

GALLIARD EXTERNAL MANAGER OVERSIGHT PROGRAM

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Galliard Places PIMCO on Watch List Downgrades to Good From Superior Additional Allocations to PIMCO on Hold

Galliard External Manager Team

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Galliard has
downgraded PIMCO's
rating from Superior
to Good and placed
PIMCO on our
Watch List.

SUPERIOR

GOOD

ACCEPTABLE

BELOW
AVERAGE

NOT RATED

PIMCO is currently one of the external managers utilized as a manager in Galliard's multi-manager stable value investment solutions. Galliard's External Manager Team shares their thoughts on the recent changes at PIMCO and Galliard's evaluation process.

Q: PIMCO is currently one of Galliard's approved external managers for multi-manager investment solutions. Has Bill Gross' recent departure prompted you to reconsider keeping PIMCO on your approved list? What is Galliard thinking?

GALLIARD EXTERNAL MANAGER TEAM: Any time a manager has significant organizational changes we are concerned. We have been in close contact with the investment team at PIMCO and have initiated a full review of our utilization of PIMCO strategies. In the meantime, our External Manager Oversight Committee has downgraded PIMCO's rating from Superior to Good and placed PIMCO on our Watch List, restricting further allocations. We anticipate communicating the results of our full evaluation over the upcoming weeks.

Q: Are you familiar with the newly appointed Group CIOs at PIMCO? What do you think of the succession plan that PIMCO put in place?

GALLIARD EXTERNAL MANAGER TEAM: The Deputy CIO model put in place following the departure of Mr. El-Erian earlier this year was a positive step. Ideally, the model would have had more time to develop ahead of the departure of Mr. Gross, planned or otherwise. Galliard has been following Daniel Ivascyn, Andrew Balls, Mark Kiesel, Virginie Masisonneuve, Scott Mather and Mihir Worah since their appointments earlier this year. Our External Manager Team met with Mihir Worah earlier this year during one of our visits to Newport Beach.

From an organizational standpoint, a reliance on a single key individual is risky, as evidenced by the departure of Mr. Gross from PIMCO. The new Leadership structure does not rely as heavily on a single individual, and we believe this structure has potential longer-term. However, we were disappointed that PIMCO did not appear to have a succession plan immediately in place for Mr. Gross as Mr. Ivascyn was not announced as Group CIO until late Friday. This is especially frustrating in light of media reports that PIMCO had been considering terminating Mr. Gross.

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Q: Was Mr. Gross involved with the management of the strategy PIMCO manages for Galliard?

GALLIARD EXTERNAL MANAGER TEAM: No, Mr. Gross was not directly involved in managing any of Galliard's client portfolios. The PIMCO strategies managed for Galliard are overseen by Saumil Parikh and Sudi Mariappi. PIMCO has assured us that Mr. Parikh and Mr. Mariappi will continue to manage our portfolios.

Q: Do you think Mr. Gross' departure will have a broader impact on the organization as a whole?

GALLIARD EXTERNAL MANAGER TEAM: Clearly, Mr. Gross' departure will present significant change for PIMCO as an organization. As the founder of PIMCO and the originator of their investment process, Mr. Gross has long been viewed synonymously with PIMCO. We are currently focused on analyzing the extent to which PIMCO's investment process has evolved to rely on key individuals other than Mr. Gross. We are also evaluating the ability of PIMCO to endure a potentially significant and lengthy outflow of assets. We also have some concern that PIMCO may lose some talent either to Janus or other investment firms in the wake of Mr. Gross' departure. Notably, PIMCO is a large organization with an emphasis on a macro oriented, top-down investment philosophy. We believe the current leadership is unproven in this arena and as a result are continuing to evaluate all aspects of the changes following Mr. Gross' departure.

Q: Can you describe the strategy PIMCO currently manages for Galliard clients who are utilizing a multi-manager solution?

GALLIARD EXTERNAL MANAGER TEAM: For the majority of our multi-manager clients, PIMCO employs a total return strategy that is benchmarked against the Barclays Intermediate Aggregate Index. Assets are managed in a Wells Fargo Collective Fund and a Commingled Insurance Separate Account exclusively for Galliard's clients as well as Separate Accounts for Galliard clients. Allocations to external managers are broadly diversified and typical allocations range from 10-20% of the overall stable value portfolio per manager, limiting the impact of a single manager on the overall plan.

It is important to note that Galliard's stable value portfolios impose tight investment guidelines that restrict the risk parameters that external managers such as PIMCO may employ for our stable value strategy. The restrictions, which include duration bands, liquidity minimums, sector maximums, quality restrictions, limits on derivatives, and a prohibition on leverage, are specifically designed to reduce volatility from active management. Therefore, the nature of a stable value strategy can be quite different

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from a mutual fund.

Q: How have the PIMCO portfolios performed for Galliard?

GALLIARD EXTERNAL MANAGER TEAM: PIMCO has been part of Galliard's multi-manager solution since 1999. For the majority of that time period, PIMCO-managed portfolio performance has been strong. We have, however, observed some underperformance in the PIMCO-managed portfolios since the second quarter of 2013. Even before the events of the past year, we had been monitoring this closely. When we evaluate external managers for our multi-manager program, we consider a number of quantitative and qualitative factors. Short-term underperformance is not a key input into our evaluation and monitoring process. Instead, Galliard utilizes a number of criteria in evaluating managers, including: an assessment of the manager's investment process, the depth and breadth of the investment team, organizational stability, primary areas of investment risk-taking and how those risks are managed, support and compliance functions, and how the broader firm is managed. These criteria will be important considerations as we complete our full evaluation of PIMCO.

Q: Are you currently in contact with PIMCO? What changes has PIMCO communicated to you regarding their investment process?

GALLIARD EXTERNAL MANAGER TEAM: We have been in close contact with PIMCO following the changes earlier this year and we have also spoken directly with several key investment individuals at PIMCO following last week's announcement. PIMCO has reiterated that their investment process and the management of Galliard's portfolios will not change as a result of Mr. Gross' departure. Our External Management Team has scheduled a visit to PIMCO's Newport Beach office this month to further inform our opinion. Galliard will also be hosting representatives from PIMCO's New York office in the coming weeks as part of our routine visits with external managers.

Q: What is Galliard currently doing regarding the current allocation to PIMCO?

GALLIARD EXTERNAL MANAGER TEAM: Our External Manager Oversight Committee has placed PIMCO on Galliard's Watch List. We have also made the decision to put any additional allocations to PIMCO on hold at this time. We have commenced a full review of our use of PIMCO strategies and are in the process of determining whether further action is appropriate.

Q: Do you expect increased performance volatility in the short-term? Over the longer-term?

GALLIARD EXTERNAL MANAGER TEAM: As noted earlier, the investment guidelines that we have in place with all of our external managers, including PIMCO, restrict the latitude of

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external managers to limit performance volatility. This has long been Galliard's strategy with respect to our Stable Value External Manager program. Hence, we do not expect a significant increase in volatility that is directly related to the organizational changes at PIMCO. That said, specific asset classes and specific positions may experience temporary volatility as the indirect impact of increased mutual fund redemptions, but we believe this impact will be limited and temporary. Importantly, we expect the majority of assets leaving PIMCO will stay invested in fixed income, resulting in buying from other managers, broadly offsetting the impact of sales by PIMCO.

Q: Overall, do you think the changes going on at PIMCO will have a positive, negative, or no effect on the strategies PIMCO manages for Galliard?

GALLIARD EXTERNAL MANAGER TEAM: Galliard is concerned about the potential disruption of the investment process and team dynamic that might result from the changes as well as whether Mr. Gross' top-down insights can be replaced. We believe that the immediate concern is the distraction that the changes might have with the investment personnel at PIMCO, and the potential for further departures. As noted earlier, we believe the current investment leadership is somewhat unproven with respect to top-down macro strategy.

Q: What is PIMCO's plan to manage the distractions?

GALLIARD EXTERNAL MANAGER TEAM: PIMCO is structured internally with a model where the Account Managers are effectively the client facing Portfolio Managers. They work closely with the desk Portfolio Managers and with the clients and serve to insulate the desk Portfolio Managers from demands on their time. The desk Portfolio Managers are still very focused on managing underlying portfolios. In the short-term, they do expect the desk Portfolio Managers to be pulled into additional calls and meetings, but are working to minimize the amount of time that the desk Portfolio Managers are impacted during times when the market is open. Importantly, since Galliard client assets are in dedicated portfolios, the portfolios have not been directly impacted by increased redemptions.

Q: Are you making any immediate changes to the stable value strategy in light of the PIMCO situation?

GALLIARD EXTERNAL MANAGER TEAM: Our External Manager Oversight Committee is carefully monitoring and evaluating the changes at PIMCO and has responded by placing PIMCO on its Watch List, downgrading PIMCO's ranking to Good and restricting further allocations at this time.

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