STRS report for OSURA Board, January 2021. Jerry Newsom.

**STRS report**

The financial reports to the STRS Board in December included their investment returns (as of Sept. 30, 2020), broken down by asset class, as follows:

Asset Class 5 year 15 year 25 year

Domestic equities 14.1% 9.05% 8.77%

International equities 6.72% 5.36% 6.05%

Fixed income 4.74% 5.08% 6.01%

Real estate 6.52% 9.04% 10.48%

Alternative investments 8.06% 9.80% 7.75%

The Domestic equities class includes a very wide range of options. For instance, over the first 9 months of CY 2020, the Russell 1000 Growth stocks increase by 24.3%, while the Russell 1000 Value stocks **decreased** by 11.6%, a huge 35.9% difference. If only we’d known this before the year began... Results also varied widely by type of business. Consumer Discretionary stocks in the S&P 500 for the third quarter of 2020 were up 15.1%, while Energy stocks were down 19.7%, for example.

The investment return depends on two very different considerations: what fraction of the assets should be invested in the different classes (set by the STRS Board) and within each asset class which stocks or bonds or buildings or alternatives to buy (selected by the investment staff). This is illustrated by returns for the July-September period, where the Board selected the first column and the staff efforts resulted in the second column. The last column lists the ten-year expected rate of return, as estimated by consultants. Note that the return assumed by the Board, 7.45%, is not attainable with the expected returns listed.

Asset class Weight Asset Class Return Weight x Return Expected Return

Domestic equities 28% 9.21% 2.58 7.35%

International equities 23% 4.56% 1.05 7.55%

Fixed income 21% 0.82% 0.17 3.00%

Real estate 10% 0.84% 0.08 6.00%

Alternatives 17% 9.04% 1.54 7.09%

Liquidity reserves 1% 0.04% 0.00 2.25%

Total 5.44% 6.84%

Occasionally speakers at the public input session (back when face-to-face meetings existed) noted that STRS would have had much higher total returns in recent years if they invested entirely in a stock index fund – excellent advice as long as the market goes up but disastrous when the market tanks.

The total investment return for October was -1.1% (attributed to uncertainty over the election, the pandemic, and European markets). However, November was strong, returning +7.75%, the best monthly return in over 20 years. Domestic and international equities returned nearly 13% for November. For the first 5 months of FY 2021, the total fund returned +12.4%, and investments increased in FY 2021 so far by $7.6 billion to $84.7 billion. To meet the “target” weight in each asset class, the rise in equities required STRS to sell about $2 billion worth of equities in November. This “rebalancing” prevents their investments from having a heavier exposure to the inherent risk of the stock market, but it also means moving funds out of sectors that have historically done well into areas that usually have smaller returns.

**Legislative news**

Biden is expected to propose many changes to retirement plans. Some of the changes, if enacted, would have a major effect on those nearing retirement or already retired. Considering how many Americans reach retirement age with no or trivial retirement savings, changes are needed. Among the proposals are ones to lower the age for Medicare eligibility to 60, provide a $5,000 tax credit to caregivers looking after spouses or parents, require workers to be automatically enrolled in 401(k)-style plans unless they opt out, increase the cap on earnings subject to the payroll tax, give a flat-tax credit for contributions to 401(k)-style plans (that helps lower-income people and hurts higher earners), and “shore up public and private pensions and help to ensure workers keep their earned benefits by passing legislation that provides a path towards helping distressed plans.” Of course, proposing plans and having them enacted into law are not the same, and the Senate election in Georgia may have a lot to do with how the plans fare; most observers seem to expect tough sledding. Getting 60 Senate votes to overcome a filibuster on a proposal to end the $142,800 cap on earnings taxed to support Social Security, for example, would be a real stretch. There was bipartisan support for ending many surprise medical bills, included in the federal budget passed by Congress on 21 December, but it doesn’t take effect until 2022.