MISSOURI'S 529 EDUCATION PLAN

September 23, 2020

FROM: Bruce A. Ring, Jr.
Director of Investments

RE: 2019 Annual Program Review

Section 166.450 of the Revised Statutes of Missouri requires the Director of Investments of the State Treasurer's office to annually review the Missouri Higher Education Savings Program ("MOST") and report those findings to the MOST Board ("Board"). The director must review five areas:

- Board administration
- Financial status
- Investment policy
- Participation rate
- Continued viability

Accordingly, I am pleased to report the following from my review for calendar year 2019.

I. Board Administration

Ascensus Government Savings Recordkeeping Services, LLC serves as MOST's program manager, record-keeper, and servicing agent. Together with its affiliates, Ascensus Government Savings has overall responsibility for the day-to-day operations of the plan. Formerly known as Upromise Investments, Ascensus Government Savings assumed responsibility as recordkeeping and servicing agent, for both the Direct and Advisor Plans on June 3, 2006. On February 7, 2011, the Board entered into another contract with Ascensus Government Savings extending through June of 2016. Another RFP for program management services was issued in 2015. On February 8, 2016, a new contract was entered into with Ascensus Government Savings extending the contract service period to June of 2021, under the terms of this contract the Advisor Plan was eliminated and the participants were migrated into the Direct Plan in 2016. In addition, the Board met quarterly during 2019, as required by law.

In June of 2020, the Board entered into a new contract with Ascensus Government Savings extending the contract service period to June of 2026.

II. Financial Status

Following is a review of the financial status of our major partners and a summary of the investment performance of the investment options within the MOST plan.

A. Financial Status of MOST Partners

Ascensus Government Savings is part of Ascensus, Inc., the largest independent retirement and college savings services provider in the United States, helping over twelve million Americans save for the future. With more than 35 years of experience, the firm partners with financial institutions to offer tailored solutions that meet the needs of financial professionals, employers, and individuals. Ascensus specializes in recordkeeping, administrative, and program management services, supporting over 115,500 retirement plans and 6.3 million 529 college savings accounts. It also administers more than 1.5 million IRAs and health savings accounts.

The investment manager for the Direct Plan, The Vanguard Group, Inc., remains a strong franchise. Vanguard is one of the world's largest investment companies, offering about 426 low-cost traditional funds and ETFs. As of June 30, 2020, more than 30 million investors have entrusted Vanguard with more than $6.3 trillion in global assets under management. Vanguard continues to be a leader in the 529 plan industry, evidenced by over $114 billion in 529 savings and pre-paid tuition plan assets under management. Headquartered in Malvern, Pennsylvania, Vanguard has about 17,600 employees spread across 19 locations worldwide.

B. Performance of MOST Underlying Funds

Overall, 2019 had a positive performance from all of its underlying portfolio's, both fixed income and equity showed improvement from the prior year. Equity portfolios showed results ranging from +21.56% to +30.88%, while the fixed income results ranged from +2.87% to +8.73%. Overall, the results show much better performance in all portfolio's from the previous program year. Overall it was a very good year from an investment perspective.

In 2019, the returns on the underlying funds in the Plan were quite a bit higher than the returns we saw in 2018, with all funds showing positive returns. The annual returns ranged from +2.87% in the DFA 2-year Global Fixed Income Portfolio to a high of +30.88 in the Vanguard Total Stock Market Index Plus Fund.

Treasurer Fitzpatrick's office is responsible for monitoring the relative performance of each of the underlying investment alternatives versus an established benchmark. This effectively measures the contribution that the investment manager's expertise has on participants' returns. During calendar year 2019, both absolute returns and relative performance were positive with a couple exceptions to relative performance. All of the underlying portfolios performed as expected or slightly below benchmark, with 3 of the DFA funds underperforming enough to warrant WATCH list status during 2019. While index funds are expected to be at or slightly below benchmark, depending on the extent to which they stray from exact matching of the index, actively-managed funds are expected to exceed those benchmarks. All Watch List funds from 2019 have been removed from WATCH.

III. Investment Policy

In mid-2007, the Board adopted a formal investment policy governing program investment. The policy establishes objectives for structuring the investment options; formulates policies for selecting appropriate investment managers and the use of specific investment vehicles; and establishes an investment-performance process for underlying funds in the Plan. The policy is an important statement by the Board in terms of defining its fiduciary responsibilities and standards for Treasurer Fitzpatrick's office staff and MOST partners.

Since its adoption, the policy has been amended twice. In 2008, the Board modified the policy to allow the Director of Investments, rather than the Board, to place a fund on, or release it from, the "WATCH" status.

In August 2011, the Board made several modifications to the policy. The Board lengthened a fund's formal review period—specifically, up three consecutive quarters from two—when looking at benchmark performance evaluation for the Watch List. When determining a fund's Watch List eligibility and quarterly performance, the Board also added "Beta" and "Alpha" measures to a review process. Finally, the Board eliminated the "value of active management" measurement criteria.

In June 2016, a new Investment Policy was adopted by the Board when the Advisor Plan participants were merged into the Direct Plan and the Advisor Plan was eliminated.

In September 2019, a new version of the investment policy was adopted by the Fitzpatrick Administration, after review, with no substantive changes.

IV. Participation Rate

The following is an examination of the participation rate of the MOST programs. By examining the participation rate for the program, we can attempt to gauge the relative success the program has had in reaching the state's residents and encouraging them to increase 529 savings—the original goal of the IRS section authorizing these programs. The relative success or failure of states' various 529 programs rests on many different factors including the effectiveness of marketing efforts, availability of a state tax deduction, demographic and economic conditions, cost structure and the abilities, and resources of states' partners to attract and retain assets. However, one facet that has remained a constant is the competition for assets among states' program managers, which remains fierce.

A. Growth of Plan in 2019

The MOST Plan experienced growth in both accounts and assets during the year. After a severe downturn in December of 2018, the plan experienced significant growth throughout the 2019 calendar year. The positive change in number of accounts is primarily due to the marketing efforts and public awareness of the program as well as the expansion of benefits to K-12 participants.

Plan assets grew by over 17% in 2019, as compared to a -3.74% growth rate in 2018, ending the year at approximately $3.4 billion as compared to calendar year 2018 at $2.893 billion and year-end 2017 at $3.006 billion.

2019 contributions were slightly outpaced by withdrawals in the plan. Total contributions for 2019 were at $356.1M, roughly the same as 2018. Total withdrawals for 2019 were at $356.7M, up $27M from last year.

The number of accounts increased in 2019 to 172,900 as compared to 167,380 in 2018 and 157,634 in 2017. The vast majority of accounts are Missouri residents which account for almost 90% of account ownership.

B. Comparison of MOST Participation to National Trends

Nationally, assets in 529 Plans on average have grown significantly over the past decade. However, last year the significant negative market action in December created an environment where most 529 Plans experienced a dip in assets under management (despite strong contributions last year). The Missouri's MOST Plan's 2018 results were consistent with its peers.

For 2019, MOST assets were increased by 17% which was comparable to most Direct Plans in 2019. This was attributable to the positive market environment during the year. When compared to our peer plan group, MOST has performed well over the past 5 periods showing a 7.79% compound growth rate, once again outperforming 4 of our six peer group members.

Nationally, assets in 529 Plans on average have grown significantly over the past decade. As indicated earlier, assets in the MOST program increased to $3.4B at the end of 2019. This represented a 18.82% increase from assets in the plan at the close of 2018. The Missouri MOST Plan's 2019 asset growth results were close to the national average of other Direct Plans (according to Strategic Insight Reporting, the average Direct Plan assets increased by 22.10% in 2019).

The MOST Plan continues to show strong organic growth. The plans added 5,590 new unique beneficiary accounts in 2019, which represents 3.6% growth, which is consistent with its peers.

V. Continued Viability

The MOST 529 Plan remains a viable 529 savings program. In Ascensus Government Savings' 12½-years of program management, we have experienced strong trends in asset and account growth despite the market turmoil that plagued much of this period. We also saw an upswing in the number of new beneficiaries enrolled in the plan, which shows growth of new customers.

Throughout the economic downturn and subsequent recovery, the Plan's performance has been resilient. The fact that participants weren't required to make non-qualified withdrawals on a large scale during this period is promising. As a result, the majority of participants should have experienced full recovery of their 529 savings account balances and some asset growth. The economic environment has been quite good for the past two or three years and should remain so for the coming months although fears of a recession have been surfacing.

In an effort to further strengthen our future performance, in 2018 the Board decided to restructure the glidepaths in the plan to provide a smoother transition through the years and lessen some of the risks associated with transitioning from 1 age group to the next. The addition of DFA funds has enhanced our program offerings and should improve our overall plan.

Additionally, with the addition of K-12 participation in the plan, we saw a new significant driver of new accounts and withdrawals during 2019. This will most likely trend higher in future years as the availability of this option becomes more widely understood.

Missouri's MOST 529 Plan remains not only viable, but well positioned for growth as one of the remiere plans in the country.