

**PENSION REVIEW COMMITTEE
RECOMMENDATION
REPLACE GIBRALTAR GUARANTEED FUND WITH CORE INTERMEDIATE BOND FUND
May 3, 2018**

INTRODUCTION

The Pension Review Committee met April 10, 2018 to consider whether the Gibraltar Guaranteed Fund (Gibraltar) should be replaced with the Core Intermediate Bond Fund (CIBF) for both the 401(a) Retirement Plan and the 457(b) Deferred Compensation Program. During the meeting a conference call was conducted involving the following representatives from Prudential and Segal Marcos Advisors: Robb Craddock, Prudential Vice President of Investment Strategy; Leah Kostuck, Prudential Client Service Manager; Frank Picarelli, Segal Marcos Senior Vice President; and Christopher Hill-Junke, Segal Marcos Research Associate. A document was presented to the Committee by Prudential with a hypothetical crediting rate performance illustration showing the differences between the Gibraltar Guaranteed Fund, the Core Conservative Intermediate Bond Fund, and the Core Intermediate Bond Fund.

After reviewing the document and extended discussion with Prudential about the hypothetical crediting rate illustration, it was determined by the Committee that additional information was needed to explain how Prudential structures rates, charges, and returns for Gibraltar and CIBF. A conference call with Prudential and Segal Marcos was arranged for this purpose and conducted on April 27, 2018. Cyr and Eagan participated on the call, along with Craddock and Mike McCann from Prudential, and Picarelli from Segal Marcos. During the call an updated hypothetical crediting rate performance illustration comparing Gibraltar and CIBF was presented and discussed. This information was then presented to the Committee at a meeting on May 1, 2018. Fact sheets on Gibraltar and CIBF were also presented to the Committee at the May 1st meeting.

DISCUSSION

During the past several years the Gibraltar Guaranteed Fund has performed very well, ranking as one of the best funds in the stable value category. Gibraltar employs a strategy based on the Barclay's Capital Aggregate Fund Index, which results in holding assets for longer durations than most stable value funds. The longer durations have helped Gibraltar because interest rates have been stable. However, the bond market has now entered a period of rising interest rates, and longer durations are beginning to hurt Gibraltar returns.

Prudential has proposed replacing Gibraltar with the Core Intermediate Bond Fund. CIBF holds assets for shorter durations, averaging 4.23 years compared to Prudential's 6.02 years. This provides an advantage when interest rates are rising. Moreover, CIBF is more actively managed than Gibraltar, which

is also an advantage in a rising interest rate environment. Additionally, CIBF has a lower expense ratio than Gibraltar. During the last year CIBF returns have increased by approximately 100 bps.

However, the market value to book value ratio for Gibraltar is 95.81% as of April 20, 2018. This means that liquidation of the Gibraltar account would yield only 95.81¢ on the dollar. The market value to book value ratio is also known as the market value adjustment, or MVA. It should be noted that the MVA for Gibraltar was 96.82% on March 29, 2018, indicating the Gibraltar MVA continues to fall as interest rates are rising.

If the County decides to move from Gibraltar to CIBF, the CIBF returns will be negatively affected by the Gibraltar MVA. On the day the Gibraltar funds are transferred to CIBF the existing market value for Gibraltar would also be transferred. The Gibraltar MVA would then be amortized, thereby negatively affecting the CIBF rate during the amortization period.

On the other hand, moving from Gibraltar will minimize the effects of the declining MVA. Also, as the longer duration Gibraltar assets are replaced with shorter duration assets, the CIBF yield is expected to increase in the rising interest rate environment. In this regard, the Federal Reserve Board has indicated more interest rate increases will be implemented during the upcoming year.

After carefully reviewing the information presented, the Committee determined that the advantages of moving from Gibraltar to CIBF outweigh the disadvantages.

RECOMMENDATIONS

Based on the foregoing information and discussion the following recommendation is hereby tendered to the Lancaster County Board of Commissioners:

- 1. THE GIBRALTAR GUARANTEED FUND SHOULD BE REPLACED WITH THE CORE INTERMEDIATE BOND FUND AND ALL ASSETS TRANSFERRED ACCORDINGLY AS SOON AS POSSIBLE.**

Respectfully submitted May 3, 2018 on behalf of the Pension Review Committee.


Kerry P. Eagan
Chief Administrative Officer