

# Regions Investment Management

## Quarterly Overview

### State of Alabama Treasurer's Office

### Prepaid Affordable College Tuition (PACT) Program

As of September 30, 2019

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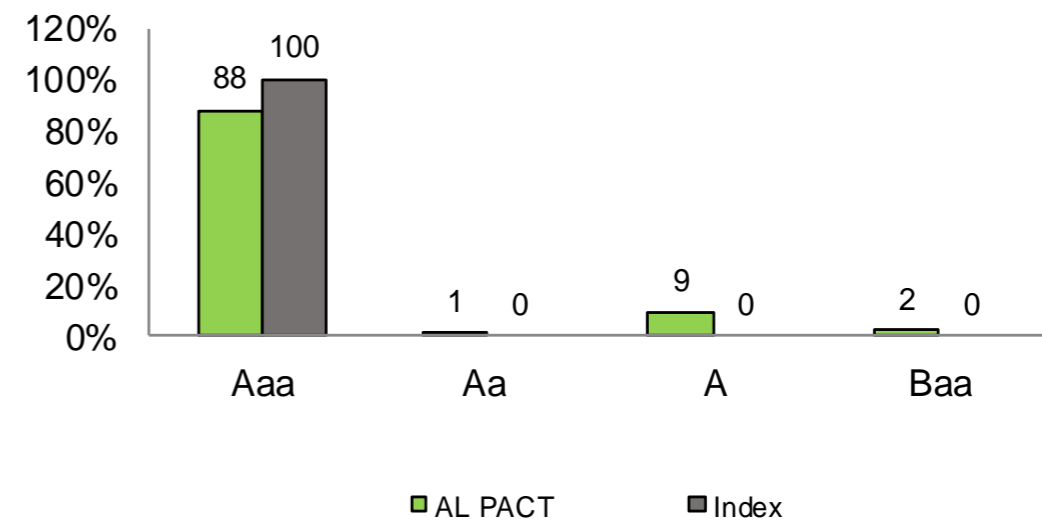
# Bond Portfolio Overview

- Characteristics
- Performance
- Manager Universe
- Allocation Detail

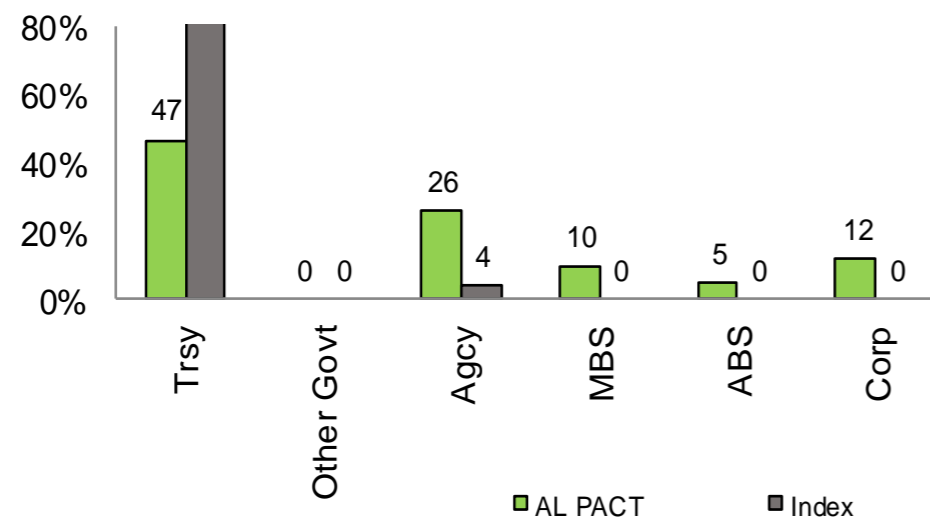
# 3Q19 Fixed Income Portfolio Characteristics vs. Index

	AL PACT	Index
Yield to Maturity	1.81%	1.69%
Effective Duration	1.94 Yrs	1.90 Yrs
Maturity	2.18 Yrs	1.96 Yrs
Average Coupon	2.13%	2.06%
Average Quality	Aa1	Aaa

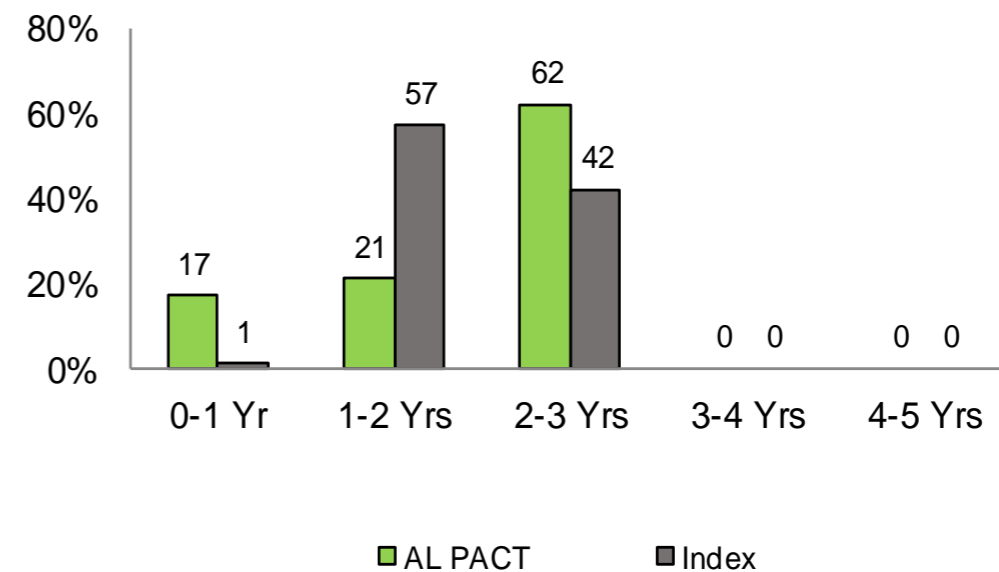
### Quality vs. Index



### Sector Distribution vs. Index



### Duration Distribution vs. Index



Source: Portfolio: Bondedge; Index: Bloomberg Barclay's 1-3 Year Govt Only

# State of Alabama Treasurer's Office - Prepaid Affordable College Tuition (PACT) Program

## Total Returns Compared with the Benchmark

As of 09/30/2019

	Qtr	YTD	1-Yr	3 Years *	Inception *
<b>AL PACT</b>	<b>0.65%</b>	<b>3.45%</b>	<b>4.44%</b>	<b>2.00%</b>	<b>2.10%</b>
1-3 YR Govt Only	0.59%	3.07%	4.42%	1.54%	1.59%
<i>Excess Return</i>	<i>0.06%</i>	<i>0.38%</i>	<i>0.02%</i>	<i>0.46%</i>	<i>0.51%</i>

1-3 YR Govt/Credit	0.69%	3.42%	4.64%	1.82%	1.90%
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Returns are shown **net of fees**;

Past performance does not guarantee future returns; \*Periods greater than one year are annualized; Inception Date as of 12/31/2015

Source: SEI & Bloomberg Barclays

Indexes: Bloomberg Barclays

# State of Alabama Treasurer's Office - Prepaid Affordable College Tuition (PACT) Program

## Allocation Detail

INVESTMENT RETURN SUMMARY - QUARTER ENDING SEPTEMBER 30, 2019					
Name	Current Quarter Total Return	Prior Quarter Market Value	Net Cashflow	Investment Return	Current Quarter Market Value *
Regions (STFI)	0.60%	\$64,766,315	\$0	\$387,295	\$65,153,610
Regions Cash (CASH)	0.51%	25,689,110	4,000,000	150,442	\$29,839,552
Regions Lockbox (CASH)	0.00%	407,091	152,210	0	\$559,301
<b>Total Portfolio</b>		<b>\$90,862,516</b>	<b>\$4,152,210</b>	<b>\$537,737</b>	<b>\$95,552,463</b>

\* The total market value of the Alabama PACT Composite portfolio does not include the cash balance of \$2,011,620.07 that was in the Treasury Account on September 30, 2019.

MANAGER ALLOCATION SUMMARY - QUARTER ENDING SEPTEMBER 30, 2019					
Prior Quarter Market Value	%	Fund Name	Style	Current Quarter Market Value *	%
\$4,470	0%	Residuals	(FIXD)	4,494	0%
\$64,766,315	71%	Regions	(STFX)	65,153,610	68%
\$25,689,110	28%	Regions Cash	(CASH)	29,839,552	31%
\$407,091	0%	Regions Lockbox	(CASH)	559,301	1%
<b>\$90,866,986</b>	<b>100%</b>	<b>Composite</b>	<b>(TOTL)</b>	<b>95,556,957</b>	<b>100%</b>

\* The total market value of the Alabama PACT Composite portfolio does not include the cash balance of \$2,011,620.07 that was in the Treasury Account on September 30, 2019.

\*Source: SEI

# Economic & Financial Market Update

# Market Returns

Equities	YTD As of 9/30/19	Trailing 3 Months 9/30/19	2018	2017	2016	2015	2014	2013
S&P 500 Index (Large Cap Stocks)	20.55%	1.70%	-4.38%	21.83%	11.96%	1.38%	13.69%	32.39%
S&P 500 (Large Cap Growth)	21.06%	0.72%	-0.01%	27.44%	6.89%	5.52%	14.89%	32.75%
S&P 500 (Large Cap Value)	20.01%	2.83%	-8.95%	15.36%	17.40%	-3.13%	12.36%	31.99%
Russell 2500 Index (Small to Mid Cap Stocks)	17.72%	-1.28%	-10.00%	16.81%	17.59%	-2.90%	7.07%	36.80%
Russell Mid Cap TR USD	21.93%	0.48%	-9.06%	18.52%	13.80%	-2.44%	13.22%	34.76%
Russell 2000 Index (Small Cap Stocks)	14.18%	-2.40%	-11.01%	14.65%	21.31%	-4.41%	4.89%	38.82%
MSCI ACWI Ex-US (Foreign Stocks, Net Return)	11.56%	-1.80%	-14.20%	27.19%	4.50%	-5.66%	-3.87%	15.29%
MSCI EAFE Index (Foreign Stocks, Net Return)	12.80%	-1.07%	-13.79%	25.03%	1.00%	-0.81%	-4.90%	22.78%
MSCI EM (Foreign Stocks, Net Return)	5.89%	-4.25%	-14.58%	37.28%	11.19%	-14.92%	-2.19%	-2.60%
<b>Fixed Income</b>								
Barclays US Agg Bond TR USD	8.52%	2.27%	0.01%	3.54%	2.65%	0.55%	5.97%	-2.02%
BofA Merrill Lynch Muni 1-12 YR (Muni Bonds)	4.87%	0.84%	1.62%	3.21%	0.02%	2.34%	4.27%	-0.12%
Barclays Global Agg Ex USD TR	4.38%	-0.58%	-2.15%	10.51%	1.49%	-6.02%	-3.08%	-3.08%
Barclays High Yield Corp TR USD	11.41%	1.33%	-2.08%	7.50%	17.13%	-4.47%	2.45%	7.44%
Barclays US Treasury US TIPS	7.58%	1.35%	-1.26%	3.01%	4.68%	-1.44%	3.64%	-8.61%
FTSE Treasury Bill 3 Month (Money Market)	1.78%	0.56%	1.86%	0.86%	0.33%	0.05%	0.03%	0.05%
<b>Diversified Strategies</b>								
HFRX Global Hedge Index	5.90%	1.61%	-6.72%	5.98%	2.50%	-3.64%	-0.58%	6.72%

Source: Morningstar

# Economy

## Overview & Outlook

Economy		<p><u>Risks:</u></p> <ul style="list-style-type: none"> <li>▪ Business sentiment continues to erode as trade disputes intensify, choking off business investment</li> <li>▪ A slowing Chinese economy drags other Asian nations and the Euro Zone down</li> <li>▪ Low/negative interest rates distort asset prices and lead to unsustainable growth in debt</li> </ul>	<p><u>Opportunities:</u></p> <ul style="list-style-type: none"> <li>▪ Labor market conditions continue to improve</li> <li>▪ Rising real incomes</li> <li>▪ Solid rate of house price appreciation</li> <li>▪ Healthy household balance sheets</li> </ul>
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### Something's Happening Here . . . What It Is Ain't Exactly Clear

#### Services Sector Beginning To Waver?

- The BEA's third estimate puts annualized Q2 real GDP growth at 2.0 percent, unchanged from the second estimate. Consumer spending and government spending were the main drivers of Q2 growth, with business and residential fixed investment, trade, and inventories acting as drags.<sup>1</sup> Our baseline forecast anticipates real GDP growth around 2.0 percent over the final two quarters of 2019, which would put full-year growth at 2.3 percent.
- Monthly data on orders and shipments of core capital goods<sup>2</sup> suggest business fixed investment as measured in the GDP data was on course to decline in Q3. If so, this would mark back-to-back quarterly declines, something rare outside of recessionary periods. Flagging business sentiment and slowing global economic growth, which largely reflect the effects of trade disputes, are weighing on business investment and, in turn, real GDP growth.
- The ISM Manufacturing Index fell to 47.8 percent in September, the second straight month in which the headline index was below the 50.0 percent break between contraction and expansion. More disturbingly, the details of the September report were even weaker than the headline number. Perhaps the most telling detail is that only 3 of the 18 industry groups included in the ISM survey reported growth in September, the fewest of any month since April 2009, when the economy was still in the clutches of the 2007-09 recession.
- The ISM Non-Manufacturing Index fell to 52.6 percent in September; the broader services sector continues to expand, but this is nonetheless a three-year low.<sup>3</sup> This raises concerns over whether weakness in the industrial sector is infiltrating the broader economy, and bears watching in the months ahead.

#### September Employment Report: Not Great, But It Didn't Need To Be

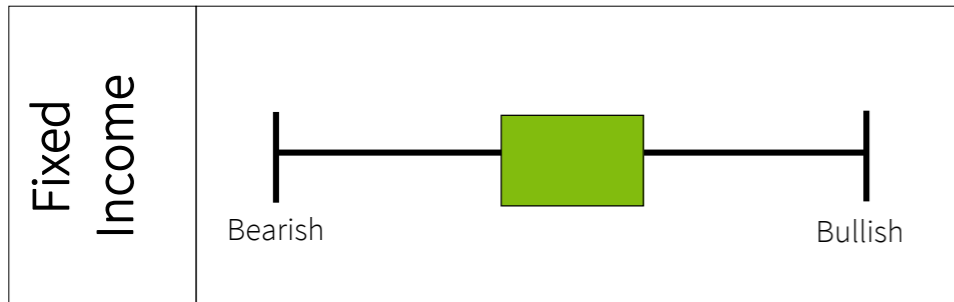
- In the wake of the surprisingly weak reports from the ISM the September employment report didn't need to be great, it only needed to not be terrible. Happily, it cleared that low bar. Total nonfarm employment rose by 136,000 jobs in September, while prior estimates of job growth in July and August were revised up by a net 45,000 jobs for the two-month period.<sup>4</sup>
- The unemployment rate fell to 3.5 percent in September, a 50-year low, while the broader U6 rate, which also accounts for underemployment, fell to 6.9 percent, the lowest rate since December 2000.<sup>4</sup>
- Average hourly earnings were unchanged in September, leaving them up 2.9 percent year-on-year.<sup>4</sup> Keep in mind, however, that weak prints on wage growth are common in months in which the survey period ends prior to the 15<sup>th</sup> of the month, as was the case in September. Also, there was a clear split in the September data, with average hourly earnings for production workers up by 0.2 percent after a 0.8 percent increase in August; over the past three months, year-on-year wage growth for this group, which constitutes the largest block of nonfarm employment, is running at a 3.5 percent pace, an 11-year high.<sup>4</sup>
- The employment data show signs of decelerating job growth, but do not suggest an economy on the verge of recession. The September employment report does not settle the question of whether or not the FOMC will again cut the Fed funds rate at this month's meeting. Though recent data show inflation pressures are building, the FOMC's sole focus at present is on sustaining the expansion. Our baseline forecast incorporates only one more funds rate cut by year-end, but we won't be at all surprised if the FOMC delivers two more cuts.

Source: 1) Bureau of Economic Analysis (BEA); 2) U.S. Census Bureau; 3) Institute for Supply Management (ISM); 4) Bureau of Labor Statistics (BLS)

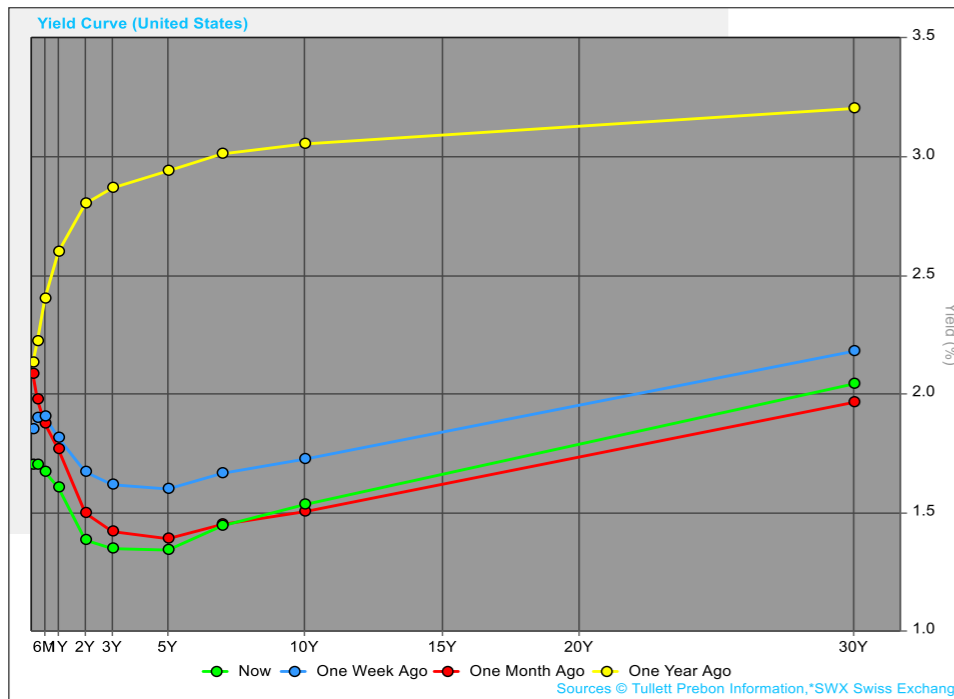
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# Fixed Income

## Overview & Outlook



Yields as of September 30, 2019	
US Treasuries	
3-month	1.83%
2-year	1.63%
5-year	1.55%
10-year	1.67%
30-year	2.11%



### Summary View: Neutral

- Federal Reserve has shifted from a “pause” to being open to rate cuts creating a more favorable environment for bonds.
- Restrained inflation and slowing growth should keep longer-term bonds from resuming towards higher yield levels
- Valuations remain expensive but will provide diversification with our expectations for higher equity market volatility. High Yield offers an attractive YTM over 6%, but don't expect much additional return from spread compression.
- Global developed sovereign bonds remain unattractive where the majority of bonds carry negative rates. Emerging market bonds provide a more attractive yield (~5% YTM) especially relative to developed countries, but currency effects can greatly influence a U.S. investor's return.

### Risks:

- Lower/higher growth and inflation creates less/more pressure on long-term interest rates versus expectations.
- USD appreciation impacts international bond returns and specifically EM countries ability to finance USD denominated debt.

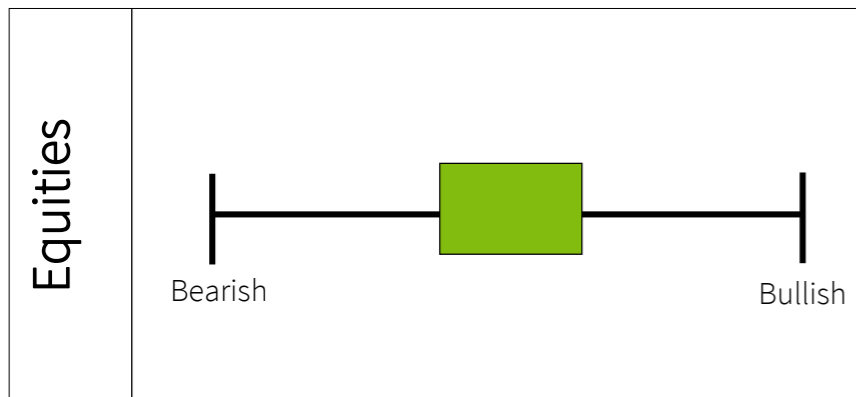
	YTD 9/30/2019	2018	2017	2016	2015	2014
<b>Total Return</b>						
Barclays US Agg Bond TR USD	8.52%	0.01%	3.54%	2.65%	0.55%	5.97%
Barclays High Yield Corp TR USD	4.87%	-2.08%	7.50%	17.13%	-8.30%	2.45%
Barclays Global Agg Ex USD TR	4.38%	-2.15%	10.51%	1.49%	0.36%	-3.08%
Barclays US Treasury US TIPS	11.41%	-1.26%	3.01%	4.68%	-1.44%	3.64%
FTSE Treasury Bill 3 Month (Money Market)	7.58%	1.86%	0.86%	0.33%	0.05%	0.03%

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Source: Prepared by Regions Asset Management using data from Morningstar and FactSet.

# Equities

## Overview & Outlook



S&P 500 Statistics as of September 30, 2019	
<b>Fundamentals</b>	
2018 Earnings	\$161
2019 Earnings Estimates	\$164
Forward P/E	18x
Dividend Yield	1.93%
<b>Technicals</b>	
% of Stocks Above 200ma	55%
VIX (CBOE Volatility Index)	16.24



### Summary View: Neutral

- After a substantial rebound in global equity prices to start 2019, forward returns are likely to slow to modest levels warranting a strategic neutral weight. Domestic valuations are in-line with historical averages while int'l markets are below.
- We believe global growth will remain a positive in 2019 but trade tariffs remain the largest risk and wildcard. Bottom-line, the probability of a U.S. recession in 2019 remains low, and the U.S. administration will likely be looking for a deal/political win in the coming months causing sentiment to improve and multiples to expand.
- We expect economic growth to steadily slow (not stop) over the next several quarters while global growth has already slowed materially. With limited revenue growth at a time when cost pressures are building should ultimately impact company margins.
- Long-term return expectations within equities remain favorable vs. other asset classes, especially emerging market international stocks.

### Risks:

- Central bank policy error or investors resetting expectations could create a flight to safety.
- Oil and commodity prices in general have a price shock causing dislocations for consumer spending and margin pressures for corporations.

	YTD 9/30/2019	2018	2017	2016	2015	2014
<b>Total Return</b>						
S&P 500 Index (Large Cap)	20.55%	-4.38%	21.83%	11.96%	1.38%	13.69%
S&P 500 (Large Cap Growth)	21.06%	-0.01%	27.44%	6.89%	5.52%	14.89%
S&P 500 (Large Cap Value)	20.01%	-8.95%	15.36%	17.40%	-3.13%	12.36%
Russell 2500 Index (Small to Mid Cap)	17.72%	-10.00%	16.81%	17.59%	-2.90%	7.07%
Russell Mid Cap Index (Mid Cap)	21.93%	-9.06%	18.52%	13.80%	-2.44%	13.22%
Russell 2000 Index (Small Cap)	14.18%	-11.01%	14.65%	21.31%	-4.41%	4.89%
MSCI World Ex-US (Foreign Stocks, Net Return)	11.56%	-14.09%	24.21%	2.75%	-3.04%	-4.32%
MSCI EAFE Index (Foreign Stocks, Net Return)	12.80%	-13.79%	25.03%	1.00%	-0.81%	-4.90%
MSCI EM (Foreign Stocks, Net Return)	5.89%	-14.58%	37.28%	11.19%	-14.92%	-2.19%

Source: Prepared by Regions Asset Management using data from Morningstar and FactSet.

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Are Not Deposits	Are Not Insured by Any Federal Government Agency	Are Not a Condition of Any Banking Activity