

**ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
BOARD OF RETIREMENT
2223 E. WELLINGTON AVENUE, SUITE 100
SANTA ANA, CALIFORNIA**

**INVESTMENT COMMITTEE MEETING
August 23, 2017**

MINUTES

Attendance was as follows:

Present: Chris Prevatt, Chair; Wayne Lindholm, Vice Chair; Roger Hilton; Eric Gilbert; Russell Baldwin; Shawn Dewane; David Ball; Frank Eley; and Shari Freidenrich

Absent: Charles Packard

Also Present: Steve Delaney, Chief Executive Officer; Molly Murphy, CFA, Chief Investment Officer; Shanta Chary, Director of Investment Operations; David Beeson, Investment Officer; Stina Walander-Sarkin, Investment Analyst; Gina Ratto, Chief Legal Officer; Anthony Beltran, Visual Technician; and Julius Cuaresma, Recording Secretary

Meketa Investment Group: Stephen McCourt, CFA; John Humphries; and Steve Hartt
Pension Consulting Alliance: Allan Emkin; and Collin Bebee, CFA

The Chair called the meeting to order at 9:05 a.m. Mr. Eley led the Pledge of Allegiance.

CONSENT AGENDA

All matters on the Consent Agenda are to be approved by one action unless a Board Member or a member of the public requests separate action on a specific item.

Mr. Ball and Ms. Murphy discussed C-3 Meketa Economic Outlook.

A **motion** was made by Mr. Hilton and **seconded** by Mr. Eley to approve the Consent Agenda. The **motion carried unanimously.**

C-1 COMMITTEE MEETING:

Approval of Meeting and Minutes

Investment Committee Meeting

July 27, 2017

Investment Manager Monitoring Subcommittee Meeting

August 3, 2017

Recommendation: Authorize meetings and approve minutes.

C-2 INVESTMENT REPORTS

Recommendation: Receive and file.

Recommendation: Receive and file.

*** * * * * END OF CONSENT AGENDA * * * * ***

INDIVIDUAL ITEMS AGENDA

I-1 INDIVIDUAL ACTION ON ANY ITEM TRAILED FROM THE CONSENT AGENDA

I-2 CIO COMMENTS

Presentation by Molly Murphy, CFA, CIO, OCERS

Ms. Murphy presented an update on OCERS' real estate investments, including a discussion on labor law compliance.

Ms. Murphy provided an update on EnerVest Fund XII.

I-3 PORTFOLIO ACTIVITY REPORT

Presentation by Molly Murphy, CFA, CIO & David Beeson, IO, OCERS

Mr. Beeson presented the portfolio activity report, including the total fund overview, subscriptions and redemptions, as well as the asset allocation for July 2017.

Mr. Beeson provided an update on OCERS' performance.

Ms. Freidenrich and Mr. Beeson discussed recent cash flows, particularly as it relates to proceeds from OCERS' Absolute Return portfolio.

Ms. Freidenrich and Ms. Murphy discussed OCERS' asset allocation targets and ranges.

Mr. Ball and Mr. Beeson discussed the liquidation of OCERS' REIT program.

A **motion** was made by Mr. Ball and **seconded** by Mr. Baldwin to receive and file I-3. The **motion carried unanimously.**

I-4 2nd QUARTER 2017 PORTFOLIO RISK DISCUSSION

Presentation by Allan Emkin & Colin Bebee, CFA, PCA

Mr. Emkin and Mr. Bebee presented PCA's 2nd Quarter 2017 Portfolio Risk Discussion for OCERS' portfolio.

Mr. Emkin discussed the importance of portfolio diversification.

Mr. Emkin stated that PCA's report focuses on top-down risk, including, growth risk and liquidity risk, rather than manager level risk.

Mr. Emkin discussed the difference between OCERS' capital portfolio dollar allocation and the actual risk allocation.

Mr. Emkin presented the drivers of fixed income risk and noted that the systematic risk of changing rates is not as dominant as credit risk, foreign exchange risk, and emerging market equity risk.

Mr. Emkin remarked that currency risk is uncompensated risk due to the rationale that currency has a zero expected return over the long-term.

Mr. Prevatt and Mr. Emkin discussed what OCERS can and should do in light of knowing and understanding the drivers of OCERS' risk.

Mr. Emkin suggested that OCERS review and discuss OCERS' foreign exchange risk at the overall portfolio level.

Mr. Ball discussed the original rationale behind OCERS' foreign exchange hedge transactions.

Mr. Emkin noted that the pricing mechanism of private equity masks its true volatility.

Mr. Emkin discussed the need for trustees to understand OCERS' bets, and potential ways on how to diversify those bets.

Mr. Emkin discussed the recent performance of long treasury bonds. He also discussed that there will be further discussion on this asset class at the Strategic Annual Planning Meeting, particularly with regards to Risk Mitigation Strategies (RMS).

Mr. Ball and Mr. Emkin discussed the interest rate movements in various market regimes, particularly in periods of market crises.

Mr. Emkin explained that long treasury bonds is not a panacea, as there have been outlier periods where rates rose during equity drawdown periods.

Mr. Ball expressed agreement with the process that OCERS is heading in terms of being positioned in long treasury bonds.

Mr. Eley and Mr. Emkin discussed various fixed income systematic risks and what kind and size allocation PCA prefers in a rising rate environment.

Mr. Dewane and Mr. Emkin discussed key issues from PCA's presentation, including: the positive correlation of risk and returns; OCERS' portfolio may be less diversified than intended or wanted; OCERS has non-quantifiable risk due to the natural limitations in pricing private equity; and the portfolio's currency risk is unmanaged.

Mr. Dewane asked that those respective key issues be presented at the upcoming Strategic Annual Planning Meeting. He also asked that OCERS set Board policy to address those issues in order to maximize the portfolio's risk-adjusted returns.

Ms. Murphy voiced agreement and suggested that Mr. Dewane is expressing his preference in moving towards a risk budget framework.

Mr. Baldwin and Mr. Emkin discussed the quality of the various asset baskets in OCERS' portfolio. They also discussed OCERS' energy basket, specifically as it relates to sustainability.

Mr. Prevatt outlined recommended actionable items from PCA's presentation, specifically that the Committee set strategic policy that gives direction to staff and consultants at the upcoming Strategic Annual Planning Meeting

Ms. Murphy observed that the Committee, consultants, and staff appear to be on the same page and heading towards the same goal. She noted that staff and consultants would bring a number of strategies that could be within the RMS allocation at the Strategic Annual Planning Meeting.

A **motion** was made by Mr. Hilton and **seconded** by Mr. Baldwin to receive and file I-4. The **motion carried unanimously.**

The Committee recessed at 10:12 a.m.

The Committee reconvened at 10:30 a.m.

I-5 2nd QUARTER 2017 PORTFOLIO EVALUATION REPORT
Presentation by Stephen McCourt, CFA, Meketa

Mr. McCourt initiated OCERS' 2nd Quarter 2017 Portfolio Evaluation Report by first presenting specific slides from the consent agenda C-3 Meketa Economic Outlook: 1) Global Central Bank intervention in the aftermath of the Global Financial Crisis; 2) Trade Weighted U.S. Dollar index over the past 20 years.

Ms. Freidenrich and Mr. McCourt discussed the costs and benefits of a strengthening (weakening) U.S. dollar, including its impact upon International Developed Equities in (non) dollar-denominated share classes.

Mr. McCourt discussed the one-year performance of public and private equities relative to their respective benchmarks.

Mr. McCourt discussed positive and negative outliers at the manager level.

Mr. Ball and Mr. McCourt discussed the present late-stage cycle of the credit markets.

Mr. Dewane suggested, ahead of the Strategic Annual Planning Meeting, a possible re-organization of Meketa's presentation to focus on timely, relevant, and actionable items for the Committee.

Ms. Murphy expressed agreement, suggesting there be more deliberate focus on what is actionable versus what is data.

Mr. Ball and Mr. McCourt discussed benchmarking.

A **motion** was made by Mr. Dewane and **seconded** by Mr. Hilton to receive and file I-5. The **motion carried unanimously.**

I-6 2016 ANNUAL FEE REPORT

Presentation by Molly Murphy, CFA, CIO & Stina Walander-Sarkin, IA, OCERS

Ms. Murphy noted the similarities and differences of the 2016 Annual Fee Report relative to prior Annual Fee Reports. She also noted that this year's report includes peer group comparison data from Greenwich Associates.

Ms. Murphy indicated this Fee Report continues to be a work in progress, and noted that next year's report will be different due to the requirements of AB 2833.

Ms. Walander-Sarkin provided an overview of the 2016 Annual Fee Report. She also discussed trends and outliers.

Ms. Freidenrich and Ms. Walander-Sarkin discussed outlier performance fees, particularly relative to various tailwind/headwind periods in the real estate and energy markets.

Ms. Murphy discussed OCERS' fees relative to other public pension plans, including fees from OCERS' equity allocation.

Ms. Murphy discussed the importance of performance fees with hurdles.

Ms. Freidenrich, Ms. Murphy, and Ms. Walander-Sarkin discussed the inherent limitations in the peer group survey data.

Mr. Ball, Ms. Freidenrich, and Ms. Murphy discussed the goal of decomposing performance and fees relative to alpha and beta.

Mr. Ball and Ms. Walander-Sarkin discussed real estate fees incurred from OCERS' real estate investments relative to performance.

Ms. Murphy discussed performance fees in relation to: hurdles and high watermarks; active versus passive investments; and liquid versus illiquid assets.

Ms. Walander-Sarkin and Ms. Murphy remarked upon the larger amount of fees from OCERS' private equity portfolio due to investing through fund-of-funds.

Mr. Hilton, Ms. Murphy, and Mr. Emkin discussed AB 2833, the Institutional Limited Partners Association, and the overall trend of LPs seeking improved fee transparency from GPs.

Mr. Eley and Ms. Murphy discussed the costs and benefits of OCERS' P4 Private Equity allocation.

Mr. Ball commented on the difficulty in measuring beta in private markets.

Mr. Stephen Wontrobski, member of the public, addressed the Committee about fees and performance claw backs.

Mr. Eley and Ms. Murphy discussed performance claw backs in various asset classes and strategies.

A **motion** was made by Mr. Dewane and **seconded** by Mr. Eley to receive and file I-6. The **motion carried unanimously.**

I-8 1st QUARTER 2017 REAL ESTATE PERFORMANCE REPORT

Presentation by Stephen McCourt, CFA & John Humphries, Meketa

Mr. McCourt and Mr. Humphries presented OCERS' 1st Quarter 2017 Real Estate Performance Report.

Mr. Humphries provided a quantitative and qualitative commentary on various real estate markets. He also discussed performance outliers at the manager level.

Mr. McCourt remarked that the actionable task going forward is confirming (disaffirming) the real estate policy direction, particularly as it relates to the portfolio's investment strategy composition i.e., core versus value-add.

Mr. Ball and Mr. McCourt discussed displaying allocation percentages of OCERS' core versus value-add investments on Meketa's Real Estate Performance Report.

Mr. Ball and Mr. McCourt discussed the costs and benefits of open-ended and closed-end funds.

A **motion** was made by Mr. Hilton and **seconded** by Mr. Eley to receive and file I-8. The **motion carried unanimously.**

The Committee recessed at 11:47 a.m.

The Committee reconvened at 11:50 a.m.

I-7 PRIVATE EQUITY REVIEW

Presentation by Stephen McCourt, CFA & Steve Hartt, Meketa

Mr. Hartt provided a summary of OCERS' private equity program through the 1st quarter of 2017, including a performance and pacing plan update. He discussed changes in the portfolio on a quarter-over-quarter basis.

Mr. Prevatt and Mr. McCourt discussed OCERS' target private equity allocation.

Mr. Prevatt and Mr. McCourt discussed Meketa's recommended pacing plan in order to achieve the 8% target allocation.

Mr. Prevatt, Mr. McCourt, and Ms. Murphy discussed the prospective private equity portfolio.

A **motion** was made by Mr. Ball and **seconded** by Mr. Dewane to receive and file I-7. The **motion carried unanimously.**

*******END OF INDIVIDUAL ITEMS AGENDA*******

PUBLIC COMMENTS: At this time members of the public may address the Committee of Retirement regarding any items within the subject matter jurisdiction of the Committee, provided that no action may be taken on non-agendized items unless authorized by law.

Mr. Stephen Wontrobski, member of the public, addressed the Committee about pension contributions.

COMMITTEE MEMBER/CEO/CIO/STAFF/CONSULTANT COMMENTS

Mr. Delaney discussed Segal Consulting's tri-annual study.

Mr. Delaney discussed PCA's recent involvement as OCERS' enhanced consultant and their prospective role now that OCERS has hired a CIO.

Mr. Emkin commented upon fees. He projected a reduction next year due to hedge fund redemptions and OCERS actively moving those proceeds into passive investments. He also commented upon the costs and benefits of open-end and closed-end real estate investments. He also remarked upon the prudence in migrating away from the private equity fund-of-fund model and instead, investing directly. However, he also noted that fund-of-funds could capitalize on pricing dislocations that can occur in the private equity secondary market.

COUNSEL COMMENTS

None

ADJOURNMENT: The Chair adjourned the meeting at 12:09 p.m.

Submitted by:



Steve Delaney
Secretary to the Committee

Approved by:



Chris Prevatt
Chair