To:	**Cash Management Policy Board Investment Committee**
From:	**Jonovan Sackey, Jennifer Appel, Kevin Leonard**
Date:	**July 12, 2024**
Subject:	**2024 Endowment Manager Due Diligence Meetings**

Background

Members of the Delaware Office of the State Treasurer (OST) Staff and NEPC met with the two investment management firms charged with implementing the endowment portfolio structure for the Delaware OST. The purpose of the meetings was to discuss any significant changes to the investment management organizations, team members, and investment process, along with receiving updates on current portfolio positioning, potential portfolio positioning changes, and current market conditions. Further, the investment management firms relayed potential Investment Guideline enhancements to their mandates managed on behalf of the Delaware OST. The remainder of this memo summarizes the findings during these meetings.

Endowment Managers

SEI – Endowment Manager

SEI noted that there had been no significant changes to the investment organization, the assigned investment team, the investment philosophy, or the approach since the last annual update with Delaware OST staff and NEPC.

SEI is aligned with the belief that inflation will remain 'higher-for-longer', supported by encouraging consumer behavior and a strong labor market. While some level of disinflation has occurred, getting inflation down to the 2% Federal Reserve (Fed) target will prove much more challenging. SEI sees few signs of a recession looming and highlighted a potential hesitancy for the Fed to make any policy rate changes in light of the upcoming U.S. elections. From a global perspective, the portfolio was underweight Japan given a challenging combination of expensive security valuations and difficult macroeconomic conditions, which resulted in underperformance in that portion of the fund as Japanese markets continued to outperform other non-U.S. developed markets. Within Emerging Markets, an underweight to China and an overweight to Latin America have been additive to returns.

The portfolio is very concentrated from a risk management standpoint within core fixed income. The duration of this portion of the portfolio is about 6 years, a little longer than the benchmark, reflecting SEI's outlook for a rate cut in the near-term. High yield was a key contributor to performance over the last year given better-than-expected economic growth and the U.S.-denominated emerging markets debt allocation was also additive to performance.

SEI proposed an adjustment to the asset allocation policy within the portfolio that primarily centers around a reduction to U.S. equity and an increase to the world equity ex-U.S. exposure. SEI would also aim to consolidate the Emerging Markets Equity fund into the World Equity ex-U.S. fund in order to create more control over the global exposure. Lastly, the newly proposed allocation would see slight increases within U.S. high yield and Emerging Markets Debt. SEI projects these changes would result in a more efficient portfolio, capable of a slightly elevated return as well as reduced risk. No change in the fee structure should result from these adjustments.

Mercer – Endowment Manager

Mercer stated that there had been no significant changes to the investment organization, the assigned investment team, the investment philosophy, or the approach since the last annual update with Delaware OST staff and NEPC.

Mercer commended the strong economic growth that took place in the U.S. during Q1, compared to weaker growth in developed countries outside the U.S. Mercer highlighted China's economy, which continued to struggle but has exited a multi-month deflation spell. Overall, the firm expects a moderate slowdown in global growth in 2024 and 2025, while avoiding a hard landing.

Mercer recommended an adjustment be made to the target weights within the equity portion of the portfolio relative to the MSCI World Index benchmark. Mercer proposed increasing the current weight toward the Vanguard Total Stock Market Index from 39.6% to 42.4% and reducing the Vanguard Developed Markets Index exposure from 20.4% to 17.6%. As the firm does not have a one fund solution to track the MSCI World Index, these changes to the aforementioned funds would accomplish a similar exposure to the MSCI World Index. The recommendation includes no change to the Vanguard Total Bond Market Index allocation of 40%.

Closing Remarks:

NEPC believes that the recommended changes in this memo are reasonable and do not materially change the composition or goals and objectives of the portfolio. These changes primarily target operational and portfolio management efficiency and do not pose any issues from NEPC's perspective. We look forward to discussing this memo with the Investment Committee and Cash Management Policy Board at their upcoming meetings. In the meantime, please reach out with any questions you may have regarding the memo or the individual manager meetings.