

# Deferred Compensation Plan

## BOARD REPORT 14-53

Date: December 5, 2014

To: Board of Deferred Compensation Administration

From: Staff

Subject: Investment Committee Recommendations for the Underlying Providers of the Deferred Compensation Plan International Fund

*Board of Deferred  
Compensation Administration  
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### Recommendation:

That the Board of Deferred Compensation Administration approve recommendations of the Investments Committee to select the following actively managed funds as components of the Deferred Compensation Plan International Fund:

- a) **MFS Institutional International Equity Fund** as the Active Developed Markets component of the Deferred Compensation Plan International Fund;
- b) **DFA Emerging Markets Core Equity Portfolio Institutional** as the Active Emerging Markets component of the Deferred Compensation Plan International Fund; and
- c) **Brandes International Small Cap Equity Fund I** as the Active Small-Cap component of the Deferred Compensation Plan International Fund.

### Discussion:

On February 18, 2014, in accordance with provisions of its Investment Policy Statement (IPS), the Board of Deferred Compensation Administration approved the use of mutual fund search processes to search for actively managed funds for the Deferred Compensation Plan's Bond, Small-Cap, Mid-Cap and International core investment menu offerings. On March 18, 2014, the Board adopted specific search criteria for each of these investment mandates.

The Board's investment consultant, Mercer Investment Consulting ("Mercer") then initiated search processes in accordance with the IPS and the adopted search criteria. The Investments Committee has been reviewing the results generated by Mercer's analysis.

On October 22, 2014 and October 30, 2014, the Investments Committee met to review the search results for the Active International Developed Markets, International Emerging Markets, and International Small-Cap fund categories. The Committee established a list of finalists for further review within each category.

On December 5, 2014, the Investments Committee reviewed a subsequent report from Mercer providing more detailed findings regarding the finalists. The Committee then finalized provider recommendations within each category to recommend to the full Board.

This report and the attached report contain the recommendations of the Committee and the finalist data that was reviewed by the Committee in developing its recommendation.

The Plan currently offers two standalone international investment options: the actively managed Fidelity Diversified International Fund and passively managed DWS EAFE Equity Index Fund. Upon selection of the active international fund providers, the Plan will establish a **DCP International Fund** which will be, in accordance with the IPS, constituted as follows: 65% developed markets, 17.5% emerging markets, and 17.5% international small-cap.

Based on June 30, 2014 values, the estimated mandate size for the developed markets category is \$214 million and \$58 million each for the emerging markets and international small-cap active categories (these numbers include assets invested in the risk-based profile funds).

The Investments Committee has completed its review for both categories and developed the following recommendations for Board approval.

#### **a. ACTIVE INTERNATIONAL DEVELOPED MARKETS**

Sixteen funds were initially identified as having met all of the essential criteria adopted by the Board. The Investments Committee identified the following managers and funds as finalists for additional review:

1. Hartford International Opportunities HLS Fund IA (HIAOX)
2. MFS Institutional International Equity Fund (MIEIX)

Upon review of a subsequent follow-up report from Mercer, and discussion of the merits of each option, the Investments Committee is recommending that the MFS Institutional International Equity Fund be selected as the new Active Developed Markets component of the DCP International Fund.

#### **b. ACTIVE INTERNATIONAL EMERGING MARKETS**

Fifteen funds were initially identified as having met all of the essential criteria adopted by the Board. The Investments Committee identified the following managers and funds as finalists for additional review:

1. DFA Emerging Markets Core Equity Portfolio Institutional (DFCEX)
2. Harding Loevner Institutional Emerging Markets Portfolio I (HLMEX)

Upon review of the subsequent report from Mercer, and discussion of the merits of each option, the Investments Committee is recommending that the DFA Emerging Markets Core Equity Portfolio Institutional be selected as the new Active Emerging Markets component of the DCP International Fund.

### c. ACTIVE INTERNATIONAL SMALL-CAP

Eleven funds were initially identified as having met all of the essential criteria adopted by the Board. The Investments Committee identified the following managers and funds as finalists for additional review:

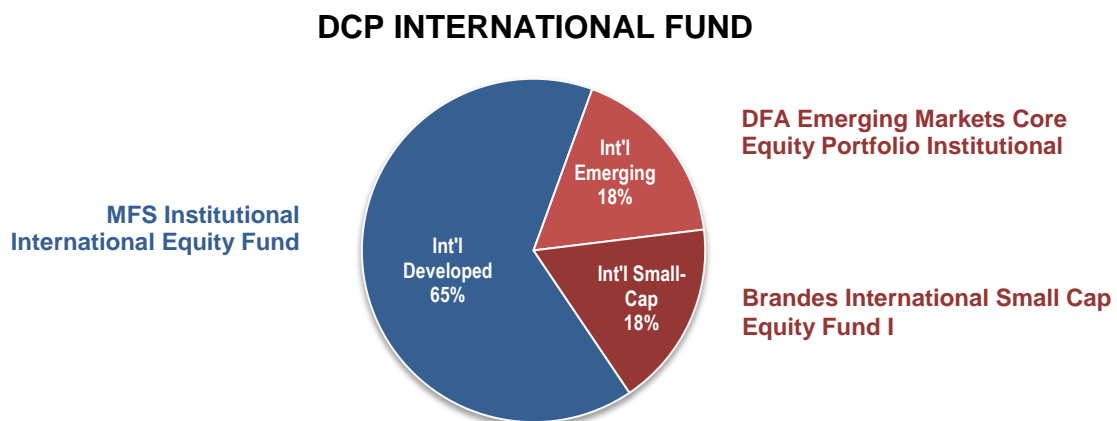
1. Brandes International Small Cap Equity Fund I (BISMX)
2. DFA International Small Company Portfolio Inst (DFISX)

Upon review of the subsequent report from Mercer, and discussion of the merits of each option, the Investments Committee is recommending that the Brandes International Small Cap Equity Fund I be selected as the new active international small-cap component of the DCP International Fund.

The MFS Institutional International Equity Fund, DFA Emerging Markets Core Equity Portfolio Institutional, and Brandes International Small Cap Equity Fund I are being recommended based on their qualifications within various review areas including long-term performance (including considerations to value added above benchmark), management team depth, personnel stability, portfolio construction, competitive fees, performance in different market environments, risk-adjusted returns, and other criteria reviewed by the Committee and detailed in the attached consultant report.

The Committee further reviewed hypothetical modeling of different combinations of the finalist funds together, as all three components would become underlying providers of the DCP International Fund. This analysis is also included in the attached report.

Should the Board approve the Committee's recommendations, the DCP International Fund would be implemented as depicted by the following chart:



*\*Subject to the Board's approval.*

The estimated net expense ratio for the newly comprised DCP International Fund would be approximately **0.77%** (after a 0.03% revenue share from the Brandes fund). The consultant will be present at the Board meeting to review additional details regarding these funds. Staff recommends that the Board adopt the funds recommended by the Investments Committee.

Submitted by: \_\_\_\_\_  
Paul Makowski

Approved by: \_\_\_\_\_  
Steven Montagna