One of the early signs of springtime in Salem are the cherry blossoms at Capitol Mall State Park.

INVESTOR EDUCATION

Buoyed by strong markets, Treasury-managed Public Employees Retirement Fund posted a 15.4% return and reached a new asset value record

The long-term performance and sustainability of the Oregon investment portfolio matters to every Oregonian. That’s why Treasury is focused on building and managing portfolios that achieve positive results over decades and across market cycles.

We are not day-traders and we don’t try to time markets. Under the policies set by the Oregon Investment Council, the Oregon Public Employees Retirement Fund is much more a “buy and hold” investor.

That said, and as much as anyone else, we like to see good performance in any single year. From that lens, 2017 was an exceptionally good year for the portfolios under Treasury management.

Buoyed by a banner year in both domestic and overseas stock markets, the pension fund posted a 15.4 percent gain and reached a record high year-end balance in December.

The globally-diversified trust fund closed 2017 with a value of $77.9 billion. That sum includes the “variable account” that is no longer open to new investments.

Historically, more than 73 cents of every dollar in benefits comes from investment returns, which means positive investment performance lowers the pressure on taxpayers and other sources.

Just as important as the strong returns in 2017 -- which are largely a reflection of the broader financial markets in which we invest -- is the fact that we are in the midst of increasing our capacity at Treasury, which will reduce costs, and lessen our reliance on expensive Wall Street consultants. Every dollar we can save on fees helps make the fund more stable over time.

The performance of the overall pension fund does not mirror the stock markets exactly, however, because it is diversified -- or split up -- into different kinds of investments in order to better manage risk and volatility. Oregon also invests in bonds, privately-held companies, real estate, commodities and timberland. In 2017, the fund realized positive returns across all these and other asset classes.

As of Dec. 31, the pension fund realized a 6.0 percent average annual return for the past 10 years, a decade that includes the severe bear market of 2008-09.

As always, thanks for all you do, for Oregon.
The Oregon Public Employees Retirement Fund (OPERF) is the trust fund that belongs to beneficiaries of Oregon’s public employee retirement system, including teachers, public safety workers, and other state and local government employees. By law, OPERF assets must be invested with the goal of maximizing investment returns on a risk-adjusted basis. The Oregon Investment Council (OIC) sets investment policy and oversees overall fund performance, while Oregon State Treasury investment staff is responsible for all daily fund management activities. To increase the likelihood of successful, sustainable investment performance, OPERF capital is diversified across a wide array of asset classes, markets, and investment strategies including public company stocks, real estate, bonds, private equity, and alternatives like timberland and agriculture.

Depending on initial hire date, PERS-covered workers are impacted differently by OPERF performance. “Tier 1” workers (hired before 1996) have some investment guarantees no matter what happens in financial markets, while most other PERS members earn “realized” or actual returns. Annual OPERF performance impacts the PERS system’s “unfunded liability,” an amount equal to the difference between the present value of OPERF’s assets and the present value of all projected benefit payment obligations.

Q&A—Interest rates are rising. How will that impact investing?

Q: Interest rates are rising. How does that impact investments in the pension fund?  
A: Interest rates most often rise for one or both of two primary reasons: a) accelerating economic growth that raises the demand for credit which in turn produces upward pressure on interest rates; and/or b) inflationary trends that produce upward interest rate pressure in order to offset the erosion of money’s “store of value” function. Accelerating economic growth is a good or healthy reason for interest rate increases, whereas rate increases triggered by inflation are often symptomatic of economic instability. Interest rates often rise in response to rapid economic growth (good) and then continue to rise once inflationary pressures take hold (not good).

Economic growth in the U.S. has accelerated recently due to the stimulative effects of last year’s tax cuts and recent regulatory reforms. So far, these policies have produced advances in economic growth, employment and companies’ capital expenditures. In other words, so far, so good. But most economic cycles end when a period of sustained economic expansion eventually sows inflationary seeds. When those seeds germinate, the Federal Reserve usually steps in with more rate increases to moderate economic activity and tame inflation before it takes root.

As long as the pace of economic growth, and more specifically, corporate earnings, exceeds that of rate increases, financial markets, and stocks in particular, should continue to appreciate. However, once the Fed intervenes more vigorously and the pace of rate increases exceeds growth in economic activity and corporate profits, financial markets usually suffer. We are not at the juncture today, but as the unemployment rate approaches record lows, the odds of incipient inflation and more aggressive Fed action are increasing.

Q: Is the pension fund invested in “cryptocurrency” such as Bitcoin? Why?  
A: No. While exciting as an investment and the most visible expression of blockchain technology, Bitcoin today does not meet several institutional investment standards, notably liquidity and counter-party risk.

Q: Is the pension fund public money?  
A: No. OPERF is a trust fund and by law must be invested for the sole and exclusive benefit of its constituent owners. OPERF assets also cannot legally be invested or diverted for any political purpose that might otherwise impair the fund’s investment productivity and purpose.
THREE THINGS TO KNOW ABOUT FIXED INCOME INVESTING

As part of a balanced strategy, Treasury invests in bonds.

1. Bonds are loans. An investor like the Oregon Public Employees Retirement Fund (OPERF) lends money to a bond issuer. Bond issuers can be government entities like the U.S. Government or companies. Bond investors are then repaid over time -- with interest. These bonds are part of our “fixed income” portfolio.

2. We choose bonds based on careful research. Bonds have grades, which indicate risk level and help determine the interest rate investors receive. The risk and return analyses on all potential bond investments are part of our fiduciary imperative to maximize risk-adjusted returns.

3. As of Dec. 31, 2017, OPERF had a total of $16 billion in fixed income investments. The majority of those bonds are government issued. Of the total bonds in the portfolio, 62.4% are rated AAA, the highest possible grade.
Beyond the balance sheet: Oregon Treasury interfaces with companies and regulators to promote sustainable returns

When it comes to measuring corporate performance, you can quantify short-term results with math. Financial statements spell out profit and loss, expense ratios, supply chain statistics and labor and benefit costs, to name just a handful of factors.

All of this information is valuable for investors including the Oregon Public Employees Retirement Fund, and also for those who rely on it.

Oregon’s trust fund investments are managed on a long-term horizon of 25 years or more. Against that backdrop, today’s performance is important — but so is the sustainability of that performance, which will shape returns and fund values years from now.

A significant share of Oregon’s holdings are in commingled funds that include publicly traded companies, broadly diversified across industry sector and market geography. As “buy and hold” owners, investors like Oregon can take a hands-off approach. Alternatively, we can engage in ways that shape the direction of both the companies whose shares we own and the regulatory landscape in which those companies do business.

Treasury, at the direction of the Oregon Investment Council, has settled upon the latter, more activist approach.

Fair and transparent market structures are essential for the long-term success of all investors, so we engage regularly with policymakers and regulators including the U.S. Securities and Exchange Commission.

In addition, shareholder value is most often maximized when company executives align their decision-making and compensation programs with long-term corporate performance metrics. Good governance and appropriate risk management practices affect public companies in equity and fixed income portfolios, and also apply to the privately-held enterprises we invest in through our private equity and other alternative investment portfolios.

Promoting sustainability often means looking beyond the balance sheet — and considering factors that have historically been harder to quantify, like environmental, social and governance (ESG) risks. These factors include: Who sits on a board of directors and what expertise do they bring, how and to what extent is executive compensation tied to performance, are workers and their safety prioritized, and have companies prepared for climate-related risks and opportunities.

In addition to acting alone, Oregon frequently takes action in coalitions of like-minded shareholders, which increases the leverage to spur desired corporate or government action. As a last resort, if companies and executives act in ways that impair long term value, Oregon can file securities lawsuits.

These actions are consistent with Treasury’s fiduciary obligation. Oregon trust funds must be invested for the “sole and exclusive” long-term benefit of fund beneficiaries. Shareholders have a voice in management decisions. Non-shareholders do not.

LEARN MORE
Treasury is analyzing Environmental, Social and Governance (ESG) risks and engaging as a responsible shareholder to seek long term sustainability and performance. See the Treasurer’s Stewardship report.

SHAREDHOLDER ACTION
Learn more about key shareholder votes at #OregonProxy on Twitter.

WHO TO CONTACT

I have questions about my PERS benefits or retirement options.
Public Employees Retirement System
www.Oregon.gov/PERS
888-320-7377

I have questions about the Oregon Investment Council.
Oregon State Treasury Communications and Stakeholder Relations
www.Oregon.gov/Treasury
503-378-4000

I have questions about my PERS account balance.
Public Employees Retirement System
www.Oregon.gov/PERS
888-320-7377

I have questions about the IAP and my personal account balance.
Public Employees Retirement System
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888-320-7377

I would like to communicate with the State Treasurer.
Office of the State Treasurer
www.Oregon.gov/Treasury
Oregon.Treasurer@ost.state.or.us
503-378-4329

I would like to know more about the Oregon Savings Growth Plan.
osgp cstsvc-PERS@state.or.us
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I have questions or story ideas for Invested For You.
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