +11.5% y-t-d
  - Large caps helped by double-digit returns from Amazon, Apple and Microsoft
  - “FAANG” stocks plus Microsoft had a more muted impact than in previous quarters, but still contributed nearly 25% of the S&P 500's quarterly return

## Non-U.S. Equity

- Non-U.S. developed indices continued to underperform U.S. as growth did not keep pace and trade worries weighed on markets
  - ACWI ex-US: +0.7%; -3.1% y-t-d
  - Japan was a top performer +3.7% as economic news surprised on the upside and the Prime Minister retained his role as President
  - Switzerland and Sweden both up over 7%
  - Italy (-4.5%) was roiled by political and fiscal woes
  - Concern over the fate of Brexit hurt the UK (-1.7%)
  - As in the U.S., Health Care (+4.3%) was a top performing sector while Real Estate (-2.8%) was among the worst
- Dollar was mixed
  - Up versus the Japanese yen, Australian dollar and British pound
  - Down versus the Canadian dollar
  - Essentially flat versus the euro
- Emerging markets lagged
  - MSCI EM: -1.1%; -7.7% y-t-d
  - Not atypically, returns across countries highly divergent
  - China sank (-7.5%) on trade angst and a sell-off in tech companies
  - Greece (-17.6%) and Turkey (-20.5%) were among the worst
  - Mexico (+6.9%), Brazil (+6.1%) Russia (+6.2%) and Poland (+10.6%) on top

# Market Environment 3Q18: Global Fixed Income

*Yields in the U.S. rose during the quarter and the yield curve continued to flatten as the Fed continued on its rate hike trajectory. Outside of the U.S., the U.S. dollar turned in mixed performance and yields were generally modestly higher.*

- **U.S. rates rose modestly and the yield curve continued to flatten**

- 2-year U.S. Treasury Note climbed nearly 30 basis points to close at a multi-year high of 2.81%
- 10- and 30-year Treasury yields rose roughly 20 bps
- Spread between the 2-year and 10-year shrank to 24 bps

- **Bloomberg Barclays Aggregate was flat (+0.0%)**

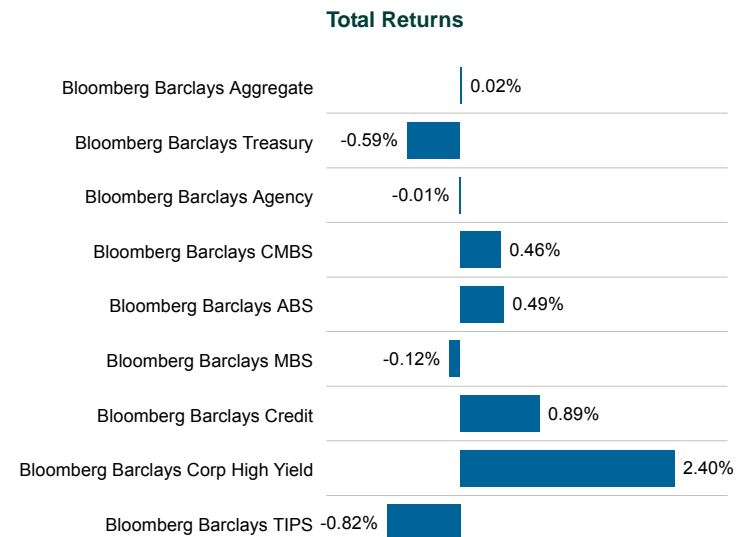
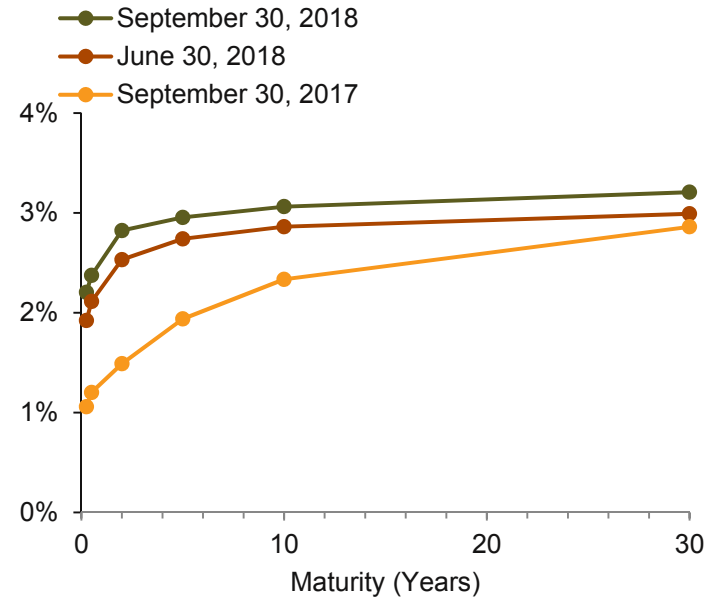
- Investment grade corporates (+1.0%) beat Treasuries (-0.6%) for the first time this year
- However, concerns about rising leverage and significant growth in BBB rated bonds weigh on investors' minds

- **Breakeven inflation expectations rose**

- 10-year breakeven inflation rate rose modestly to 2.14% (9/30) from 2.11% (6/30)
- Bloomberg Barclays TIPS Index -0.8%; -0.8% y-t-d

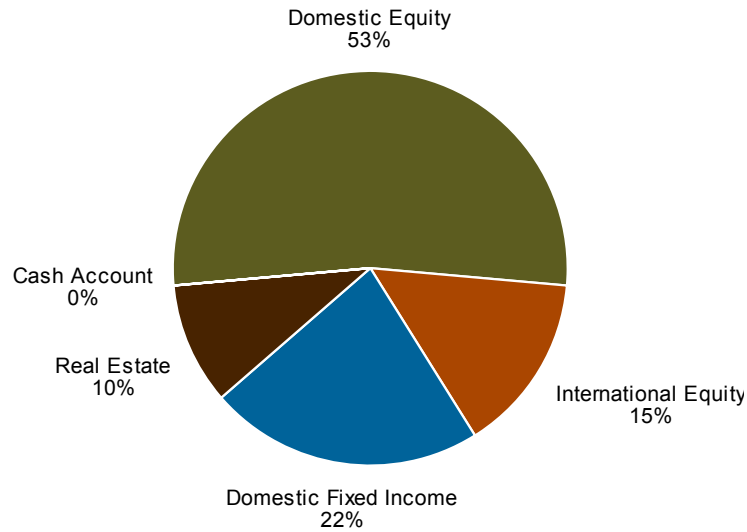
- **High yield corporates outperformed investment grade**

- Bloomberg Barclays High Yield: +2.4%; +2.6% y-t-d
- Supply down sharply from 2017; demand for yield continued

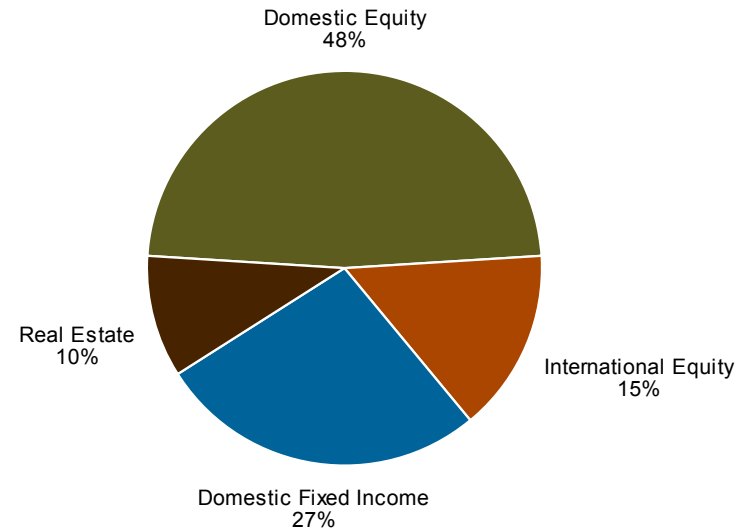


# Asset Allocation Review

**Actual Asset Allocation**



**Target Asset Allocation**



Asset Class	\$000s Actual	Weight Actual	Target	Percent Difference	\$000s Difference
Domestic Equity	107,788	52.9%	48.0%	4.9%	9,957
International Equity	29,919	14.7%	15.0%	(0.3%)	(653)
Domestic Fixed Income	45,766	22.5%	27.0%	(4.5%)	(9,264)
Real Estate	20,293	10.0%	10.0%	(0.0%)	(88)
Cash Account	48	0.0%	0.0%	0.0%	48
<b>Total</b>	<b>203,813</b>	<b>100.0%</b>	<b>100.0%</b>		

**Relative Attribution Effects for Quarter ended September 30, 2018**

Asset Class	Effective Actual Weight	Effective Target Weight	Actual Return	Target Return	Manager Effect	Asset Allocation	Total Relative Return
Domestic Equity	51%	48%	6.56%	6.46%	0.05%	0.09%	0.14%
Domestic Fixed Income	23%	27%	0.10%	0.02%	0.02%	0.13%	0.15%
Real Estate	11%	10%	1.96%	1.88%	0.01%	(0.01%)	(0.00%)
International Equity	15%	15%	0.09%	0.71%	(0.09%)	(0.00%)	(0.09%)
Cash Account	0%	0%	0.46%	0.46%	0.00%	(0.00%)	(0.00%)

**Total** **3.59% = 3.40% + (0.01%) + 0.20%** **0.19%**

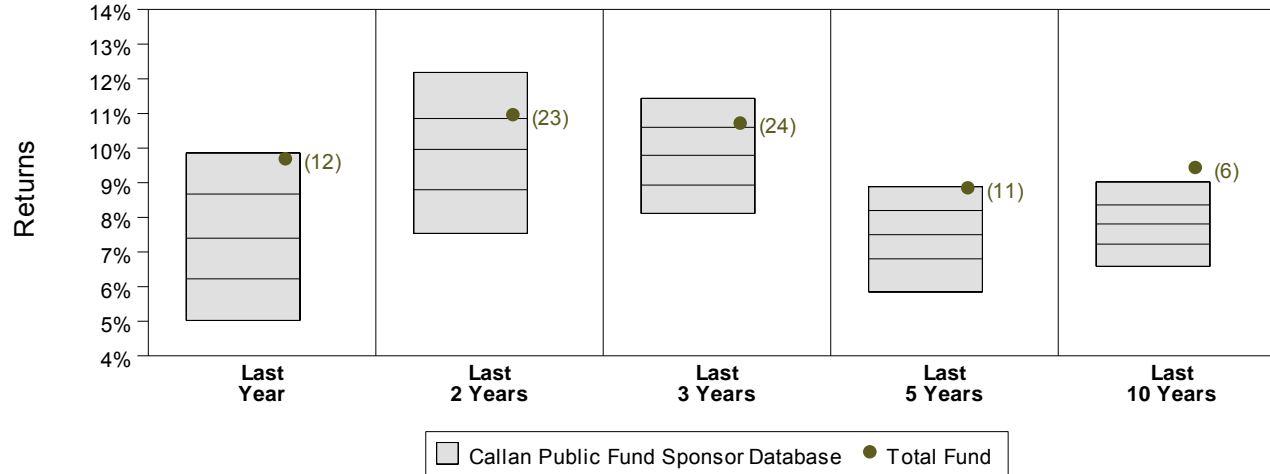
# Asset Distribution Across Investment Managers

	September 30, 2018				June 30, 2018			
	Market Value	Weight	Target	Net New Inv.	Inv. Return	Market Value	Weight	Target
<b>Domestic Equity</b>	<b>\$107,787,546</b>	<b>52.89%</b>	<b>48.00%</b>	<b>\$(47,061)</b>	<b>\$6,641,272</b>	<b>\$101,193,335</b>	<b>50.64%</b>	<b>48.00%</b>
Emerald Advisers, Inc.	9,977,318	4.90%	3.75%	(18,780)	646,247	9,349,852	4.68%	3.75%
Ceredex Value Advisors	8,138,088	3.99%	3.75%	(18,046)	123,424	8,032,711	4.02%	3.75%
SSgA S&P 500 Index	73,454,818	36.04%	33.00%	(7,161)	5,268,939	68,193,040	34.13%	33.00%
SSgA S&P 400 Index	16,217,321	7.96%	7.50%	(3,074)	602,663	15,617,733	7.82%	7.50%
<b>International Equity</b>	<b>\$29,918,712</b>	<b>14.68%</b>	<b>15.00%</b>	<b>\$(26,643)</b>	<b>\$27,912</b>	<b>\$29,917,443</b>	<b>14.97%</b>	<b>15.00%</b>
Morgan Stanley Int'l Equity	14,097,186	6.92%	7.00%	(26,643)	63,382	14,060,446	7.04%	7.00%
Morgan Stanley Emerging Mkts.	1,233,845	0.61%	1.00%	0	(35,470)	1,269,315	0.64%	1.00%
William Blair & Company	14,587,682	7.16%	7.00%	0	0	14,587,682	7.30%	7.00%
<b>Domestic Fixed Income</b>	<b>\$45,765,870</b>	<b>22.45%</b>	<b>27.00%</b>	<b>\$(34,659)</b>	<b>\$43,752</b>	<b>\$45,756,777</b>	<b>22.90%</b>	<b>27.00%</b>
Richmond Capital Management	45,765,870	22.45%	27.00%	(34,659)	43,752	45,756,777	22.90%	27.00%
<b>Real Estate</b>	<b>\$20,292,935</b>	<b>9.96%</b>	<b>10.00%</b>	<b>\$(3,000,000)</b>	<b>\$390,685</b>	<b>\$22,902,250</b>	<b>11.46%</b>	<b>10.00%</b>
Heitman	20,292,935	9.96%	10.00%	(3,000,000)	390,685	22,902,250	11.46%	10.00%
<b>Cash Account</b>	<b>\$48,087</b>	<b>0.02%</b>	<b>0.00%</b>	<b>\$0</b>	<b>\$221</b>	<b>\$47,866</b>	<b>0.02%</b>	<b>0.00%</b>
<b>Total Fund</b>	<b>\$203,813,150</b>	<b>100.0%</b>	<b>100.0%</b>	<b>\$(3,108,363)</b>	<b>\$7,103,843</b>	<b>\$199,817,671</b>	<b>100.0%</b>	<b>100.0%</b>

- The total fund increased by \$4.0 million over the quarter to \$203.8 million as of September 30, 2018

# City of Fort Pierce Total Fund

Callan Public Fund Sponsor Database



	Last Quarter		Last Year		Last 3 Years		Last 5 Years		Last 7 Years	
<b>Total Fund</b>	<b>3.59%</b>	<b>11</b>	<b>9.65%</b>	<b>12</b>	<b>10.68%</b>	<b>24</b>	<b>8.82%</b>	<b>11</b>	<b>11.12%</b>	<b>10</b>
Total Fund Benchmark(1)	3.40%	19	8.66%	25	10.77%	20	8.48%	18	10.51%	21
CPI + 5%	1.37%	95	7.34%	51	6.96%	95	6.36%	85	6.40%	96
Callan Public Fund Spr DB	2.66%		7.40%		9.79%		7.50%		9.41%	

- The Total Fund was ahead of the benchmark for the quarter and ranked near the top decile of peers
- Total Fund performance relative to the benchmark and peers has remained strong over time

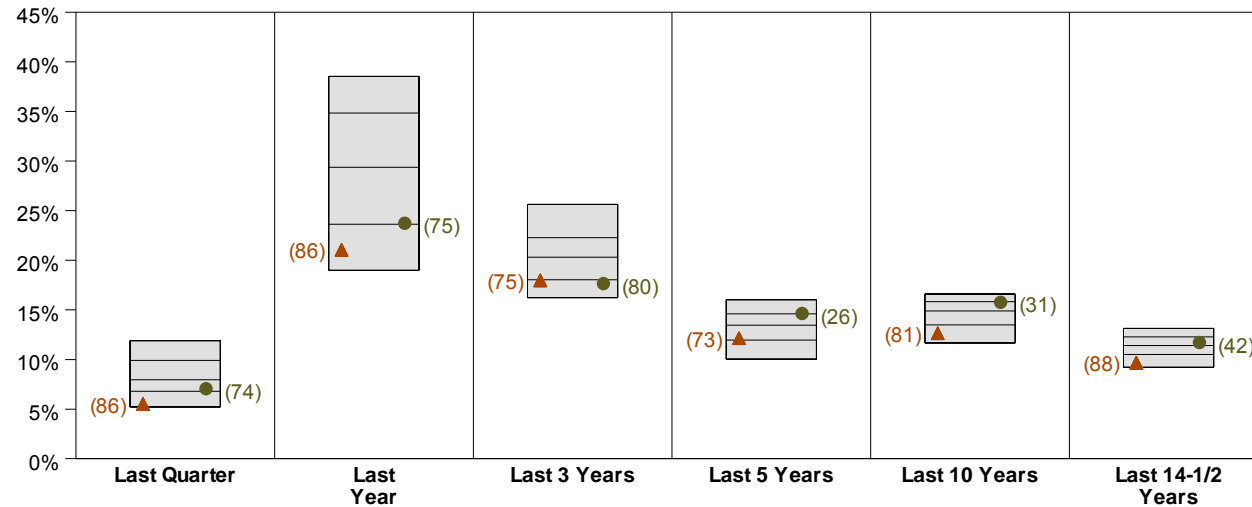
(1) The Total Fund Benchmark consists of 33% S&P 500 Index, 27% Blmbg Aggregate Index, 15% MSCI ACWI ex US (Net), 10% NFI-ODCE Equal Weight Net, 7.50% S&P MidCap 400, 3.75% Russell 2000 Growth and 3.75% Russell 2000 Value.



## Domestic Equity Performance

# Emerald Advisors Small Cap Growth

Performance vs Callan Small Cap Growth (Gross)

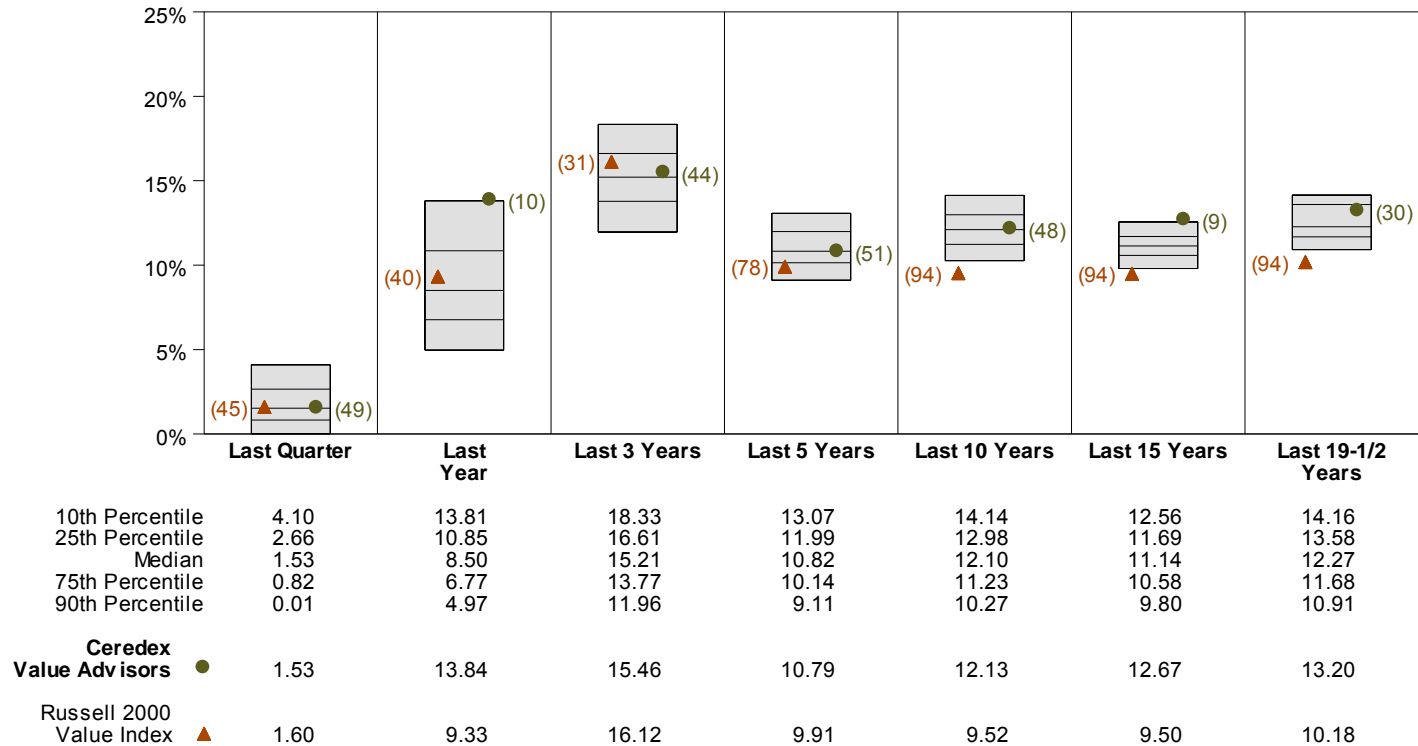


10th Percentile	11.90	38.53	25.64	16.02	16.61	13.14
25th Percentile	9.91	34.83	22.27	14.60	15.83	12.27
Median	7.95	29.38	20.31	13.45	14.89	11.41
75th Percentile	6.80	23.64	18.04	11.96	13.50	10.51
90th Percentile	5.22	18.99	16.23	10.04	11.67	9.22
<b>Emerald Advisers, Inc.</b>	● 6.92	23.60	17.51	14.48	15.63	11.57
Russell 2000 Growth Index	▲ 5.52	21.06	17.98	12.14	12.65	9.67

- Emerald outperformed the benchmark by 1.39% during the quarter and outperformed by 2.54% over the last year
- Emerald has strong long-term returns well above the benchmark
- Outperformance for the quarter was driven by stock selection in Healthcare, Materials, Consumer Discretionary, Consumer Staples and Utilities sectors

# Ceredex Value Advisors Small Cap Value

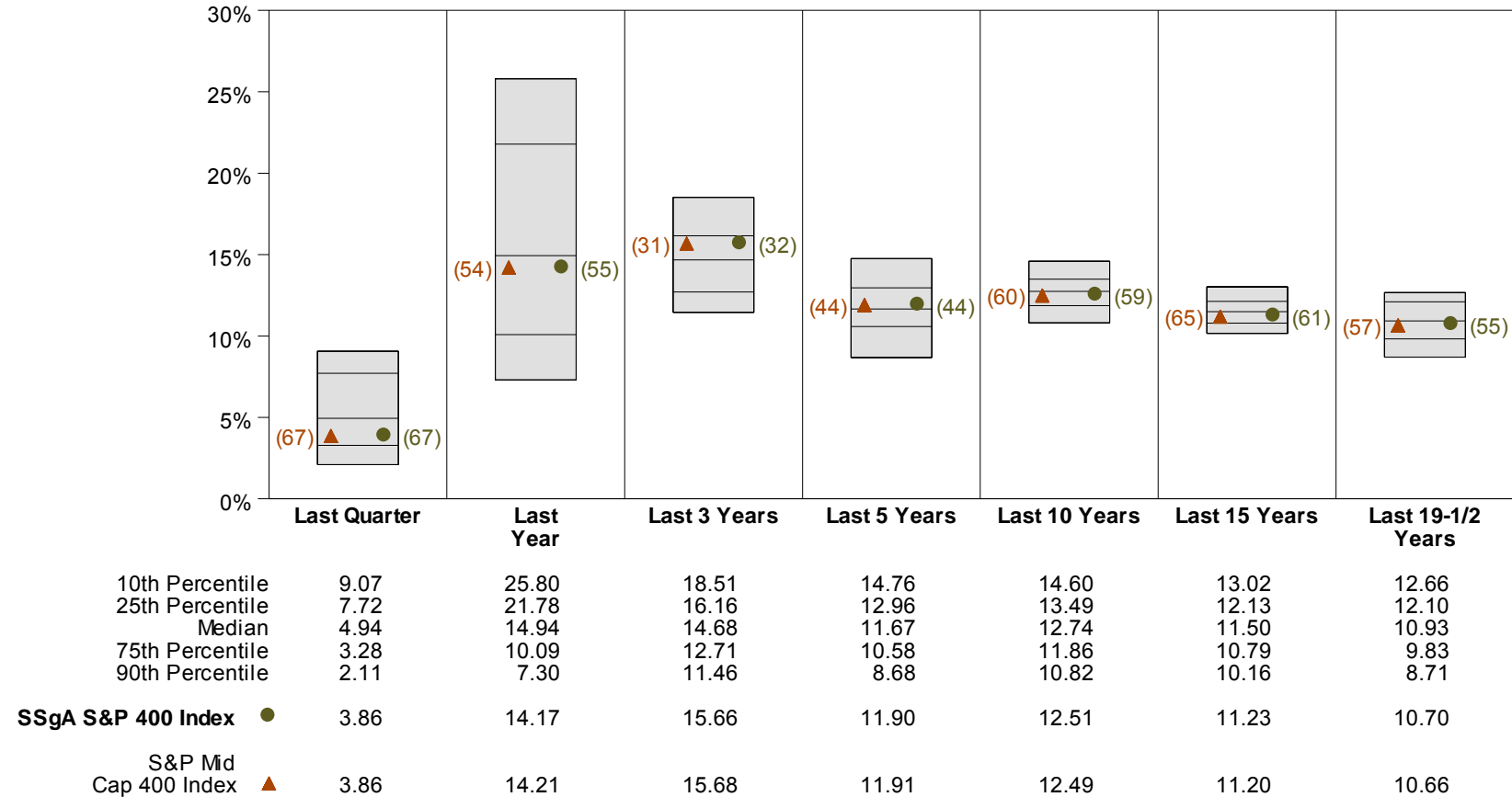
Performance vs Callan Small Cap Value (Gross)



- Ceredex underperformed the benchmark by 0.07% for the quarter and outperformed by 4.51% over the last year
- Long-term results are strong as the fund has outperformed the benchmark for most of the trailing periods shown
- Stock selection in Information Technology and Healthcare detracted from performance for the quarter

# SSgA S&P Mid Cap 400 Index

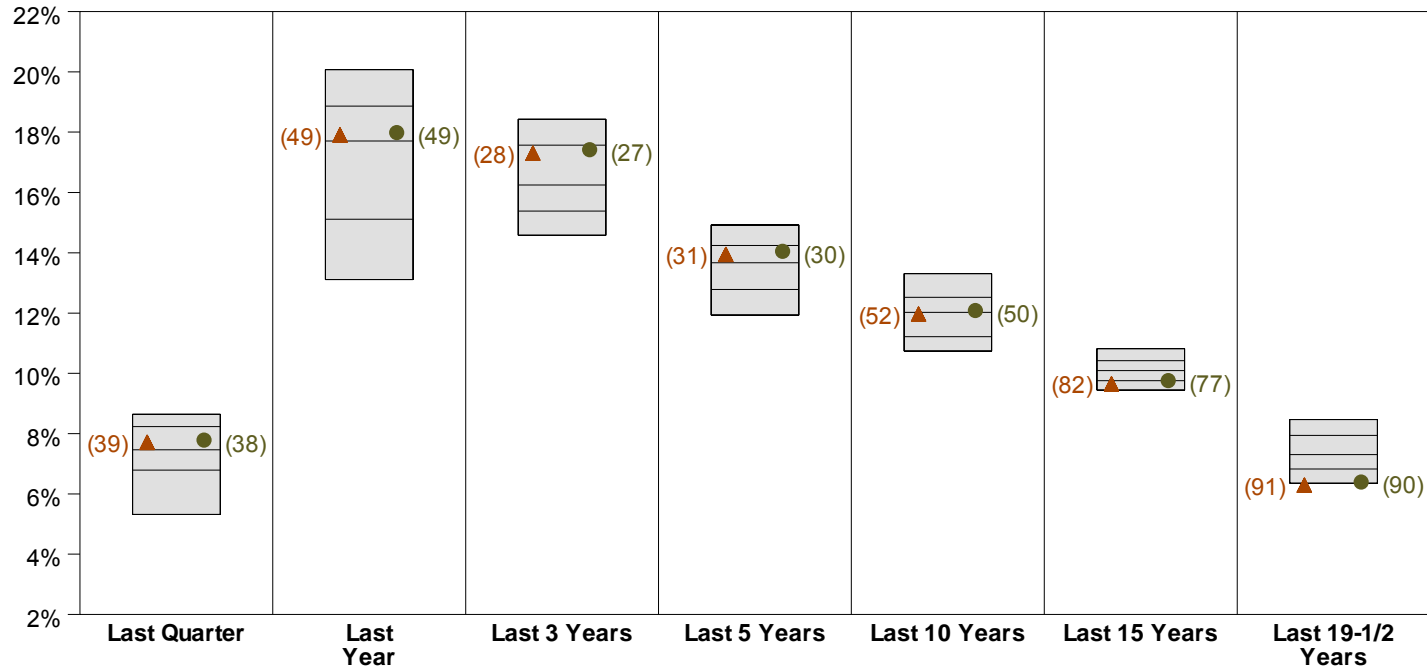
## Performance vs Callan Mid Capitalization (Gross)



- The fund continues to track the index closely at a very low fee

# SSgA S&P 500 Index

## Performance vs Callan Large Cap Core (Gross)



10th Percentile	8.64	20.07	18.43	14.92	13.31	10.82	8.46
25th Percentile	8.24	18.86	17.57	14.24	12.52	10.42	7.94
Median	7.46	17.70	16.25	13.67	12.02	10.09	7.31
75th Percentile	6.79	15.11	15.38	12.78	11.21	9.76	6.83
90th Percentile	5.32	13.11	14.58	11.93	10.74	9.44	6.35
<b>SSgA S&amp;P 500 Index</b> ●	7.73	17.93	17.36	13.99	12.03	9.70	6.34
S&P 500 Index ▲	7.71	17.91	17.31	13.95	11.97	9.65	6.29

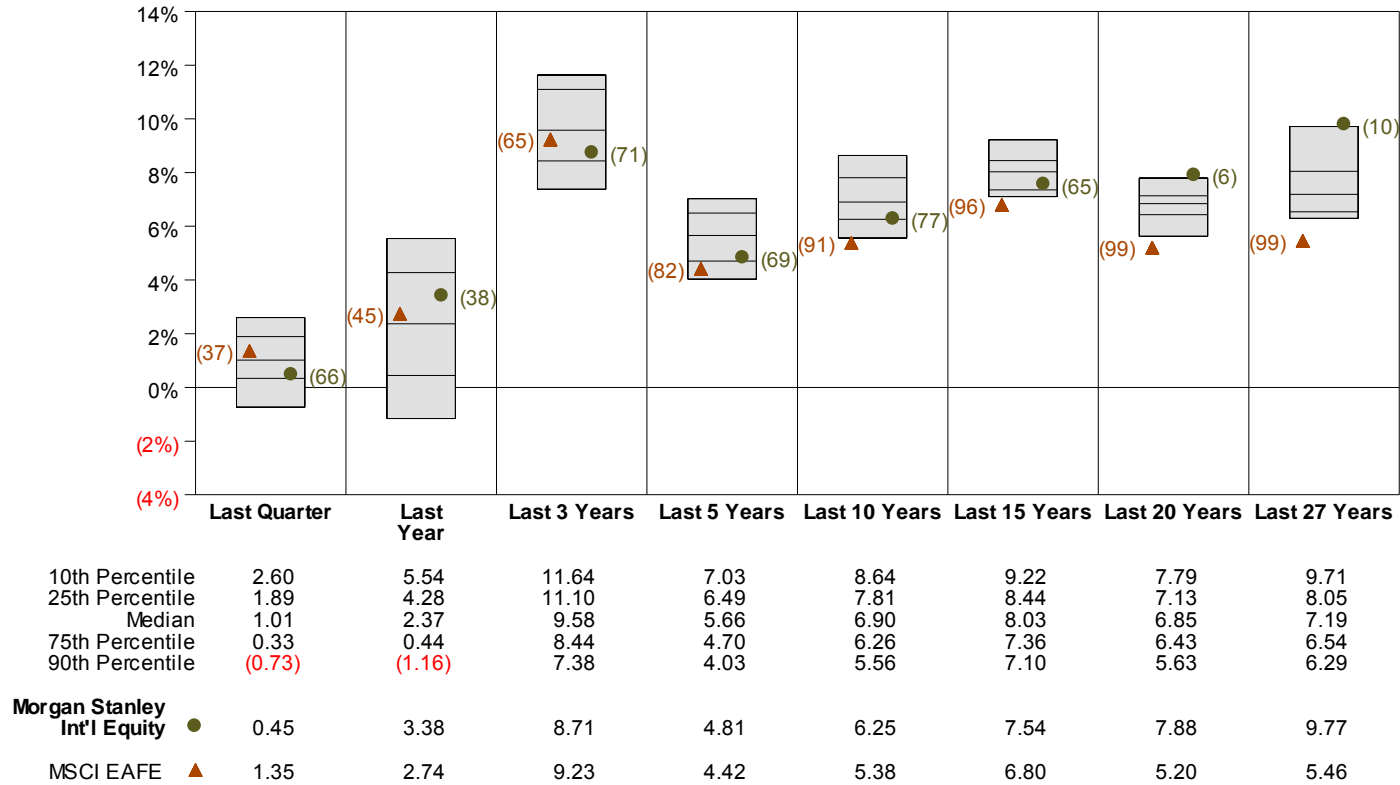
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## International Equity Performance

# Morgan Stanley Developed International Equity

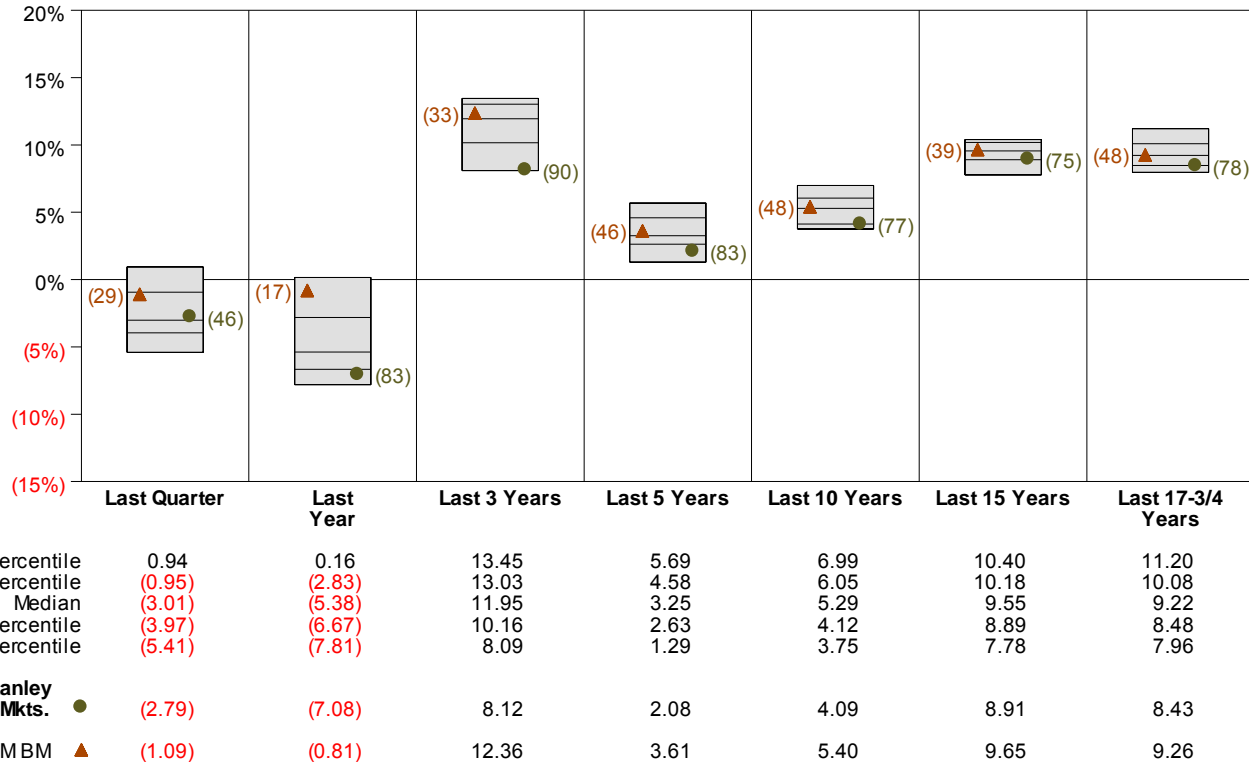
Performance vs Callan Non-US Developed Core Equity (Gross)



- The fund underperformed by 0.90% for the quarter and outperformed for the year by 0.65%
- Stock selection in Healthcare, Materials and Consumer Staples detracted from performance for the quarter

# Morgan Stanley Emerging Markets Equity

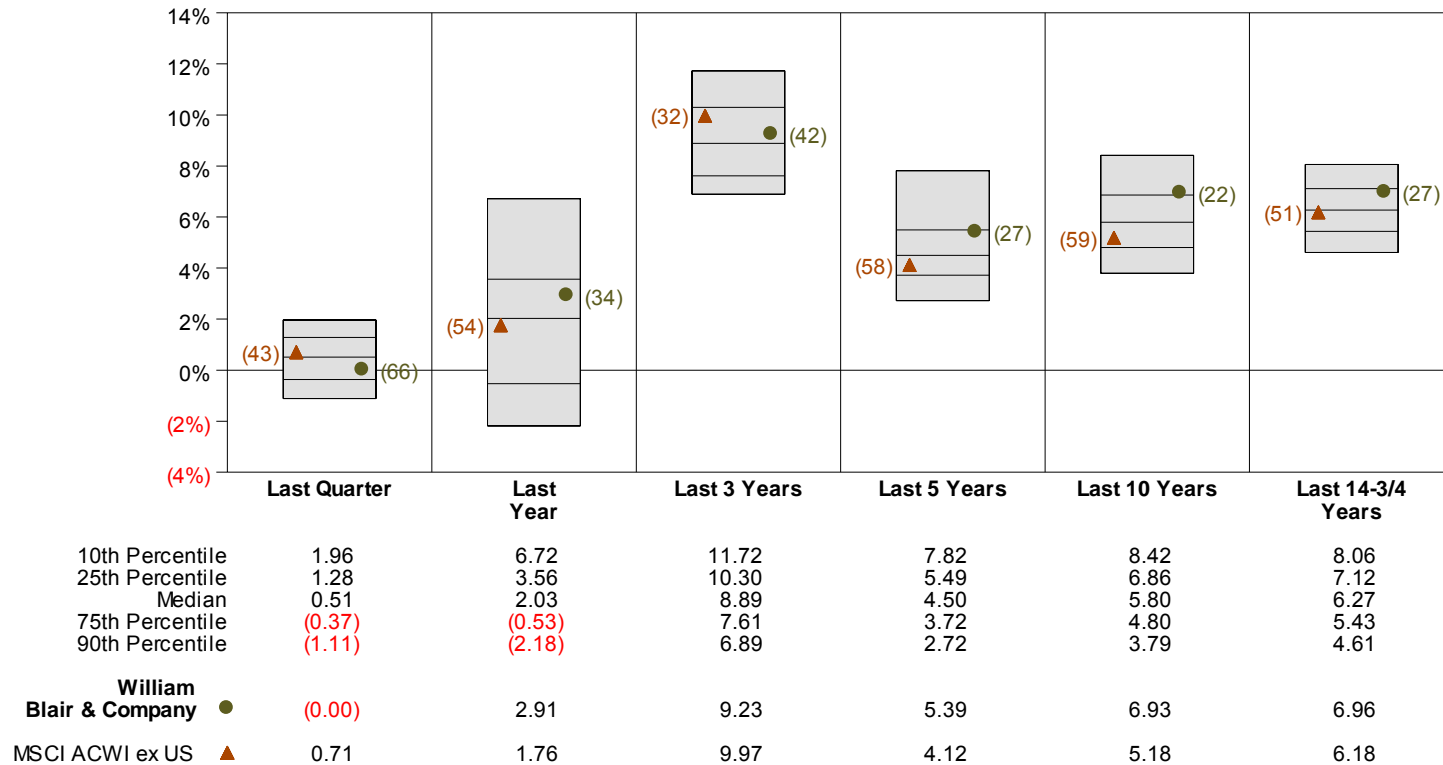
Performance vs Callan Emerging Markets Equity Mut Funds (Institutional Net)



- The fund underperformed the index by 1.70% for the quarter and underperformed by 6.27% over the last year
- The primary detractor was stock selection in India

# William Blair International Growth Equity

Performance vs Callan Non US Equity Mutual Funds (Institutional Net)



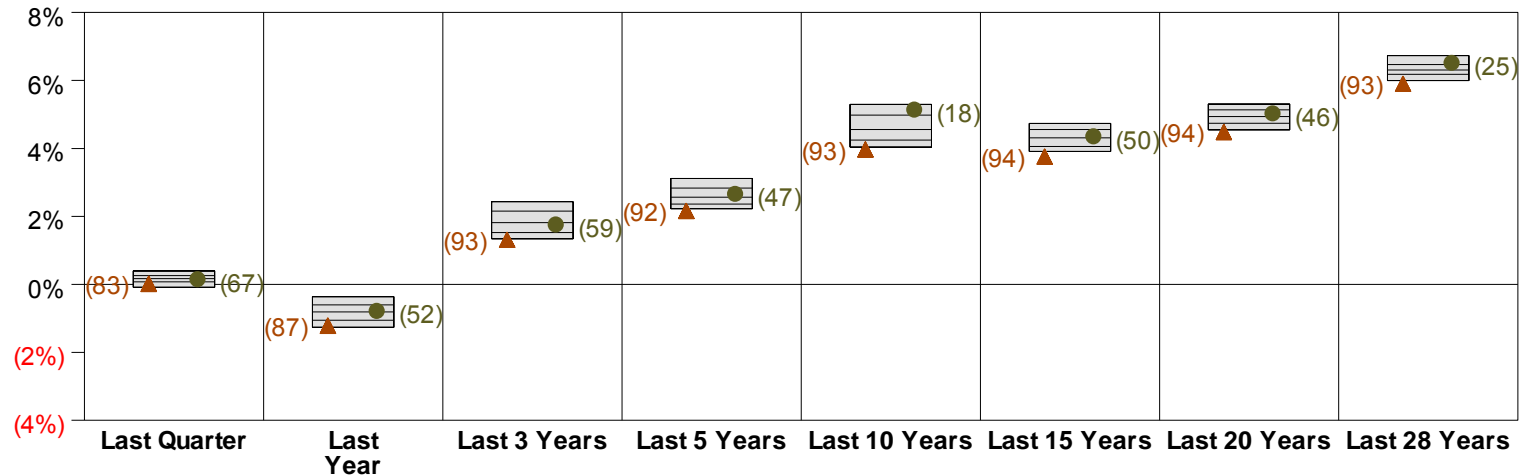
- The fund underperformed by 0.71% for the quarter and outperformed by 1.15% over the last year
- Long-term performance remains strong, as the fund has outperformed for most of the time periods presented
- Stock selection within the Consumer Staples sector was a key detractor for the quarter



Fixed Income

# Richmond Capital Core Fixed Income

## Performance vs Callan Core Bond Fixed Income (Gross)



10th Percentile	0.40	(0.37)	2.43	3.12	5.30	4.74	5.31	6.73	
25th Percentile	0.26	(0.60)	2.16	2.83	4.98	4.55	5.14	6.46	
Median	0.17	(0.81)	1.81	2.56	4.56	4.31	4.94	6.31	
75th Percentile	0.08	(1.06)	1.52	2.36	4.25	4.06	4.74	6.18	
90th Percentile	(0.09)	(1.26)	1.34	2.23	4.04	3.91	4.54	6.00	
<b>Richmond Capital Management</b>	●	0.10	(0.83)	1.70	2.60	5.08	4.30	4.97	6.47
<b>Blended Benchmark*</b>	▲	0.02	(1.22)	1.31	2.16	3.97	3.76	4.48	5.90

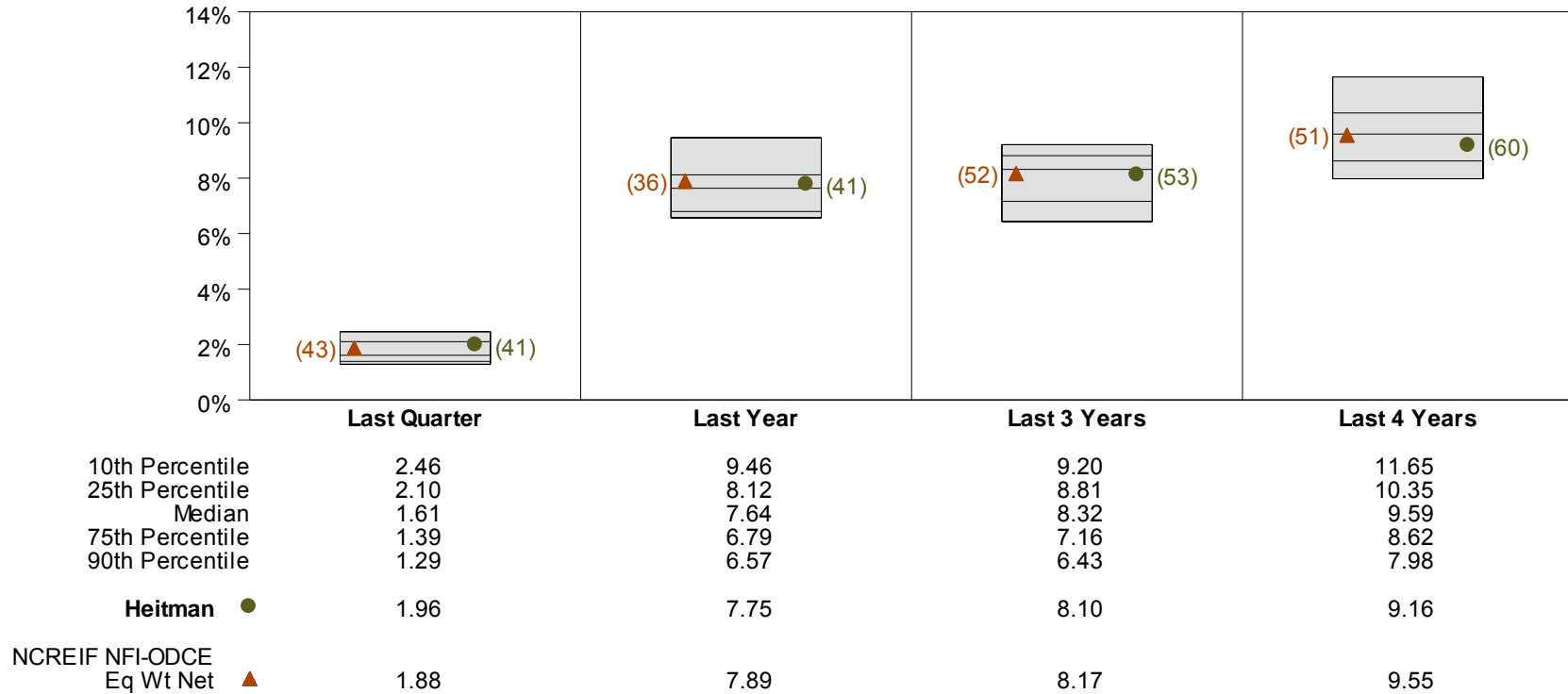
- Richmond outperformed for the quarter by 0.08% and outperformed over the year by 0.38%
- Long-term performance remains strong. The fund has outperformed by 1.11% over the last 10 years



Real Estate

# Heitman America Real Estate Trust

## Performance vs Callan Open End Core Cmmingled Real Est (Net)



- Fourth full year of performance for Heitman. The fund underperformed the index by 0.14% over the last year
- Property appreciation for the quarter was driven primarily by the Fund’s industrial and office investments

# Investment Manager Objectives

Manager	Objective	Comments
<b>Total Fund</b>	CPI + 5% over long term.	Met.
<b>Richmond</b>	Outperform BC Aggregate over rolling 3-year periods by 0.50%.	Not Met.
	Outperform the median fixed income manager over rolling 3-year periods.	Not Met.
<b>Morgan Stanley Developed</b>	Outperform the MSCI EAFE over rolling 3-year periods by 0.50%.	Not Met.
	Outperform the median international equity manager over rolling 3-year periods.	Not Met.
<b>Morgan Stanley Emerging</b>	Outperform the MSCI Emerging Markets Index over rolling 3-year periods by 1.00%.	Not Met.
	Outperform the median emerging markets equity manager over rolling 3-year periods.	Not Met.
<b>William Blair</b>	Outperform the MSCI ACWI ex-US Index over rolling 3-year periods.	Not Met.
	Outperform the median international equity manager over rolling 3-year periods.	Met.
<b>Ceredex</b>	Outperform the Russell 2000 Value Index over time.	Met.
<b>Emerald</b>	Outperform the Russell 2000 Growth Index over time.	Met.
<b>SSgA S&amp;P MidCap 400 Index</b>	Replicate the return of the S&P MidCap 400 Index.	Met.
<b>SSgA S&amp;P 500 Index</b>	Replicate the return of the S&P 500 Index.	Met.
<b>Heitman (HART)</b>	Outperform the NFI-ODCE Index by 1% or more over rolling 5-year periods	N/A