

What’s going on in the marketplace?

The quarter ending September 30th witnessed rising global equity markets driven almost entirely by the U.S. which gained over 7.0% (Russell 3000), while Non-U.S. markets gained a mere 0.4% per the MSCI ACWI Ex-US Index. Within the U.S., the earnings story remained intact, with companies continuing capital spending and hiring additional labor in response to the recent tax reform. Non-U.S. markets were subdued by concerns regarding the potential escalation of a trade war between the U.S. and China, and its influence across the emerging markets as a China slowdown appears more evident. Increased risk has led to multiple compression, which could also be attributable to a lack of performance outside of the U.S.

U.S. Equities

U.S. equity markets experienced modest gains during the month; the Russell 3000 Index added 17 basis points (bps). The market was driven by large caps, which returned 0.6%. Mid-caps and small caps were weak during the period (S&P 400: -1.1%, R2000: -2.4%). Growth outpaced value by 33 basis points as evidenced by the Russell 3000 style indices (R3000G 0.3%, R3000V 0.0%).

The KRS U.S. Equity portfolio underperformed the Russell 3000 by 38 bps during the month (-0.2% vs 0.2%). The portfolio’s relative performance was driven by both stock selection and allocation. From a stock selection perspective, the portfolio’s all cap mandates trailed their respective indices. From an allocation perspective, the value tilt and smaller cap positioning was a headwind during the period.

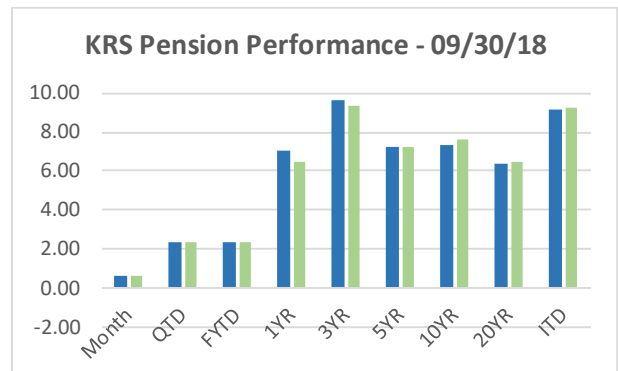
Non-U.S. Equities

Non-U.S. equities slightly outpaced the U.S. markets during the period, adding 22 bps. Developed markets outperformed their emerging market counterparts. While growth outperformed value in developed international large cap names, value outpaced growth in both the developed international small cap and emerging markets spaces.

The KRS Non-U.S. Equity portfolio performed in line with its benchmark, returning 0.2% during the month. Stock selection was mixed as two of the four active large cap managers and the portfolio’s small cap mandate outperformed their associated indices. Allocation decisions had little impact on relative performance.

Fixed Income

Fixed income market segments were positive in terms of performance during the month. The corporate high yield market rose three-quarters of a point, the core space as defined by the U.S. Aggregate gained 64 bps, intermediate credit was up 0.6%, and leveraged loans were up 40 bps during the period.



The specialty credit portion of the KRS portfolio returned 58 bps on the month, while the core fixed income piece of the portfolio fell -0.3%. Within the specialty credit bucket, relative outperformance was provided by strong selection within some of the lending, leveraged loan, and global bond mandates. Within the core portion of the portfolio, the intermediate corporate credit and aggregate investments held up slightly better than the market.

Alternative Assets

The diversifying strategy group was relatively flat during the month, gaining 5 bps. The Real Estate and Opportunistic portion of the portfolio gained 1.3% and 0.8%, respectively. The Absolute Return and Real Return portions of the portfolio declined

during the period, posting a return of -0.1% and -0.4%, respectively. The Private Equity portion of the portfolio provided a strong 5.3% return for the month.

Cash

The cash portfolio basically performed inline during the month (0.15% vs 0.17%). The cash allocation finished the period slightly above target due to transitioning assets while continuing to move toward the newly approved asset allocation.

NOTES:

- 1) Returns displayed are "net". For the purposes of this report, total fund return information is net of fees and expenses, with audited data beginning in July 2011. At the manager level returns are net of fees beginning with July 2011, and gross of fees for prior data.
- 2) Individual plan allocation and performance (pg.4).
- 3) Prior to January 1, 2014, the inception date for the Private Equity asset class was stated as 10/1/1990 for Pension Fund and 6/1/2001 for Insurance Fund. Prior to 07/01/02, the characteristics of the allocation, and the benchmark itself, were more closely aligned with Real Estate. As such, it is not appropriate to report this portion of the return stream within the Private Equity allocation, whose true inception date has been determined to be 07/01/02 based on funding the Systems' first private equity mandate. The portion of the original return streams that are no longer reported within the Private Equity allocation (Pension from 10/1/90 to 06/30/02; Insurance 06/01/01 to 06/30/02) are reported within the Fund Level performance figures.
- 4)

Private Equity Composite (Pension) Inception (07/01/02) to 06/30/11 60.00% S&P 1500 Composite Index 40.00% Barclays US Corporate High Yield Index 07/01/11 to 12/31/15 100.00% Russell 3000 Index + 4% (Qtr Lag) 01/01/16 to Present 100.00% Russell 3000 Index + 3% (Qtr Lag)	Private Equity Composite (Insurance) Inception (07/01/02) to 06/30/11 80.00% S&P 1500 Composite Index 20.00% Barclays US Corporate High Yield Index 07/01/11 to 12/31/15 100.00% Russell 3000 Index + 4% (Qtr Lag) 01/01/16 to Present 100.00% Russell 3000 Index + 3% (Qtr Lag)
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- 5) The Private Equity & Real Return Benchmarks, from one month returns up until five year returns, is equal to the performance of the associated KRS allocations. Given there is not appropriate benchmark to use for short term performance evaluation, this will allow greater focus on longer term returns, which is more appropriate given the long term nature of these investments.

<u>Pension Benchmark Composite 01/01/16 to 08/31/17</u> US Equity: Russell 3000 (25.6%) Non US Equity: MSCI AXCI Ex-US IMI (25.2%) Global Fixed Income: Barclays Universal Index (6.8%) Credit Fixed Income: Barclays US High Yield (7.2%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return: Allocation Specific (8.0%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (10.0%) Cash: Cit Grp 3-mos Treasury Bill (2.2%) <u>Pension Benchmark Composite 09/01/17 to 05/31/18 - Transition Period w/Sliding Targets</u> US Equity: Russell 3000 (23.6%) Non US Equity: MSCI AXCI Ex-US IMI (23.2%) Global Fixed Income: Barclays Universal Index (9.0%) Credit Fixed Income: Barclays US High Yield (9.0%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return<5yrs: Actual Performance Real Return>5yrs: CPI+3% (8%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (10.0%) Cash: Cit Grp 3-mos Treasury Bill (2.2%) <u>Pension Benchmark Composite 06/01/18 to Present</u> US Equity: Russell 3000 (17.0%) Non US Equity: MSCI AXCI Ex-US IMI (21.0%) Global Fixed Income: Barclays Universal Index (13.0%) Credit Fixed Income: Barclays US High Yield (12.4%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return<5yrs: Actual Performance Real Return>5yrs: CPI+3% (10.0%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (9.4%) Cash: Cit Grp 3-mos Treasury Bill (2.2%) **Fund composite benchmark is a roll-up of individual plans, which may differ from one another.	<u>Insurance Benchmark Composite 01/01/16 to 08/31/17</u> US Equity: Russell 3000 (26.5%) Non US Equity: MSCI AXCI Ex-US IMI (26.5%) Global Fixed Income: Barclays Universal Index (6.0%) Credit Fixed Income: Barclays US High Yield (6.0%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return: Allocation Specific (8.0%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (10.0%) Cash: Cit Grp 3-mos Treasury Bill (2.0%) <u>Insurance Benchmark Composite 09/01/17 to 05/31/18 - Transition Period w/Sliding Targets</u> US Equity: Russell 3000 (24.5%) Non US Equity: MSCI AXCI Ex-US IMI (24.5%) Global Fixed Income: Barclays Universal Index (8.0%) Credit Fixed Income: Barclays US High Yield (8.0%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return<5yrs: Actual Performance Real Return>5yrs: CPI+3% (8%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (10.0%) Cash: Cit Grp 3-mos Treasury Bill (2.0%) <u>Insurance Benchmark Composite 06/01/18 to Present</u> US Equity: Russell 3000 (17.9%) Non US Equity: MSCI AXCI Ex-US IMI (21.9%) Global Fixed Income: Barclays Universal Index (13.0%) Credit Fixed Income: Barclays US High Yield (11.0%) Real Estate: NCREIF ODCE (5.0%) Absolute Return: HFRI Diversified FOF (10.0%) Real Return<5yrs: Actual Performance Real Return>5yrs: CPI+3% (10.0%) Private Equity<5Yrs: Actual Performance Private Equity>5Yrs: Russell 3000 Index+3% (9.2%) Cash: Cit Grp 3-mos Treasury Bill (2.0%)
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