

MINUTES OF THE JOINT MEETING
OF THE BOARD OF TRUSTEES OF
THE KENTUCKY JUDICIAL FORM RETIREMENT SYSTEM,
THE INVESTMENT COMMITTEE FOR THE
KENTUCKY JUDICIAL RETIREMENT FUND,
AND THE INVESTMENT COMMITTEE FOR THE
KENTUCKY LEGISLATORS' RETIREMENT FUND

January 17, 2025

The Board of Trustees of the Kentucky Judicial Form Retirement System (JFRS), the Investment Committee for the Kentucky Judicial Retirement Plan (JRP), and the Investment Committee for the Kentucky Legislators Retirement Plan (LRP), convened via videoconference utilizing Microsoft Teams on Friday, January 17, 2025, at 10:00 AM. All Board members participated with the exception of Senator Jimmy Higdon.

JFRS staff present included Bo Cracraft, Executive Director. Guests attending the meeting included Don Asfahl, John Watkins, Andy Means, and Derek Bonifer of Baird Trust Company.

Chairman Venters called the meeting to order at 10:02 a.m.

The trustees considered the adoption of the previously distributed *Minutes* from the October 18, 2024 and November 15, 2024 meetings. Upon motion by Judge Douglas George, seconded by Mr. Stephen LeLaurin, the Board unanimously approved the *Minutes* of the October 18, 2024 and November 15, 2024 meetings.

Chairman Venters recognized Mr. Cracraft, who notified the Board that Stan Kerrick, Lexington Investment Partners, was not going to make the meeting. He noted for the record a copy of *Lexington Investment's Compliance Report as of December 31, 2024* was included in the materials distributed in advance. Mr. Cracraft highlighted page one of the report, which noted that each plan was within its prescribed allocation and policy guidelines. In accordance with policy, JFRS maintains a copy of the *Compliance Report*.

Chairman Venters welcomed Baird Trust Company, who had joined the virtual meeting. Mr. Cracraft had previously distributed copies of Baird's *Investment Review for Kentucky Judicial Retirement Fund and Kentucky Legislators Retirement Fund* dated January 17, 2025. In accordance with Board policy, the System maintains a copy of the Investment Review.

Mr. John Watkins began the quarterly review with a few comments regarding Baird's most recent quarterly Market Commentary, titled "Our Core Investment Principles." While equity markets had performed extremely well over the past two years, the team wanted to reiterate some of their core investment principles. He acknowledged that strong equity returns are pleasant and always welcomed, but unfortunately good or bad results don't predict or tell investors much about the future. While many pundits and analysts will forecast and make predictions about what is to come, in truth, no one knows with any certainty and thus the team at Baird seeks to ignore the noise, remain disciplined, and stick to their core philosophy.

The foundation of Baird's investment philosophy is to always think and act as long-term business owners. They seek strong businesses with durable business models, strong and honest management teams, and healthy cultures that are valued at reasonable or discounted prices. The intent is to invest for 10 to 30 years, just as a true business owner would, and reap the powerful benefits of long-term compounding growth. They want to remain rational, objective, and remove emotion from investing. Instead of acting based on what the crowd is doing or through emotion, they seek to let data and reasoning guide their decision making. Mr. Watkins noted there were several reasons to be optimistic, but also just as many that lead to pessimism. He believes the portfolio was well positioned to perform in either environment and provide long-term results regardless of what the future brings.

Mr. Asfahl reviewed several economic statistics and highlighted recent unemployment results, which were a little higher than expected. He noted CPI was pretty flat and close to where Fed wanted it. Overall, CPI has been trending down and has landed pretty close to 50-year averages. However, Mr. Asfahl did draw attention to the Common Man CPI and how prices for everyday goods, such as food, clothing, and utilities had continued to outpace growth in wages. He noted there was definitely some inflationary pressure being felt by consumers. In addition, Mr. Asfahl discussed recent S&P 500 earnings, which had seen a slight revision since October. Overall, earnings growth was expected as compared to 2024, but not quite as high the expectation as predicted three months ago.

In response to a question from Mr. Cracraft with regards to consumer spending, Mr. Asfahl referenced the recently announced retail sales growth of 4%, which was largely driven by the Christmas holiday. However, it was further proof that folks are employed, have seen wages grow a little, and continue to spend. He did note that delinquencies and credit debt had begun to creep up a little, but that was not outside the norm for the holiday season. Mr. Watkins added that most major banks had recently reported, and the consumer sentiment remained strong. Folks don't appear to be saving quite as much as during the pandemic, but still in pretty good shape on average.

Next, Mr. Asfahl reviewed current portfolio allocations, annual estimated income, and the current yield on the JRP/LRP legacy portfolios. He noted the portfolios had been rebalanced in December to bring the equity allocation back closer to its target of 70%. This represented the fourth rebalance of 2024.

In response to a question from Judge George, with regards to the tremendous growth in assets of the portfolios and how that compared to other pension plans, Mr. Cracraft stated that growth had more than exceeded any expectation or assumption. And the JFRS plans had definitely outperformed results from other state pension plans. But he also highlighted that any future growth would be driven by investment return. Given the funding level of the plans, no employer contributions were expected in the near term and both JRP and LRP would expect to experience negative cash flow. Current retiree payroll and insurance costs well exceed contributions and income being received, so the asset base may not grow as consistently as it had recently, where equity markets posted very strong results four out of the last five years. Mr. Cracraft noted that other plans in the state, which are still underfunded, are receiving significant contributions, and in some cases, more contributions than expenses. That positive cash flow will serve to grow funds over time until they too reach a level where the contributions decline. However, But Mr. Cracraft stated that would take 20 to 25 years depending on the plan.

Next, Mr. Watkins reviewed a snapshot of the equity portfolio and highlighted relative sector weightings, top performers and recent portfolio attribution. He emphasized that industry weights were not the result of any top down or macro decisions, but rather the teams bottom-up approach. For instance, he noted the portfolio was overweight to industrials, but this was not a view on the sector, but rather the team had found attractive business to invest in. Secondly, he pointed to the portfolios top performers and pointed out that only one of the "Magnificent 7" were in the portfolio's top 10, while four of the top names were financials. Lastly, he discussed a few portfolio changes during the quarter. The team decided to exit their small position in CISCO Systems and used the proceeds to add to Meta Platforms.

Mr. Watkins also reviewed some recent attribution. Over the past year, the portfolios overweight to Industrials and Financials had served to really add value. An underweight to technology was a significant detractor, but Mr. Watkin stated that the team's decision to not hold NVIDIA accounted for effectively all the negative relative performance. He acknowledged the company continued to perform extremely well, but as discussed in prior meetings, NVIDIA was not something the team was looking to add to the portfolio. All semiconductors are historically very volatile and cyclical in nature. It might be costing the portfolio some outperformance in the short term, but they will always miss a few. He pointed out that even with the negative attribution from NVIDIA, the team added 300 basis points total for the 1-year period.

In response to a question from Mr. Allison regarding Expeditors recent underperformance and how tariffs might impact, Mr. Watkins stated the team was still trying to determine that exactly. Depending on the ultimate policy implemented, tariffs would definitely impact, but the company is well positioned and has carved out a strong niche position in the industry, specifically with regards to the international trade side. He also noted the stock was one of the smallest positions in the portfolio, so the lack of action, either to add to or exit the position was another sign the team didn't have a strong opinion just yet and was trying to show some patience.

In response to a question from Mr. Cracraft regarding the health care sector and the portfolios single holding of Johnson & Johnson, Mr. Watkins noted the team had exited Pfizer a few quarters ago, but believe J&J was a different story. While the stock had struggled a bit, he pointed out the stock had provided positive results, albeit below benchmark returns, in spite of a pretty stiff headwind to the industry as a whole. Unlike Pfizer, which struggled for a multitude of reason, J&J is more diversified, and the team believes patience will be rewarded.

In response to a question from Mr. Cracraft regarding the current number of stocks and recent additions, Mr. Watkins noted that the current number of holdings [25 stocks] was on the lower end of what the team targets. More recently, it has made more sense to use capitol raised from exiting positions to add to existing names. He pointed to the team's decision to use proceeds of Pfizer to add to GE Vernova as a very recent and good example. In response to a follow up regarding the three GE spinoffs and how profitable that decision had been, Mr. Watkins agreed. From a market cap point of view, what had traded at approximately 100 billion as just GE was not trading close to 400 billion as GE Vernova, Aerospace, and Healthcare.

Next, Mr. Bonifer began a discussion of fixed income markets and a review of the current portfolios, allocations, and upcoming maturities. He noted the team was continuing to use a ladder strategy and trying to invest across a variety of maturities. He noted that with recent equity rebalances and the current rate environment, the team had extended out a little further but

still remained within the targeted 10-year window. Rates on the longer end were climbing, so there was opportunity going forward. Mr. Bonifer concluded his comments with a review of the bond portfolio's credit distribution, a summary of risk statistics, as well as the portfolio distribution between corporate, treasury, and agency debt.

In response to a question from Ben Allision regarding cash flow and the team's ability to withstand negative markets, Mr. Cracraft did acknowledge the plans were subject to some timing. Outside of substantially changing the target to fixed income, the team couldn't quite schedule maturities to fully cover cash flow. However, he did note that staff was more conservative during periods where they lacked maturities and referenced the portfolios current cash balance as an example. With no maturities for six to nine months, the staff took advantage of the equity balance in December of 2024 and held on to cash. Current overnight rates have provided some relief, whereas a few years ago those rates were negative or effectively zero. He said the goal was to avoid selling equities in a declining market, but admitted no plan was completely fool proof.

Mr. Asfahl concluded the presentation with a review of recent performance and the portfolios' risk statistics. He also quickly highlighted the cash balance plans, which currently have a very similar risk and return profile. He reminded the trustees that all accounts held identical equity portfolios, while the two cash balance portfolios utilized a basket of ETFs to try and best mirror the fixed income allocations.

The next order of business was a quarterly compliance report from Lexington Investments LLC. Chairman Venters recognized Mr. Cracraft, who notified the Board that Stan Kerrick, Lexington Investment Partners, was not able to attend the meeting. He noted for the record the *Lexington Investment's Compliance Report as of December 31, 2024*, was included in meeting materials distributed to the trustees in advance. Mr. Cracraft highlighted page one of the *Report*, noting that each plan is within its prescribed allocation and policy guidelines. In accordance with Board policy, the System maintains a copy of the *Report*.

Chairman Venters recognized Mr. Cracraft, who reported on several administrative matters. The trustees discussed the items and took action when noted.

(A) Public Pension Oversight Board (PPOB). Mr. Cracraft gave a summary of PPOB meetings since the October JFRS Board meeting.

October 22, 2024. All three plans were asked to present an overview of Membership and Retiree Payroll information. Staff included a copy of the short deck of slides in the meeting materials.

November 19, 2024. All three plans were asked to present Actuarial Valuation results. Staff included a copy of the short deck of slides in the meeting materials. The only other agenda item was a short presentation from the Kentucky Deferred Compensation Authority.

December 9, 2024. JFRS was not on the agenda. The only agenda item included a discussion of a few legislative proposals that were expected in the 2025 session, but did not have any impact on JFRS plans.

At the time of the meeting, staff had not been notified regarding a January meeting. Mr. Cracraft indicated that in the past, these meetings have largely been focused on legislative proposals, so he was not expecting JFRS to be on the agenda.

(B) 2025 General Session. Mr. Cracraft referenced the *2025 Regular Session – Legislative Update* staff memo included in their materials. He noted the 30-day 2025 Regular Session of the General Assembly began on Tuesday, January 7, 2025. He reviewed a few retirement-related proposals, but as of the meeting date no legislation materially impacting either JFRS plan had been introduced.

(C) 2025-2026 Personal Service Contracts. Mr. Cracraft reviewed the following personal service contracts, and the Board took action where noted.

Investment Management. The June 16, 2022 Personal Service Contract with Baird Trust Company contained the option to extend the contract for two additional two-year periods beginning on July 1, 2024 under the same terms and conditions at a fee of eight (8) basis points. Mr. Cracraft noted that the Board did authorize staff to execute a 2-year extension during their January 2024 meeting and on May 9, 2024, a 2-year extension was agreed upon which is set to expire on June 30, 2026.

Audit Services. The August 9, 2022 Personal Service Contract with Blue & Co contained an option to extend the contract for one additional two-year period beginning on July 1, 2024. Mr. Cracraft noted that the Board did authorize staff to execute a 2-year extension during their January 2024 meeting and on June 11, 2020, a 2-year extension was agreed upon which is set to expire on June 30, 2026.

Actuarial Consulting. Mr. Cracraft reminded the Board that staff had issued an RFP for audit services in 2024. During their April 2024 meeting, the Board choose Gabriel Roeder Smith (GRS) as a result of that process. The May 9, 2024 Personal Service Contract with GRS does contain the option to extend the contract for three additional two-year periods beginning on July 1, 2026.

Legal Services. Mr. Cracraft indicated the current Personal Service Contract with Alan Pauw, McBrayer, was set to expire with not additional extensions.

Following a discussion, Judge Douglas George made a motion, seconded by Justice Laurance VanMeter, to enter into a Personal Service Contract with Mr. Alan D. Pauw and McBrayer PLLC, for legal services subject to successful negotiation and terms.

Custodian. State Street remains the custodian of the Funds. The Commonwealth of Kentucky issued an RFP in 2023 and awarded State Street a new contract, which included services to JFRS as a named agency of the Commonwealth.

Following discussion, it was the consensus of the trustees that JFRS continue to participate in the Commonwealth's custodian contract with State Street.

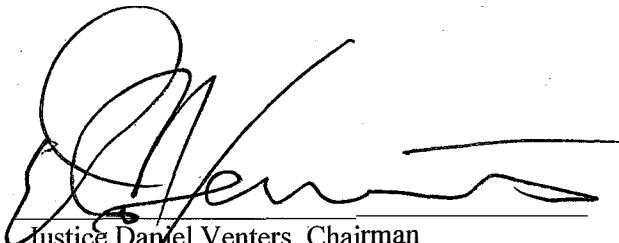
(C) FY 2024 Financial Audit Reports (Blue & Co.). Mr. Cracraft informed the Board that copies of the 2024 Audit Reports were included in the Board materials. He reminded the Board that upon receipt in November 2024, the reports were emailed to each trustee.

(D) Financial Disclosure Statements. Mr. Cracraft requested that each trustee complete a Financial Disclosure Report for calendar year 2024 on or before March 31, 2025 in order to comply with the annual mandated disclosure requirement. A copy of the disclosure was included in the material. He noted hard copies were available to those members in attendance.


(E) Line-of-Duty Taxation Question. Mr. Cracraft referenced a memo from Alan Pauw, McBrayer, regarding federal taxation of line-of-duty (LOD) benefits. He noted this topic was in response to the Board's determination to apply LOD benefits under the Fred Capps Memorial Act. Mr. Cracraft indicated there was some question as to whether or not these benefits were subject to federal tax or not, thus he had asked Mr. Pauw to review and provide an opinion.

After a health discussion, Judge Douglas George made a motion, seconded by Representative Scott Brinkman, authorizing staff to begin the process of seeking a Private Letter Ruling from the IRS as it relates to these benefits, while treating the benefits as taxable until notified otherwise. The motion passed unanimously.


There being no further business, the meeting adjourned at 12:01 p.m.




Justice Daniel Venters, Chairman
Board of Trustees



Mr. Ben Allison, Chairman
Judicial Retirement Fund Investment
Committee



Bo Cracraft, Executive Director



Representative Brad Montell, Chairman
Legislators Retirement Fund Investment
Committee