

Prepared for  
Bay County Employees' Retirement System  
April 21, 2016

# Representing Baird Advisors

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# Section 1

## Firm Overview

# Overview of Baird

Baird has been helping clients achieve their asset management, investment banking and private equity goals for over 90 years.

**1919**

Founded in Milwaukee

**2004**

Baird becomes employee-owned

**\$1 billion**

Revenue

**3,200**

Employees

**2,110**

Employee shareholders

**13**

Number of consecutive years Baird has been recognized as one of the FORTUNE 100 Best Companies to Work For®

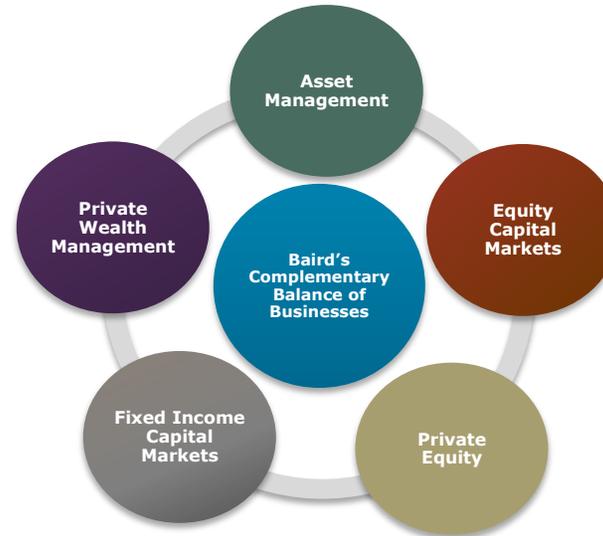
**1**

Pension & Investments recognized Best Places to Work in Money Management for fourth consecutive year (50-99 employees)

**1**

Ranked No. 1 "most trusted" research in Greenwich Associates survey 2004-2014

## A Comprehensive Financial Services Firm



## Baird Advisors Highlights

- Dedicated team focused on fixed income
- Over **\$40.0 billion** of assets under management as of March 31, 2016
- Disciplined, research driven approach
- Focus on superior customer service

## Baird's International Presence

### United States



### Europe



### Asia

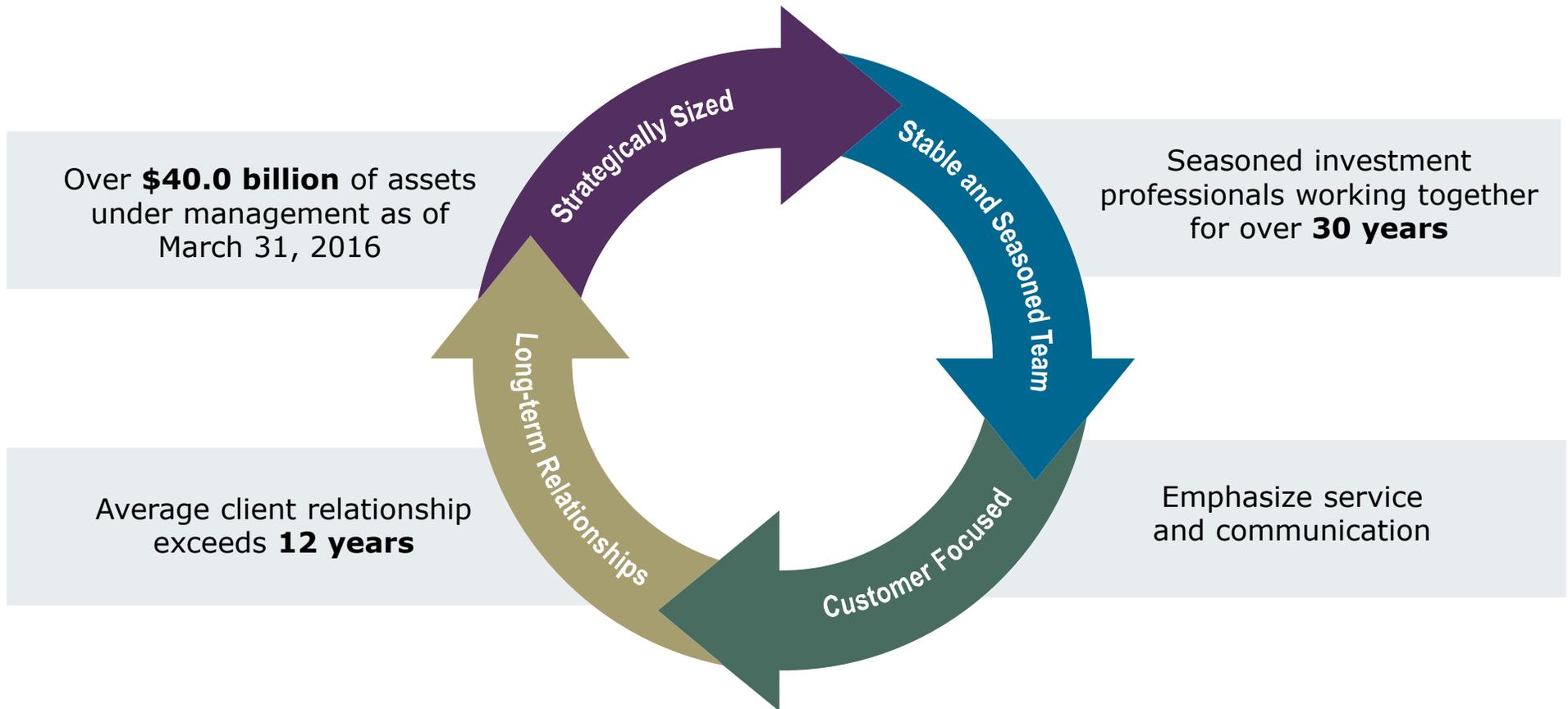


Milwaukee Chicago New York London Frankfurt Hamburg Hong Kong San Francisco Palo Alto  
Atlanta Boston Philadelphia Tampa Washington, D.C. Beijing Shanghai Stamford Charlotte

Greenwich Associates U.S. Equity Investors – Small/Mid-Cap Funds, 2004-2013. Surveys conducted with 94 U.S. small-cap and mid-cap fund managers. Rankings based on top 10 research firms in survey. Baird ranked No. 1 for "Most Trusted" Research and No. 1 for "Top Five" Research Firms for Importance. Baird and its operating affiliates have offices in the United States, Europe and Asia. Robert W. Baird Ltd. and Baird Capital Partners Europe are authorized and regulated in the UK by the Financial Conduct Authority.

# Overview of Baird Advisors

Experienced team with a track record of consistent results in high quality fixed income management



# Baird Advisors - Representative Clients

Client relationships exceeds 12 years

The image displays a large collection of logos for representative clients, organized into four main categories represented by colored arrows pointing towards a central seal:

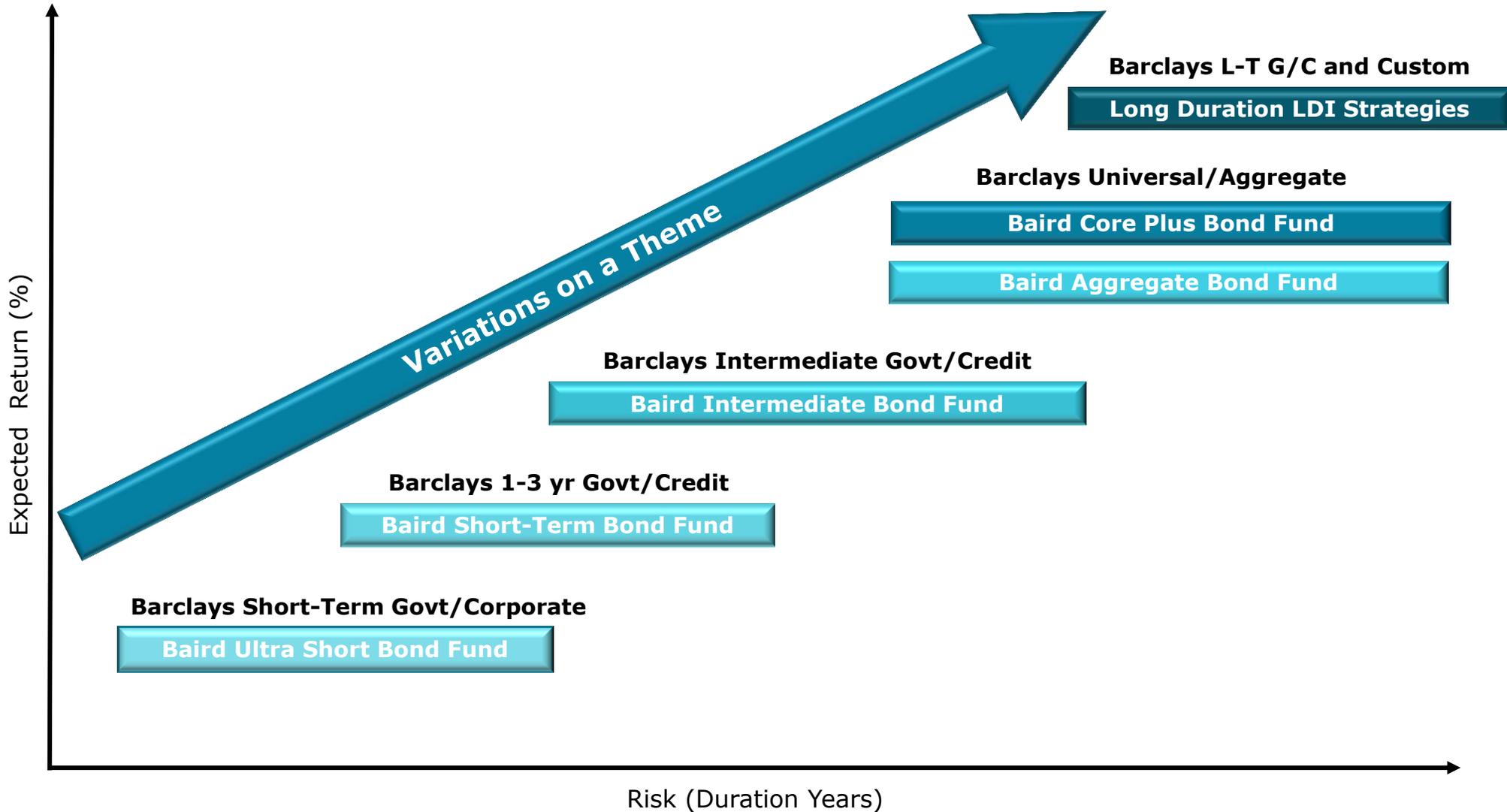
- Insurance & Healthcare (Dark Blue Arrow):** Includes logos for Meriter, Anthem, Mack, maif, WCRB, Texas Mutual, Blue Cross, and others.
- Retirement Plans (Green Arrow):** Includes logos for North Central States Regional Council of Carpenters' Benefit Funds, GOODYEAR, SFERS, MTA, MILWAUKEE ERS, MedStar Health, CERA, LACERS, DRESSER-RAND, KOHL'S, and others.
- Foundation / Endowment (Dark Green Arrow):** Includes logos for University of Colorado Boulder, VIDANT HEALTH, Presence Health, MAKE-A-WISH, Charter School Growth Fund, THE CATHOLIC COMMUNITY FOUNDATION, PBS, and others.
- Customized (Light Blue Arrow):** Includes logos for ASCENSION HEALTH, SUMMA Health System, Christian Brothers Services, WEST BEND, the Pension Fund, VML, BLOODCENTER of WISCONSIN, Children's Hospital of Wisconsin, Aurora Health Care, Gavi, WELS, LOCAL 139, KERA KXT91.7, and others.

At the center of the four arrows is the seal of Bay County, Michigan, featuring a figure holding a scale and a sword, with the text "BAY COUNTY MICHIGAN - 1857".

Note: The clients listed above represent various industry groups and geographic locations and were not selected based upon performance. Their appearance is not an indication of approval or disapproval of the investment management services provided.

# Structured, Risk-Controlled Taxable Portfolio Management

Consistent approach applied across risk spectrum



# Baird Taxable Bond Funds

## Total Net Returns as of March 31, 2016

	Annualized						Since Inception Lipper Rank & Percentile
	1Q 2016	1 Year	3 Year	5 Year	10 Year	Since Inception <sup>1</sup>	
<b>Baird Core Plus Bond Fund - Institutional</b>	<b>3.06%</b>	<b>1.38%</b>	<b>2.66%</b>	<b>4.49%</b>	<b>5.92%</b>	<b>6.21%</b>	6 of 59
Barclays Universal Bond Index	3.07%	1.75%	2.51%	3.95%	5.03%	5.48%	<b>11%</b>
<b>Baird Aggregate Bond Fund - Institutional</b>	<b>3.03%</b>	<b>1.78%</b>	<b>2.87%</b>	<b>4.69%</b>	<b>5.21%</b>	<b>5.76%</b>	12 of 158
Barclays Aggregate Index	3.03%	1.96%	2.50%	3.78%	4.90%	5.28%	<b>8%</b>
<b>Baird Intermediate Bond Fund - Institutional</b>	<b>2.55%</b>	<b>1.93%</b>	<b>2.09%</b>	<b>3.67%</b>	<b>4.85%</b>	<b>5.24%</b>	50 of 158
Barclays Intermediate Govt/Credit Index	2.45%	2.06%	1.83%	3.01%	4.34%	4.78%	<b>32%</b>
<b>Baird Short-Term Bond Fund - Institutional</b>	<b>1.21%</b>	<b>1.30%</b>	<b>1.46%</b>	<b>2.09%</b>	<b>3.18%</b>	<b>2.95%</b>	32 of 137
Barclays 1-3 Year Govt/Credit Index	0.98%	1.04%	0.95%	1.14%	2.80%	2.61%	<b>24%</b>
<b>Baird Ultra Short Bond Fund - Institutional</b>	<b>0.35%</b>	<b>0.38%</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>0.83%</b>	9 of 111
Barclays Short-Term Govt/Corporate Index	0.26%	0.43%	n/a	n/a	n/a	0.31%	<b>9%</b>

Performance data quoted represents past performance. Past performance does not guarantee future results. Investment return and principal value of an investment in the fund will fluctuate so that an investor's shares when redeemed, may be worth more or less than their original cost. The funds' current performance may be lower or higher than the performance data quoted. For performance current to the most recent month-end, please visit [www.bairdfunds.com](http://www.bairdfunds.com).

Expense Ratio for the Institutional Share Classes is 0.30%; for the Investor Share Classes is 0.55%. The Advisor has contractually agreed to waive management fees for the Baird Ultra Short Bond Fund in an amount equal to an annual rate of 0.15% of the average daily net assets for the Fund until April 30, 2017. The agreement may only be terminated prior to the end of this term by or with the consent of the Board of Directors of Baird Funds, Inc.

Returns shown include the reinvestment of all dividends and capital gains.

<sup>1</sup> The Baird Core Plus, Aggregate and Intermediate Bond Funds Since Inception net returns are based on performance from September 30, 2000 through March 31, 2016. The Baird Short-Term Bond Fund Since Inception net return is based on performance from August 31, 2004 through March 31, 2016. The Baird Ultra Short Bond Fund Since Inception net return is based on performance from December 31, 2013 through March 31, 2016.

# Consistency is Key

## Baird Taxable Bond Funds – Institutional Shares

Percentage of Time the Funds Outperform their Morningstar Category Average				
Rolling Time Periods	Baird Short-Term Bond	Baird Intermediate Bond	Baird Aggregate Bond	Baird Core Plus Bond
1 Year	91 %	61 %	94 %	91 %
2 Year	95 %	67 %	96 %	94 %
3 Year	99 %	77 %	99 %	100 %
5 Year	100 %	85 %	100 %	100 %

Source: Morningstar Direct as of March 31, 2016

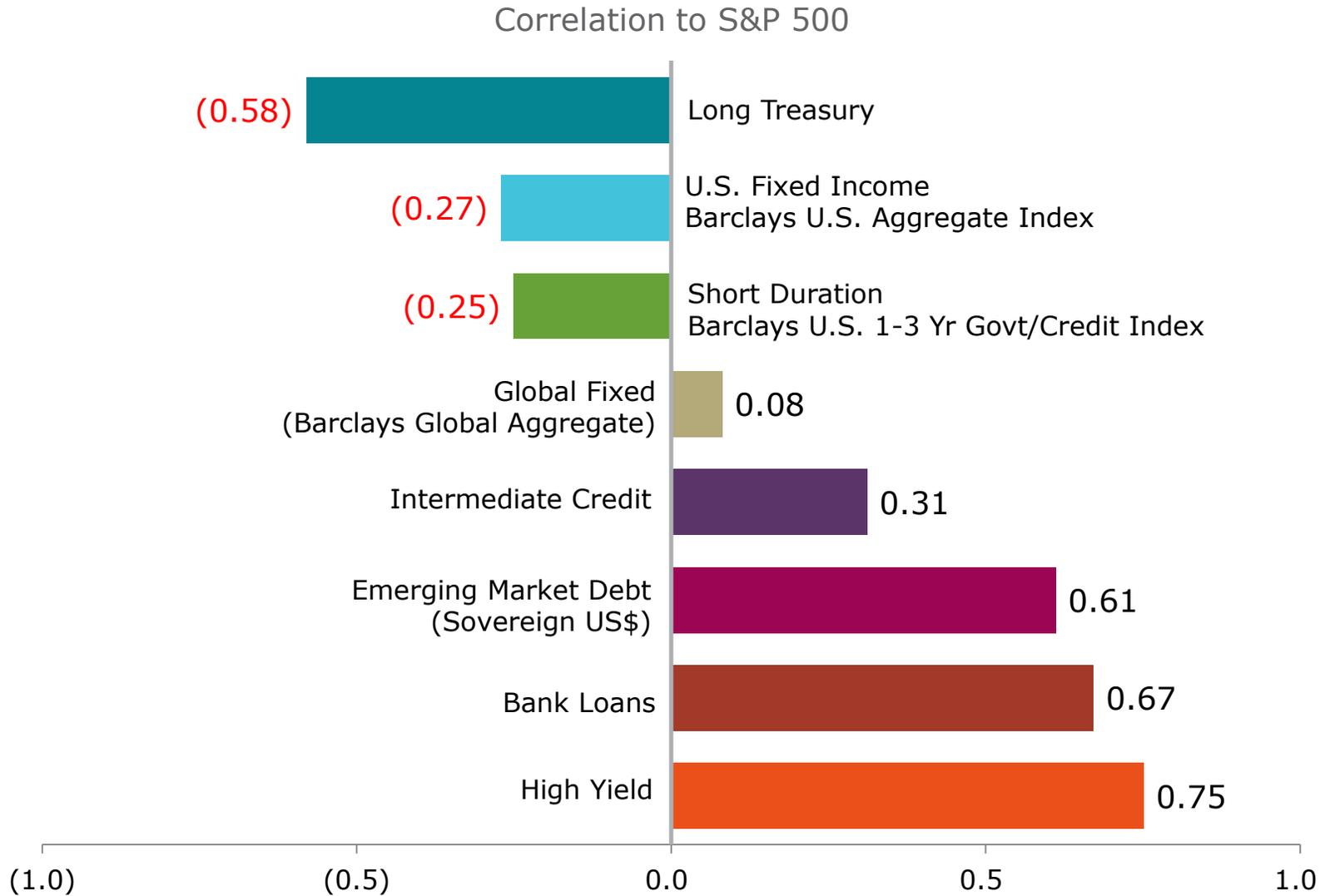
Performance numbers used are through each month end period from each fund's inception date.

The Baird Core Plus, Aggregate and Intermediate Bond Funds Since Inception net returns are based on performance from September 30, 2000 through March 31, 2016. The Baird Short-Term Bond Fund Since Inception net return is based on performance from August 31, 2004 through March 31, 2016.

All supporting information available upon request.

Past performance does not guarantee future results.

# Diversification Benefits of High Quality Bonds



Analysis for 10 years through 12/31/15, using quarterly data  
 Source: Callan Investments Institute

# Investment Philosophy & Process:

## A Two-Fold Approach

### Step 1: Structure Portfolio to Achieve Return of the Benchmark

Step 2

- |   |   |
|---|---|
| <ul style="list-style-type: none"> <li>Complete Understanding of the Benchmark</li> </ul>                         | <ul style="list-style-type: none"> <li>Quantify duration, sector and sub sector weightings</li> <li>Evaluate pricing, turnover and projected changes to benchmarks</li> <li>Purchase only U.S. dollar denominated securities</li> </ul>     |
| <ul style="list-style-type: none"> <li>Remain <b><i>Duration Neutral</i></b> to Control Portfolio Risk</li> </ul> | <ul style="list-style-type: none"> <li>Precisely match duration to index at all times</li> <li>Immediately adjust portfolio as contributions and withdrawals occur</li> <li>Rebalance at month-end to match benchmark changes</li> </ul>    |
| <ul style="list-style-type: none"> <li>Maintain Strict Adherence to Portfolio Guidelines</li> </ul>               | <ul style="list-style-type: none"> <li>Continuously monitor risk-control measures</li> <li>Use scenario analysis</li> <li>Compliance systems for all portfolio trades</li> </ul>  |
| <ul style="list-style-type: none"> <li>Emphasis on Security Structure/Credit Research</li> </ul>                  | <ul style="list-style-type: none"> <li>Evaluate specific security covenants, cash flows and liquidity concerns</li> <li>Assess company financials and management</li> <li>Consider prospects for sector and position in industry</li> </ul> |

# Investment Philosophy & Process:

## A Two-Fold Approach

Step 1

### Step 2: Add Incremental Value through Bottom-Up, Risk Controlled Process

**Consistent, Competitive Performance over Complete Market Cycles**

#### Sources of Added Value:

- |                                  |  |
|----------------------------------|--|
| ▪ <b>Yield Curve Positioning</b> | <ul style="list-style-type: none"> <li>▪ Optimize yield and "roll down"</li> <li>▪ Analyze yield curve on a continual basis</li> </ul>   |
| ▪ <b>Sector Allocation</b>       | <ul style="list-style-type: none"> <li>▪ Evolve sector allocations around long-term biases</li> <li>▪ Focus on relative value</li> <li>▪ Yield spreads and underlying risks change constantly</li> </ul> |
| ▪ <b>Security Selection</b>      | <ul style="list-style-type: none"> <li>▪ Structure</li> <li>▪ Attributes</li> <li>▪ Liquidity</li> </ul>   |
| ▪ <b>Competitive Execution</b>   | <ul style="list-style-type: none"> <li>▪ Capitalize on market inefficiencies</li> <li>▪ Receive timely market information</li> <li>▪ Utilize long-standing dealer relationships</li> </ul>               |

**We seek to consistently add 15-50 basis points of incremental return**

## Section 2

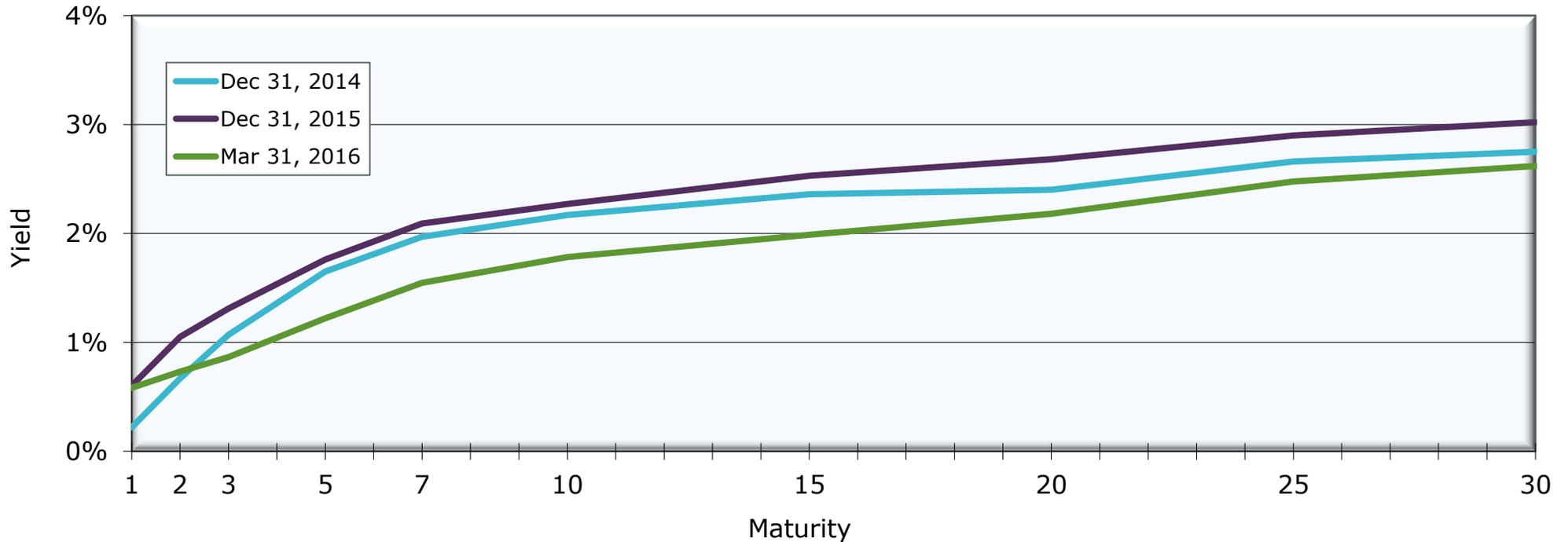
### Market Update

# Current Environment

- **U.S. Economy:** Moderate growth continues; broad-based and durable though headwinds remain
- **Inflation:** Modest uptick in wages though still benign; consumer inflation well below Fed's 2% target on lower oil
- **Europe:** Slow growth and disinflationary pressures continue even with extraordinary ECB stimulus
- **China:** Transitioning economy continues to slow; further currency devaluation likely
- **Fed:** Recent market turmoil shifts Fed's thinking to fewer rate hikes; "caution is especially warranted"
- **Risk Environment:** Remains elevated
  - Heightened global growth concerns
  - Effectiveness of central bank policies in question
  - Volatility in commodities and global currencies

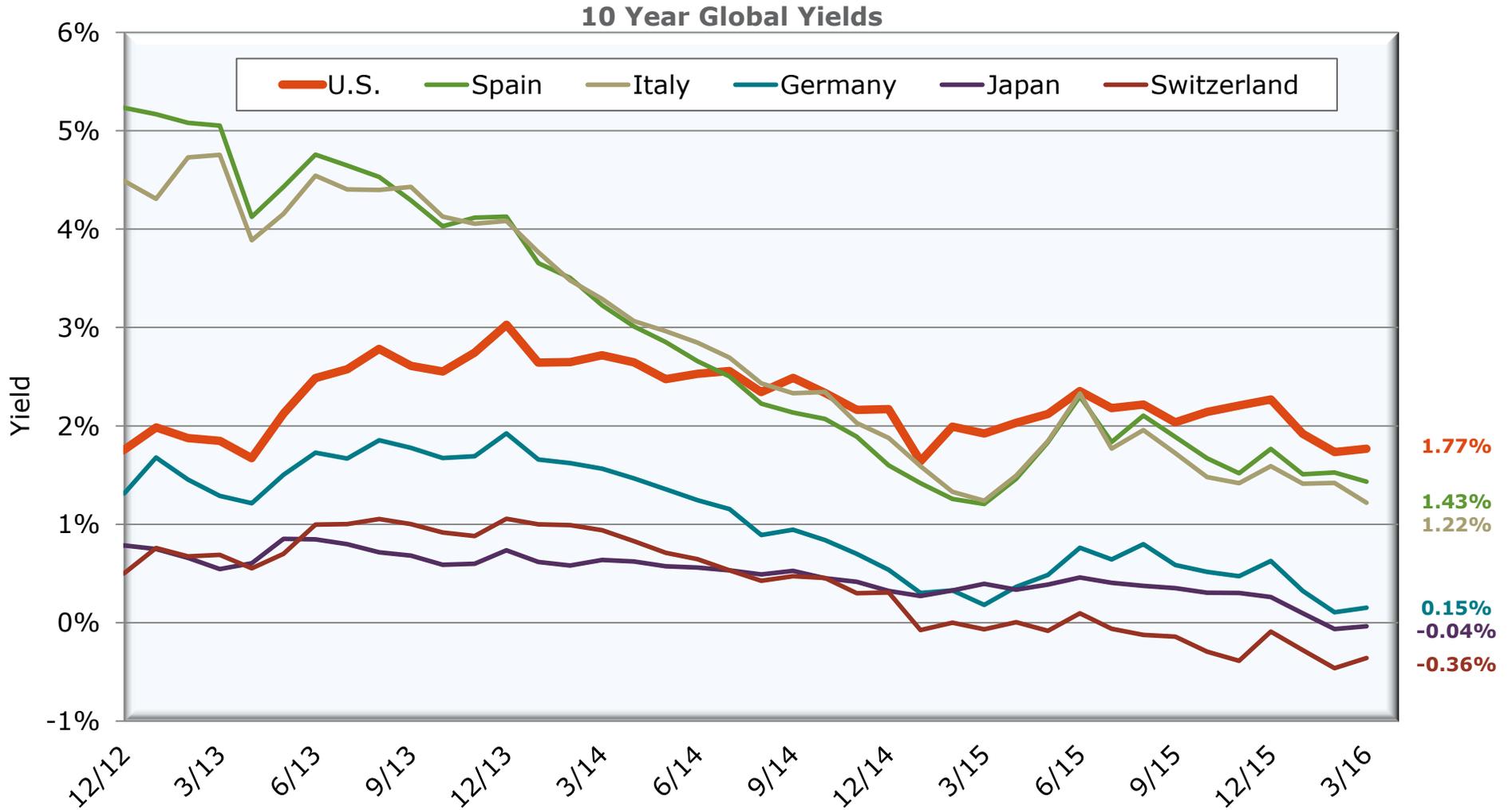
# U.S. Treasury Yields - 2016

Rates Fall on Global Growth Concerns and Resulting Market Turmoil



Maturity	December 31, 2014	December 31, 2015	March 31, 2016	1Q Change
1	0.22%	0.60%	0.58%	-0.02%
2	0.67%	1.05%	0.73%	-0.32%
3	1.07%	1.31%	0.86%	-0.45%
5	1.65%	1.76%	1.22%	-0.54%
7	1.97%	2.09%	1.55%	-0.54%
10	2.17%	2.27%	1.78%	-0.49%
30	2.75%	3.02%	2.62%	-0.40%

# U.S. Treasuries Attractive to Global Investors



# Yield Spreads Volatility High to Start 2016

Option-Adjusted Spreads (bps)								
	6/30/07	12/31/08	12/31/15	2/11/16 (Qtrly Wide)	3/31/16	1Q Change	5 yr Avg OAS	10 yr Avg OAS
<b>U.S. Aggregate Index</b>	53	213	56	68	56	0	57	72
<b>U.S. Agency (non-mortgage) Sector</b>	34	93	21	21	20	-1	18	32
<b>Mortgage and ABS Sectors</b>								
U.S. Agency Pass-Throughs	65	145	24	21	22	-2	44	54
Asset-Backed Securities	57	955	72	68	74	2	60	142
CMBS	82	1010	121	135	109	-12	158	256
<b>Credit Sectors</b>								
U.S. Investment Grade	97	555	165	214	163	-2	151	183
Industrial	104	500	183	235	168	-15	144	166
Utility	100	537	150	165	151	1	141	170
Financial Institutions	88	629	134	185	155	21	164	211
U.S. High Yield	292	1669	660	839	656	-4	516	590

# Bay County 1Q2016 Agency PT Purchase

- **January 2016 Buy ~\$450,000 current face FG G07801 at \$107.00**
- **Purchase price equates to +25 bps option adjusted spread (OAS)0**

## Buy Rationale:

- **4% coupon Freddie Mac Giant “benchmark” mortgage pool – original pool size >\$1BLN total size**
- **>5600 loans with maximum average loan size of 175,000 – mortgages with smaller loan sizes require more interest rate incentive to refinance to cover the fixed costs associated with the transaction**
- **These pools help protect against the unfavorable duration drift (negative convexity) associated with the sector**

## Section 3

### Update on Bay County Employees' Retirement System

# Risk Controls in Taxable Portfolio Construction



**Duration neutral to benchmark**



## **U.S. Treasury and Government Agency Securities**

- Emphasized for long duration exposures
- Used to match duration



## **Credit Securities**

- Limited credit exposure in more volatile sectors with continuous review of credit allocation
- Focus on financial industry with higher priority given to credit rating
- Diversification increases as quality decreases



## **Mortgage-Backed and Asset-Backed Securities**

- Focus on fixed-rate collateral vs. ARMs
- Safety of senior tranches if not U.S. Government Guaranteed
- Subject to ongoing stress-testing



## **Cash Bonds**

- No foreign currency
- No derivatives
- No leverage



## **Ongoing Portfolio Monitoring**

- Continuous review of portfolios for adherence to stated guidelines and objectives

**Risk control is the foundation of our investment discipline**

# Investment Outlook

- **Portfolio yield advantage over benchmark**
- **Portfolio positioned to modestly benefit from flattening of the yield curve**
  - Duration neutral overall
  - Modest underweight to front end of yield curve through use of floating rate securities
  - Continue to emphasize securities with attractive “roll-down”
- **Portfolio positioned to benefit from spread sector outperformance**
  - Maintain nominal underweight to U.S. Treasury sector
  - Opportunities across spread sectors more selective
  - Maintain modest overweight to spread sectors on duration-weighted basis
- **Continued Focus on Risk Control**
  - Emphasize diversification
  - Maintain coupon advantage
  - Use of floating rate securities
- **Experienced team and risk controlled process key to long-term success**

# Bay County Employees' Retirement System

## Summary Investment Objectives and Portfolio Guidelines

### **Investment Objective:**

To achieve a return over the longer term, 3 to 5 years, in excess of the combined (50%) Barclays Government Bond Index and (50%) Barclays Mortgage Backed Securities Index.

### **Primary Investment Focus:**

- The account will invest in U.S. government securities. Permitted investments are governments and government agency bonds and notes and governments and government agency residential and commercial mortgage-backed securities.
- All debt obligations must be rated Baa3/BBB- or better by at least one NRSRO (e.g. Moody's, Standard & Poor's, or Fitch) at time of purchase. For debt obligations rated by more than one NRSRO, the highest rating shall apply.
- The manager shall notify the Bay County Employees' Retirement System and its Investment Consultant whenever investments in cash and equivalents exceed 10% of the portfolio.
- Prohibited Investments include foreign securities, interest only ("IO's") and principal only ("PO's") mortgage securities and other structures incorporating leverage, short sales, use of futures and options for hedging purposes, securities that are not publicly traded, margin or leverage purchases, or direct commodities.

# Bay County Employees' Retirement System

Portfolio Characteristics as of March 31, 2016

	<b>Nominal Weighted Composition</b>		<b>Duration Weighted Composition</b>	
	<b>Portfolio</b>	<b>Customized Benchmark</b>	<b>Portfolio</b>	<b>Customized Benchmark</b>
<b>Yield to Maturity</b>	<b>1.86%</b>	<b>1.83%</b>		
Average Coupon	<b>3.33%</b>	2.88%		
Duration	<b>4.51 years</b>	4.51 years		
Average Maturity	<b>6.15 years</b>	6.49 years		
<b>Quality Breakdown</b>				
U.S. Treasury	<b>28%</b>	47%	<b>50%</b>	63%
U.S. Govt Agency	<b>68</b>	54	<b>50</b>	37
Aaa	<b>4</b>	0	<b>0</b>	0
Aa	<b>0</b>	0	<b>0</b>	0
A	<b>0</b>	0	<b>0</b>	0
Baa	<b>0</b>	0	<b>0</b>	0
Below Baa	<b>0</b>	0	<b>0</b>	0
	<b>100%</b>	100%	<b>100%</b>	100%
<b>Sector Breakdown</b>				
U.S. Treasury	<b>28%</b>	47%	<b>50%</b>	63%
U.S. Govt Agency Debentures	<b>2</b>	3	<b>1</b>	3
Agency Pass-Throughs	<b>44</b>	50	<b>34</b>	34
Agency CMOs	<b>3</b>	0	<b>2</b>	0
Agency CMBS	<b>19</b>	0	<b>13</b>	0
Cash	<b>4</b>	0	<b>0</b>	0
	<b>100%</b>	100%	<b>100%</b>	100%
Number of Issues	<b>93</b>	1,160		
Market Value	<b>\$26,537,171</b>			

# Bay County Employees' Retirement System

Gross Returns as of March 31, 2016

	First Quarter	1 Year	3 Years	5 Years	7 Years	Since Inception (April 2006)
<b>Portfolio Gross of Fees</b>	2.85%	2.67%	2.46%	3.58%	3.71%	4.86%
<b>Customized Benchmark</b>	2.55%	2.39%	2.40%	3.33%	3.36%	4.69%

The performance is presented on a cumulative basis and does not reflect the deduction of investment advisory fees. Return would be reduced by advisory fee and other fees such as custodial expenses. The maximum fee found in Baird Advisors form ADV is 30 basis points. All returns are calculated on a time weighted, total return basis. The results shown should not be considered representative of future investment returns. The 50% Barclays Government & 50% Barclays MBS Index is an unmanaged portfolio of specific securities. The portfolio does not invest in all the securities traded in the index. Direct investment in the index is not available. Client should review all account statements provided by its custodian and compare those account statements to any account statement provided by Baird Advisors. Baird Advisors relies on securities valuations provided by client's custodian for purposes of performance reports.

The Baird Advisors Brochure, which serves as a substitute for Form ADV Part II, is available upon request.

# Bay County Employees' Retirement System

	<b>Fixed Income Portfolio Gross of Fees</b>	<b>Customized Benchmark</b>
<b>2006 (Apr-Dec)</b>	5.04%	4.85%
<b>2007</b>	7.20%	7.78%
<b>2008</b>	9.13%	10.36%
<b>2009</b>	3.72%	1.79%
<b>2010</b>	5.63%	5.46%
<b>2011</b>	7.91%	7.62%
<b>2012</b>	3.05%	2.32%
<b>2013</b>	-2.59%	-2.00%
<b>2014</b>	5.79%	5.50%
<b>2015</b>	1.31%	1.18%
<b>2016 1<sup>st</sup> Qtr.</b>	2.85%	2.55%
<b>Since Inception</b>		
<b>Cumulative Return</b>	<b>60.75%</b>	<b>58.12%</b>
<b>Annualized Return</b>	<b>4.86%</b>	<b>4.69%</b>

The performance is presented on a cumulative basis and does not reflect the deduction of investment advisory fees. Return would be reduced by advisory fee and other fees such as custodial expenses. The maximum fee found in Baird Advisors form ADV is 30 basis points. All returns are calculated on a time weighted, total return basis. The results shown should not be considered representative of future investment returns. The 50% Barclays Government & 50% Barclays MBS Index is an unmanaged portfolio of specific securities. The portfolio does not invest in all the securities traded in the index. Direct investment in the index is not available. Client should review all account statements provided by its custodian and compare those account statements to any account statement provided by Baird Advisors. Baird Advisors relies on securities valuations provided by client's custodian for purposes of performance reports.

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# Benefits for Bay County Employees' Retirement System

- Long-term relationships focused on client and direct communication
- Experienced management team implementing proven investment discipline
  - Structured, risk controlled process
  - No derivatives, no non-\$ currency exposure, no leverage
  - Focus on **bottom-up** added value from sector allocation and security selection
- Total focus on fixed income management
- Culture and resources key to future success
- Importance of the relationship to Baird Advisors

**We believe our team, our entrepreneurial environment and substantial resources enable us to provide our clients with the best possible fixed income investment management services available**