AGENDA

Date: January 6, 2023

The regular meeting of the Dallas Police and Fire Pension System Board of Trustees will be held at **8:30 a.m. on Thursday, January 12, 2023, in the Second Floor Board Room at 4100 Harry Hines Boulevard, Dallas, Texas and via telephone conference for audio at 214-271-5080 access code 588694 or Toll-Free (US & CAN): 1-800-201-5203 and Zoom meeting for visual https://us02web.zoom.us/j/84595900972?pwd=bHdGZ3kyVjZqa2dpak53RytDSTVQdz09 Passcode: 022915.** Items of the following agenda will be presented to the Board:

A. TRUSTEES

Welcome Reappointed Trustees

B. MOMENT OF SILENCE

C. CONSENT AGENDA

1. Approval of Minutes

Regular meeting of December 8, 2022

2. **Approval of Refunds of Contributions for the Month of December 2022**

3. **Approval of Activity in the Deferred Retirement Option Plan (DROP) for January 2023**

4. **Approval of Survivor Benefits**

5. **Approval of Service Retirements**

6. **Spouse Wed After Retirement (SWAR)**

7. **Approval of Payment of DROP Revocation Buyback Contributions**

8. **Approval of Payment of Military Leave Contributions**

D. DISCUSSION AND POSSIBLE ACTION REGARDING ITEMS FOR INDIVIDUAL CONSIDERATION

1. **Report on Professional Service Provider Meeting**

2. **Monthly Contribution Report**

3. **Board approval of Trustee education and travel**

   a. Future Education and Business-related Travel
   b. Future Investment-related Travel

4. **Portfolio Update**

5. **Report on the Investment Advisory Committee Meeting**

6. **Private Asset Cash Flow Projection Update**

   Portions of the discussion under this topic may be closed to the public under the terms of Section 551.072 of the Texas Government Code.

7. **Possible Amendment to the Investment Policy Statement**

8. **Consultant Search Process**

9. **Legal issues - In accordance with Section 551.071 of the Texas Government Code, the Board will meet in executive session to seek and receive the advice of its attorneys about pending or contemplated litigation or any other legal matter in which the duty of the attorneys to DPFP and the Board under the Texas Disciplinary Rules of Professional Conduct clearly conflicts with Texas Open Meeting laws.**

10. Executive Director Performance Evaluation

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.074 of the Texas Government Code.

E. BRIEFING ITEMS

1. Public Comment

2. Executive Director's report

a. Associations' newsletters
- NCPERS Monitor (January 2023)
- NCPERS PERSist (Winter 2023)

b. Open Records

c. Staffing Update

The term "possible action" in the wording of any Agenda item contained herein serves as notice that the Board may, as permitted by the Texas Government Code, Section 551, in its discretion, dispose of any item by any action in the following non-exclusive list: approval, disapproval, deferral, table, take no action, and receive and file. At the discretion of the Board, items on this agenda may be considered at times other than in the order indicated in this agenda.

At any point during the consideration of the above items, the Board may go into Closed Executive Session as per Texas Government Code, Section 551.071 for consultation with attorneys, Section 551.072 for real estate matters, Section 551.074 for personnel matters, and Section 551.078 for review of medical records.

Memorandum

CITY OF DALLAS

DATE December 15, 2022

TO Bilierae Johnson, City Secretary
Kelly Gottschalk, Executive Director, Dallas Police and Fire Pension System

SUBJECT Appointments of Dallas Police and Fire Pension System Trustees

Dear Madam Secretary and Ms. Gottschalk:

I am reappointing following individuals to serve 3-year terms on the Dallas Police and Fire Pension System Board of Trustees:

- Michael Brown
- Steve Idoux
- Mark Malveaux

I am also appointing the following individual to serve a 2-year term on the Board.

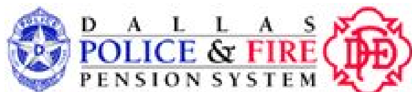
- Tina Hernandez

Should you have any questions, please do not hesitate to reach out.

Sincerely,

Eric Johnson
Mayor

c: T.C. Broadnax, City Manager
Chris Caso, City Attorney
Mark Swann, City Auditor



MOMENT OF SILENCE

In memory of our Members and Pensioners who recently passed away

NAME	ACTIVE/ RETIRED	DEPARTMENT	DATE OF DEATH
Thomas K. Elliott	Retired	Police	Nov. 28, 2022
Joe A. Pierce	Retired	Fire	Nov. 28, 2022
Robert E. Coffee	Retired	Police	Dec. 1, 2022
James D. Moses	Retired	Police	Dec. 2, 2022
Josias Prelow	Retired	Police	Dec. 2, 2022
David S. Hernandez	Retired	Police	Dec. 9, 2022
Duane H. Boy	Retired	Police	Dec. 26, 2022

Regular Board Meeting –Thursday, January 12, 2023

Dallas Police and Fire Pension System
Thursday, December 8, 2022
8:30 a.m.
4100 Harry Hines Blvd., Suite 100
Second Floor Board Room
Dallas, TX

Regular meeting, Nicholas A. Merrick, Chairman, presiding:

ROLL CALL

Board Members

Present at 8:34 a.m.	Nicholas A. Merrick, William F. Quinn, Armando Garza, Michael Brown, Kenneth Haben, Steve Idoux (by telephone), Nancy Rocha, Anthony Scavuzzo (by telephone), Marcus Smith
Absent:	Mark Malveaux
Staff	Kelly Gottschalk, Josh Mond, Brenda Barnes, Ryan Wagner, Michael Yan, John Holt, Nien Nguyen, Milissa Romero
Others	Jill Svoboda, Matt Liu, Leandro Festino, Steve Hartt, Neal T. "Buddy" Jones, Eddie Solis, James Elliston, Michael Taglienti, Rick Salinas, Kristi Walters, Sheri Kowalski, Colin Kowalski (by telephone)

* * * * * * * *

The Regular meeting was called to order at 8:34 a.m.

* * * * * * * *

A. MOMENT OF SILENCE

The Board observed a moment of silence in memory of retired police officers Thomas R. Gregory, Donald P. Williams, and retired firefighters Billy R. Pemberton, Steve G. Perry, Jr., Don Gentry.

No motion was made.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

B. CONSENT AGENDA

1. **Approval of Minutes**

   a. Required Public meeting #2 of November 10, 2022
   b. Regular meeting of November 10, 2022

2. **Approval of Refunds of Contributions for the Month of November 2022**

3. **Approval of Activity in the Deferred Retirement Option Plan (DROP) for December 2022**

4. **Approval of Estate Settlements**

5. **Approval of Survivor Benefits**

6. **Approval of Service Retirements**

7. **Approval of Alternate Payee Benefits**

8. **Approval of Payment of Military Leave Contributions**

9. **Approval of Payment of DROP Revocation Buyback Contributions**

After discussion, Mr. Quinn made a motion to approve the minutes of the Required Public meeting and the Regular meeting of November 10, 2022. Mr. Haben seconded the motion, which was unanimously approved by the Board.

After discussion, Mr. Haben made a motion to approve the remaining items on the Consent Agenda, subject to the final approval of the staff. Mr. Smith seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

C. DISCUSSION AND POSSIBLE ACTION REGARDING ITEMS FOR INDIVIDUAL CONSIDERATION

1. 2021 Financial Audit

Jill Svoboda, Partner and Matt Liu, Audit Senior Manager, representatives from BDO, DPFP's independent audit firm, were present to discuss the results of their audit for the year ended December 31, 2021.

After discussion, Mr. Haben made a motion to approve issuance of the 2021 audit report, subject to final review and approval by BDO and the Executive Director. Mr. Quinn seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

2. 2021 Annual Comprehensive Financial Report

Staff presented a draft of the 2021 Annual Comprehensive Financial Report.

After discussion, Mr. Garza made a motion to authorize the Executive Director to issue the 2021 Annual Comprehensive Financial Report upon finalization. Ms. Rocha seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

3. Report on Audit Committee

The Audit Committee met with representatives of BDO on December 8, 2022. The Committee Chair commented on the Committee's observations and advice and noted that BDO had no negative comments regarding their dealings with staff

No motion was made.

* * * * * * * *

4. Hillco - Legislative Preview for 2023

Neal T. "Buddy" Jones, and Eddie Solis, representatives from HillCo Partners, DPFP's legislative consultants, were present to discuss the upcoming legislative session.

No motion was made.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

5. Monthly Contribution Report

The Executive Director reviewed the Monthly Contribution Report.

No motion was made.

* * * * * * * *

6. Board approval of Trustee education and travel

a. Future Education and Business-related Travel
b. Future Investment-related Travel

The Board and staff discussed future Trustee education. There was no future investment-related travel scheduled.

No motion was made.

* * * * * * * *

7. Portfolio Update

Investment staff briefed the Board on recent events and current developments with respect to the investment portfolio.

No motion was made.

* * * * * * * *

8. Private Market Considerations

Leandro Festino, Managing Principal and Steve Hartt, Managing Principal of Meketa Investment Group reviewed their private market capabilities, outlined various private market investment program models and discussed high level considerations that need to be addressed prior to making new private market commitments.

No motion was made.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

9. Third Quarter 2022 Investment Performance Analysis and Second Quarter 2022 Private Markets & Real Assets Review

Leandro Festino, Managing Principal of Meketa and the Investment Staff reviewed the Third Quarter 2022 Investment Performance Analysis and Second Quarter 2022 Private Markets & Real Assets.

No motion was made.

* * * * * * * *

10. Funding Policy Benchmark

The DPFP Funding Policy requires the Board to notify the City of Dallas upon receipt of two actuarial valuations showing the actual contribution varies from the Actuarially Determined Contribution by more than 2%. This has occurred with the January 1, 2022 valuation. The Funding Policy also requires in that situation, upon a two-thirds vote of the Board, that the Board recommend an increase in City contribution rates.

The Board went into closed executive session at 11:12 a.m.

The meeting was reopened at 12:07 p.m.

After discussion, Mr. Quinn made a motion to authorize the Executive Director on behalf of the Board to (i) send the required notice under the Funding Policy to the City of Dallas and (ii) recommend an increase in City contribution rates. Mr. Smith seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

11. Legal issues - In accordance with Section 551.071 of the Texas Government Code, the Board will meet in executive session to seek and receive the advice of its attorneys about pending or contemplated litigation or any other legal matter in which the duty of the attorneys to DPFP and the Board under the Texas Disciplinary Rules of Professional Conduct clearly conflicts with Texas Open Meeting laws.

The Board went into closed executive session at 11:12 a.m.

The meeting was reopened at 12:07 p.m.

After discussion, Mr. Haben made a motion to authorize the Executive Director, with the approval of the Chairman, to consummate a settlement of the pending lawsuit involving Buck Consultants. Ms. Rocha seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

12. Closed Session - Board Serving as Medical Committee

a. Disability application 2022-3
b. Disability application 2022-4

The Board went into closed executive session at 11:12 a.m.

The meeting was reopened at 12:07 p.m.

The Executive Director reviewed two disability applications and materials with the Board.

a. After discussion, Mr. Garza made a motion to authorize the Executive Director the authority to grant an on-duty disability for applicant 2022-3 if the independent medical report concludes the member is disabled and granted an off-duty disability for applicant 2022-4. Mr. Haben seconded the motion, which was unanimously approved by the Board.

b. After discussion, Mr. Garza made a motion to grant disability retirement for applicant 2022-4 in accordance with Section 6.03 of Article 6243a-1. Mr. Quinn seconded the motion, which was unanimously approved by the Board.

* * * * * * * *

13. Executive Director Performance Evaluation

The Board went into closed executive session at 11:12 a.m.

The meeting was reopened at 12:07 p.m.

The Board met with the Executive Director to review performance and provide recommendations concerning yearly objectives, goals, and performance.

No motion was made.

* * * * * * * *

D. BRIEFING ITEMS

1. Public Comments

Prior to commencing items for Board discussion and deliberation, the Board received public comments during the open forum.

* * * * * * * *

DRAFT

Regular Board Meeting
Thursday, December 8, 2022

2. Executive Director's report

a. Associations' newsletters
- NCPERS Monitor (December 2022)

b. Open Records
c. Board Meeting Schedule

The Executive Director's report was presented.

* * * * * * * *

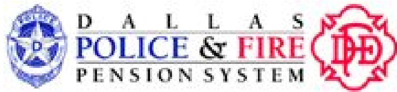
Ms. Gottschalk stated that there was no further business to come before the Board. On a motion by Mr. Haben and a second by Mr. Quinn the meeting was adjourned at 12:10 p.m.

____
Nicholas A. Merrick
Chairman

ATTEST:

____
Kelly Gottschalk
Secretary

DRAFT



DISCUSSION SHEET

ITEM #D1

Topic: **Report on Professional Service Provider Meeting**

Discussion: According to the Committee Policy and Procedure, the Professional Services Committee is responsible for meeting privately with the external service providers, without DPFP staff present, at a minimum on an annual basis. The purpose of such a meeting is to provide a forum for the service provider to provide candid comments to the Professional Services Committee. The policy provides that the Committee report to the Board any material comments and recommend to the Board any appropriate actions needed as a result of the meeting with the service provider.

The Professional Service Committee met with Chuck Campbell of Jackson Walker LLP on January 12, 2023.

Staff Recommendation: The Professional Services Committee shall **report** to the Board any material comments and **recommend** to the Board any appropriate actions needed as a result of the meeting with Chuck Campbell of Jackson Walker LLP.

DISCUSSION SHEET

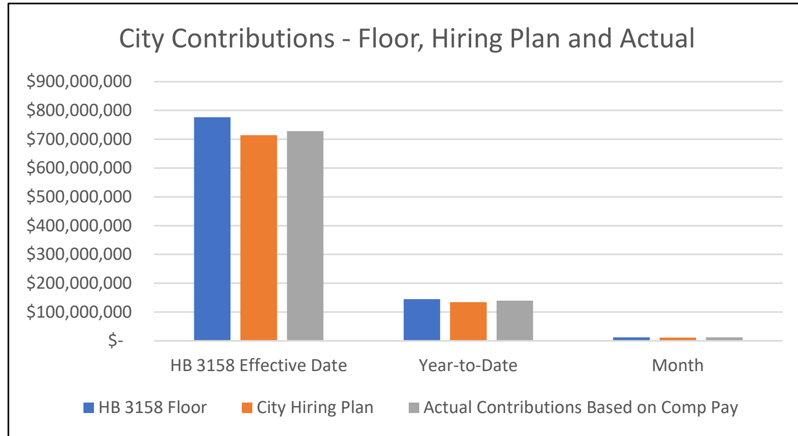
ITEM #D2

Topic: **Monthly Contribution Report**

Discussion: Staff will review the Monthly Contribution Report.

Regular Board Meeting – Thursday, January 12, 2023

Contribution Tracking Summary - January 2023 (November 2022 Data)



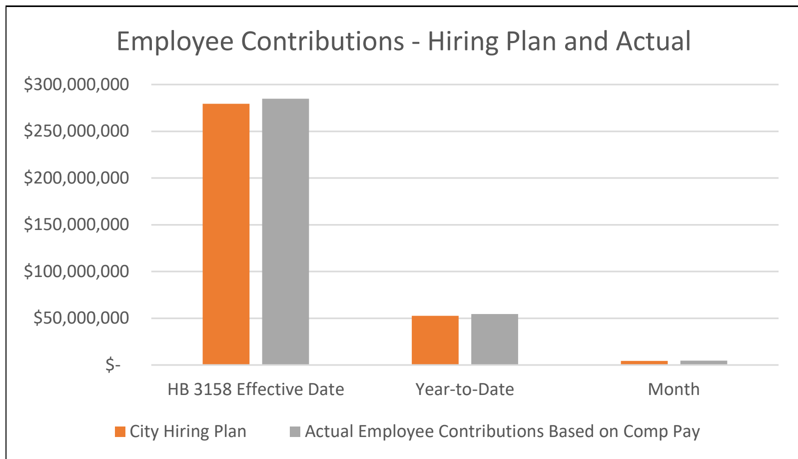
Actual Comp Pay was 102% of the Hiring Plan estimate since the effective date of HB 3158.

In the most recent month Actual Comp Pay was 105% of the Hiring Plan estimate and 97% of the Floor amount.

The Hiring Plan Comp Pay estimate increased by 3.43% in 2022. The Floor increased by 2.74%.

Through 2024 the HB 3158 Floor is in place so there is no City Contribution shortfall.

The combined actual employees was 185 less than the Hiring Plan for the pay period ending December 6, 2022. Fire was over the estimate by 71 fire fighters and Police under by 256 officers.



Employee contributions exceeded the Hiring Plan estimate for the month, the year and since inception.

There is no Floor on employee contributions.

Contribution Summary Data

City Contributions

Nov-22	**Number of Pay Periods Beginning in the Month**	**HB 3158 Floor**	**City Hiring Plan**	**Actual Contributions Based on Comp Pay**	**Additional Contributions to Meet Floor Minimum**	**Comp Pay Contributions as a % of Floor Contributions**	**Comp Pay Contributions as a % of Hiring Plan Contributions**
Month	2	$ 12,086,000	$ 11,199,231	$ 11,774,712	$ 311,288	97%	105%
Year-to-Date		$ 145,032,000	$ 134,390,769	$ 139,693,328	$ 5,338,722	96%	104%
HB 3158 Effective Date		$ 777,135,000	$ 713,911,154	$ 728,506,152	$ 48,702,605	94%	102%

Due to the Floor through 2024, there is no cumulative shortfall in City Contributions
Does not include the flat $13 million annual City Contribution payable through 2024.
Does not include Supplemental Plan Contributions.

Employee Contributions

Nov-22	**Number of Pay Periods Beginning in the Month**	**City Hiring Plan**	**Actual Employee Contributions Based on Comp Pay**	**Actual Contribution Shortfall Compared to Hiring Plan**	**Actuarial Valuation Contribution Assumption**	**Actual Contributions as a % of Hiring Plan Contributions**	**Actual Contributions as a % of Actuarial Val Assumption**
Month	2	$ 4,382,308	$ 4,585,197	$ 202,889	$ 4,236,924	105%	108%
Year-to-Date		$ 52,587,692	$ 54,626,375	$ 2,038,683	$ 50,843,088	104%	107%
HB 3158 Effective Date		$ 279,356,538	$ 284,875,287	$ 5,518,749	$ 272,502,742	102%	105%

Potential Earnings Loss from the Shortfall based on Assumed Rate of Return $ (142,373)

Does not include Supplemental Plan Contributions.

Reference Information

City Contributions: HB 3158 Bi-weekly Floor and the City Hiring Plan Converted to Bi-weekly Contributions

	HB 3158 Bi-weekly Floor	City Hiring Plan-Bi-weekly	HB 3158 Floor Compared to the Hiring Plan	Hiring Plan as a % of the Floor	% Increase/ (decrease) in the Floor	% Increase/ (decrease) in the Hiring Plan
2017	$ 5,173,000	$ 4,936,154	$ 236,846	95%		
2018	$ 5,344,000	$ 4,830,000	$ 514,000	90%	3.31%	-2.15%
2019	$ 5,571,000	$ 5,082,115	$ 488,885	91%	4.25%	5.22%
2020	$ 5,724,000	$ 5,254,615	$ 469,385	92%	2.75%	3.39%
2021	$ 5,882,000	$ 5,413,846	$ 468,154	92%	2.76%	3.03%
2022	$ 6,043,000	$ 5,599,615	$ 443,385	93%	2.74%	3.43%
2023	$ 5,812,000	$ 5,811,923	$ 77	100%	-3.82%	3.79%
2024	$ 6,024,000	$ 6,024,231	$ (231)	100%	3.65%	3.65%

The HB 3158 Bi-weekly Floor ends after 2024

Employee Contributions: City Hiring Plan and Actuarial Val. Converted to Bi-weekly Contributions

		City Hiring Plan Converted to Bi-weekly Employee Contributions	Actuarial Valuation Assumption Converted to Bi-weekly Employee contributions	Actuarial Valuation as a % of Hiring Plan
2017		$ 1,931,538	$ 1,931,538	100%
2018		$ 1,890,000	$ 1,796,729	95%
2019		$ 1,988,654	$ 1,885,417	95%
2020		$ 2,056,154	$ 2,056,154	100%
2021		$ 2,118,462	**$ 2,118,462**	100%
2022		$ 2,191,154	**$ 2,191,154**	100%
2023		$ 2,274,231	**$ 2,274,231**	100%
2024		$ 2,357,308	**$ 2,357,308**	100%

The information on this page is for reference. The only numbers on this page that may change before 2025 are the Actuarial Valuation Employee Contributions Assumptions for the years 2020-2024 and the associated percentage.

Reference Information - Actuarial Valuation and GASB 67/68 Contribution Assumptions

Actuarial Assumptions Used in the Most Recent Actuarial Valuation - These assumptions will be reevaluated annually & may change.

City Contributions are based on the Floor through 2024, the Hiring Plan from 2025 to 2037, after 2037 an annual growth rate of 2.75% is assumed

Employee Contributions for 2018 are based on the 2017 actual employee contributions inflated by the growth rate of 2.75% and the Hiring Plan for subsequent years until 2038, when the 2037 Hiring Plan is increased by the 2.75 growth rate for the next 10 years

Actuarial/GASB Contribution Assumption Changes Since the Passage of HB 3158

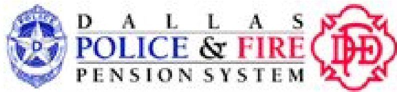
	Actuarial Valuation	GASB 67/68
YE 2017 (1/1/2018 Valuation)		
2018 Employee Contributions Assumption - based on 2017 actual plus growth rate not the Hiring Plan Payroll	$ (2,425,047)	*
2019 Estimate (1/1/2019 Valuation)		
2019 Employee Contribution Assumption	$ 9,278	*

**90% of Hiring Plan was used for the Cash Flow Projection for future years in the 12/31/2017 GASB 67/68 calculation. At 12-31-17, 12-31-18 and 12-31-2019 this did not impact the pension liability or the funded percentage.*

The information on this page is for reference. It is intended to document contribution related assumptions used to prepare the Actuarial Valuation and changes to those assumptions over time, including the dollar impact of the changes. Contribution changes impacting the GASB 67/68 liability will also be included.

City Hiring Plan - Annual Computation Pay and Numbers of Employees						
	Computation Pay			**Number of Employees**		
Year	**Hiring Plan**	**Actual**	**Difference**	**Hiring Plan**	**Actual EOY**	**Difference**
2017	$ 372,000,000	Not Available	Not Available	5,240	4,935	(305)
2018	$ 364,000,000	$ 349,885,528	$ (14,114,472)	4,988	4,983	(5)
2019	$ 383,000,000	$ 386,017,378	$ 3,017,378	5,038	5,104	66
2020	$ 396,000,000	$ 421,529,994	$ 25,529,994	5,063	4,988	(75)
2021	$ 408,000,000	$ 429,967,675	$ 21,967,675	5,088	4,958	(130)
2022	$ 422,000,000			5,113		
2023	$ 438,000,000			5,163		
2024	$ 454,000,000			5,213		
2025	$ 471,000,000			5,263		
2026	$ 488,000,000			5,313		
2027	$ 507,000,000			5,363		
2028	$ 525,000,000			5,413		
2029	$ 545,000,000			5,463		
2030	$ 565,000,000			5,513		
2031	$ 581,000,000			5,523		
2032	$ 597,000,000			5,523		
2033	$ 614,000,000			5,523		
2034	$ 631,000,000			5,523		
2035	$ 648,000,000			5,523		
2036	$ 666,000,000			5,523		
2037	$ 684,000,000			5,523		

Comp Pay by Month - 2022	**Annual Divided by 26 Pay Periods**	**Actual**	**Difference**	**2022 Cumulative Difference**	**Number of Employees - EOM**	**Difference**
January	$ 32,461,538	$ 33,363,143	$ 901,604	$ 901,604	4946	(167)
February	$ 32,461,538	$ 33,314,230	$ 852,692	$ 852,692	4943	(170)
March	$ 48,692,308	$ 50,179,220	$ 1,486,912	$ 1,486,912	4937	(176)
April	$ 32,461,538	$ 33,555,403	$ 1,093,864	$ 1,093,864	4930	(183)
May	$ 32,461,538	$ 33,573,492	$ 1,111,953	$ 1,111,953	4918	(195)
June	$ 32,461,538	$ 33,723,288	$ 1,261,749	$ 1,261,749	4915	(198)
July	$ 32,461,538	$ 33,881,549	$ 1,420,010	$ 1,420,010	4954	(159)
August	$ 48,692,308	$ 51,044,865	$ 2,352,557	$ 2,352,557	4935	(178)
September	$ 32,461,538	$ 33,992,621	$ 1,531,082	$ 1,531,082	4929	(184)
October	$ 32,461,538	$ 34,152,960	$ 1,691,421	$ 1,691,421	4942	(171)
November	$ 32,461,538	$ 34,129,601	$ 1,668,063	$ 1,668,063	4928	(185)
December	$ 32,461,538					



DISCUSSION SHEET

ITEM #D3

Topic: **Board approval of Trustee education and travel**

a. Future Education and Business-related Travel
b. Future Investment-related Travel

Discussion:

a. Per the Education and Travel Policy and Procedure, planned Trustee education and business-related travel and education which does not involve travel requires Board approval prior to attendance.

Attached is a listing of requested future education and travel noting approval status.

b. Per the Investment Policy Statement, planned Trustee travel related to investment monitoring, and in exceptional cases due diligence, requires Board approval prior to attendance.

There is no future investment-related travel for Trustees at this time.

Future Education and Business Related Travel & Webinars
Regular Board Meeting – January 12, 2023

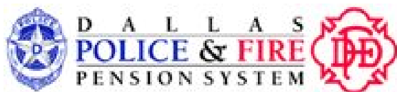
			ATTENDING	APPROVED
1.	**Conference:**	**TEXPERS Annual Conference**	**KH**	
	Dates:	April 2-5, 2023		
	Location:	Austin, TX		
	Est Cost:	TBD		
2.	**Conference:**	**NCPERS Accredited Fiduciary (NAF) Program**		
	Dates:	May 20-21, 2023		
	Location:	TBD		
	Est Cost:	TBD		
3.	**Conference:**	**NCPERS Trustee Educational Seminar (TEDS)**		
	Dates:	May 20-21, 2023		
	Location:	TBD		
	Est Cost:	TBD		
4.	**Conference:**	**NCPERS Annual Conference & Exhibition (ACE)**		
	Dates:	May 20-21, 2023		
	Location:	TBD		
	Est Cost:	TBD		

Future Education and Business Related Travel & Webinars
Regular Board Meeting – January 12, 2023

ATTENDING APPROVED

5. **Conference:** **TEXPERS Summer Education Forum**
   Dates: August 13-15, 2023
   Location: The Woodlands, TX
   Est Cost: TBD

6. **Conference:** **NCPERS Public Pension Funding Forum**
   Dates: August 20-23, 2023
   Location: TBD
   Est Cost: TBD



DISCUSSION SHEET

ITEM #D4

Topic: **Portfolio Update**

Discussion: Investment Staff will brief the Board on recent events and current developments with respect to the investment portfolio.

Regular Board Meeting – Thursday, January 12, 2023

DALLAS
POLICE & FIRE
PENSION SYSTEM

Portfolio Update

January 12, 2023

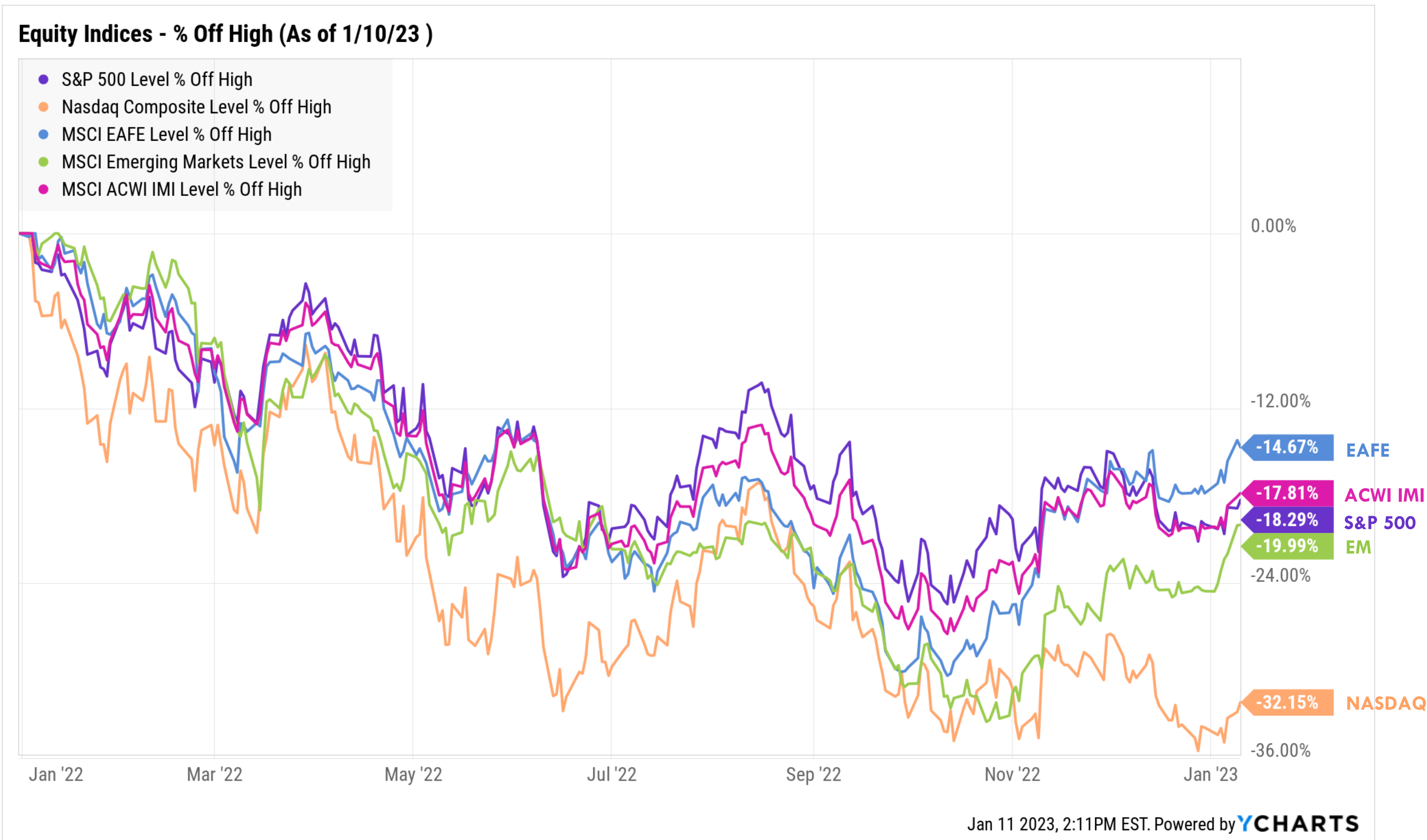
Board Meeting

Executive Summary

- Liquidation of private market assets remains the top focus.
  - $109M in distributions received in 2022, with $8.5M coming in December 2022.
  - $40M of these distributions have been redeployed into Public Equity since June.
- At the March Board meeting, staff notified the Board that the Safety Reserve would be drawn down to fund net benefit outflows.
- **Recent Rebalancing actions:**
  - The Ashmore (EM Debt) investment was fully redeemed as of 9/30/22 and $57M was invested with the new EM Debt manager MetLife at the beginning of October.
  - $26M of Private Market proceeds were redeployed into Small Cap Equity in mid-November, while $21M of Private Market proceeds were held back in Cash within the Safety Reserve.
- Estimated Year-to-Date Return (as of 12/31/22): -2.9% for DPFP portfolio; -15.1% for Public Markets (ex-Cash) which accounts for 63.7% of the assets.

DALLAS POLICE & FIRE PENSION SYSTEM

Equity Market Drawdown (1/1/22 to 1/10/23)

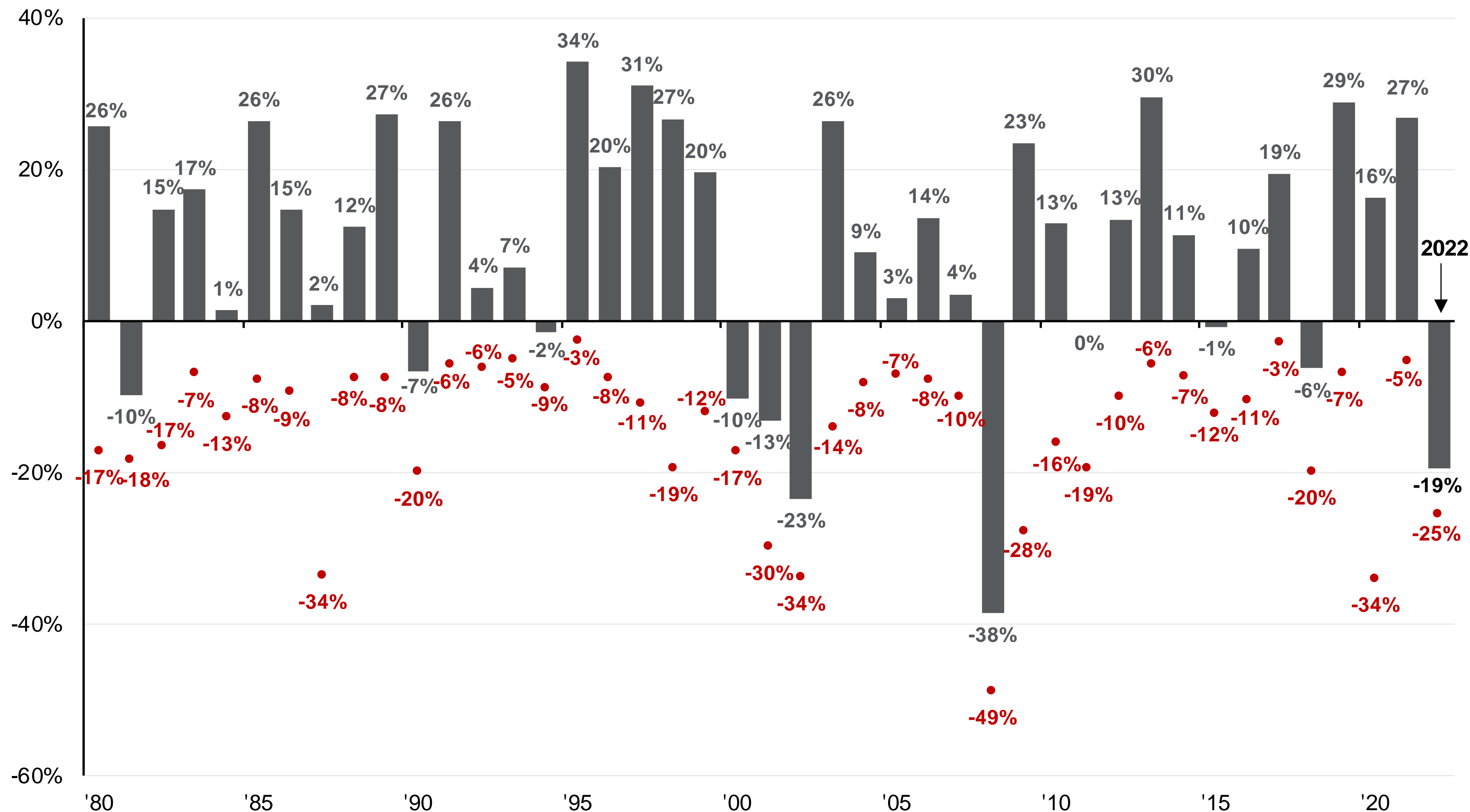


DALLAS POLICE & FIRE PENSION SYSTEM

S&P Intra-Year Declines

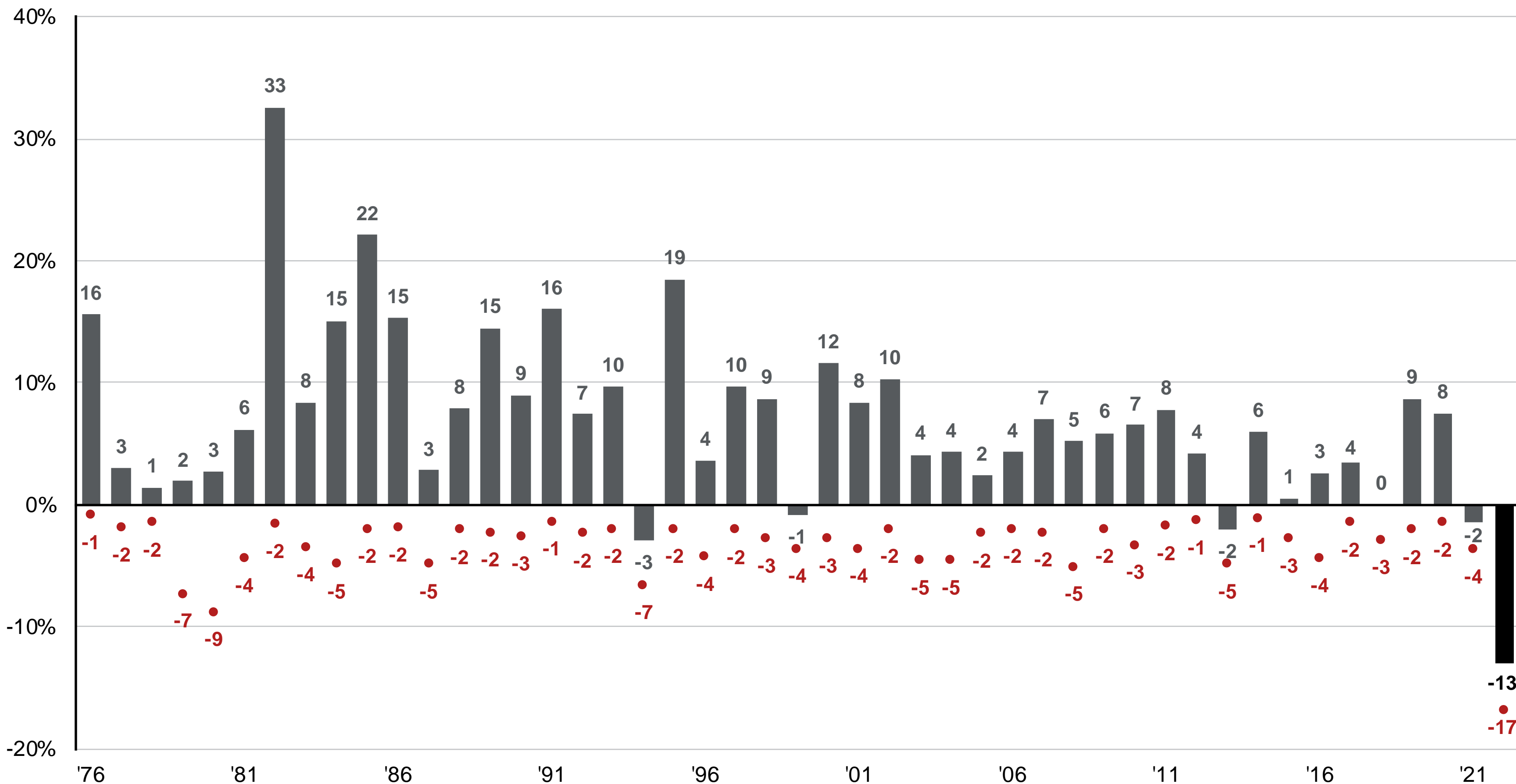
S&P intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.0%, annual returns were positive in 32 of 42 years



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.
Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2021, over which time period the average annual return was 9.4%.
Guide to the Markets – U.S. Data are as of December 31, 2022.

US Bonds Intra-Year Declines



Source: Bloomberg, FactSet, J.P. Morgan Asset Management.
Returns are based on total return. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1976 to 2021, over which time period the average annual return was 7.1%. Returns from 1976 to 1989 are calculated on a monthly basis; daily data are used afterwards.
Guide to the Markets – U.S. Data are as of December 31, 2022.

DALLAS POLICE & FIRE PENSION SYSTEM

Worst Years Ever for 60/40 Portfolio

The Worst Years Ever For a 60/40 Portfolio

Year	60/40 Portfolio	Reason
1931	-27.3%	Great Depression
1937	-20.7%	1937 Crash
2022	-16.9%	The Great Inflation
1974	-14.7%	1973-74 Bear Market
2008	-13.9%	Great Financial Crisis
1930	-13.3%	Great Depression
1941	-8.5%	WWII
2002	-7.1%	Dot-Com Crash
1973	-7.1%	1973-74 Bear Market
1969	-6.9%	Nifty Fifty Crash
2001	-4.9%	Dot-Com Crash
1966	-4.8%	1966 Bear Market

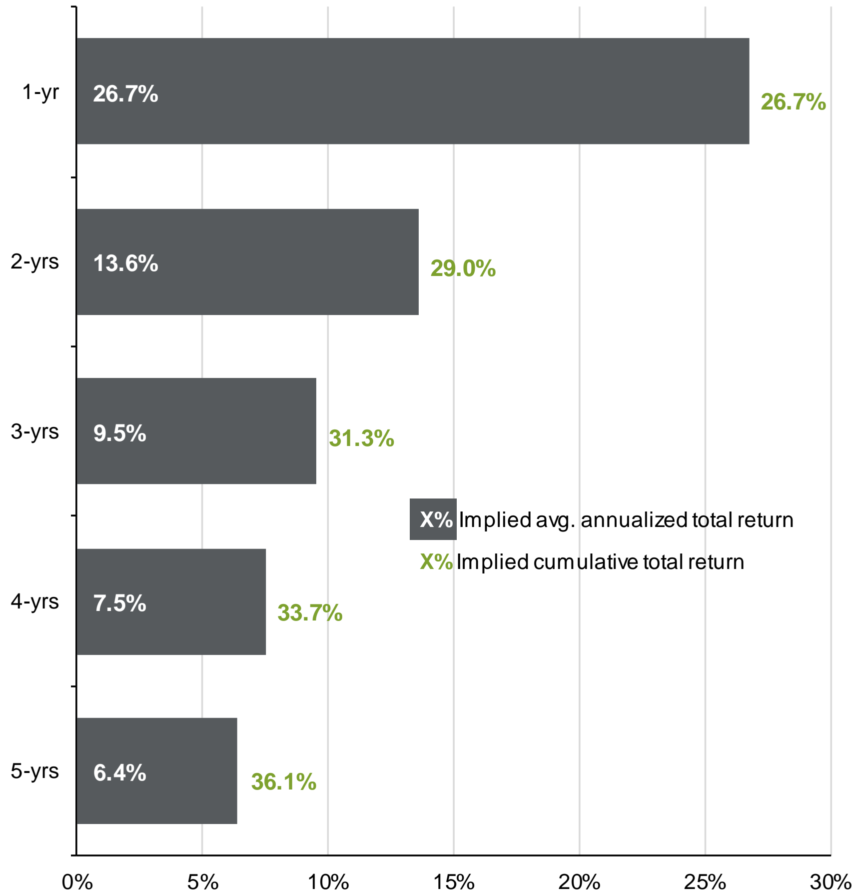
60/40 Portfolio is 60% S&P 500 and 40% 10-Year UST

Source: NYU

S&P 500 – Bull and Bear Markets & Go-Forward Returns

Return needed to reach January 2022 peak of 4797

S&P 500 level as of 12/31/2022 is 3,840



Bull and bear markets

Bull markets			Bear markets		
Bull begin date	Bull return	Duration (months)	Market peak	Bear return*	Duration (months)*
Jul 1926	152%	37	Sep 1929	-86%	32
Mar 1935	129%	23	Mar 1937	-60%	61
Apr 1942	158%	49	May 1946	-30%	36
Jun 1949	267%	85	Aug 1956	-22%	14
Oct 1960	39%	13	Dec 1961	-28%	6
Oct 1962	76%	39	Feb 1966	-22%	7
Oct 1966	48%	25	Nov 1968	-36%	17
May 1970	74%	31	Jan 1973	-48%	20
Mar 1978	62%	32	Nov 1980	-27%	20
Aug 1982	229%	60	Aug 1987	-34%	3
Oct 1990	417%	113	Mar 2000	-49%	30
Oct 2002	101%	60	Oct 2007	-57%	17
Mar 2009	401%	131	Feb 2020	-34%	1
Mar 2020	114%	21	Jan. 2022**	-25%	9
Averages	**162%**	**51**	**-**	**-41%**	**20**

Source: FactSet, NBER, Robert Shiller, Standard & Poor's, J.P. Morgan Asset Management. (Left) The current peak of 4797 was observed on January 3, 2022. (Right) *A bear market is defined as a 20% or more decline from the previous market high. The related market return is the peak to trough return over the cycle. Bear and bull returns are price returns. **The bear market beginning in January 2022 is currently ongoing, with the "bear return" and duration for this period calculated from the January 2022 market peak through the current trough in October 2022. Averages for the bear market return and duration do not include figures from the current cycle.

Guide to the Markets – U.S. Data are as of December 31, 2022.

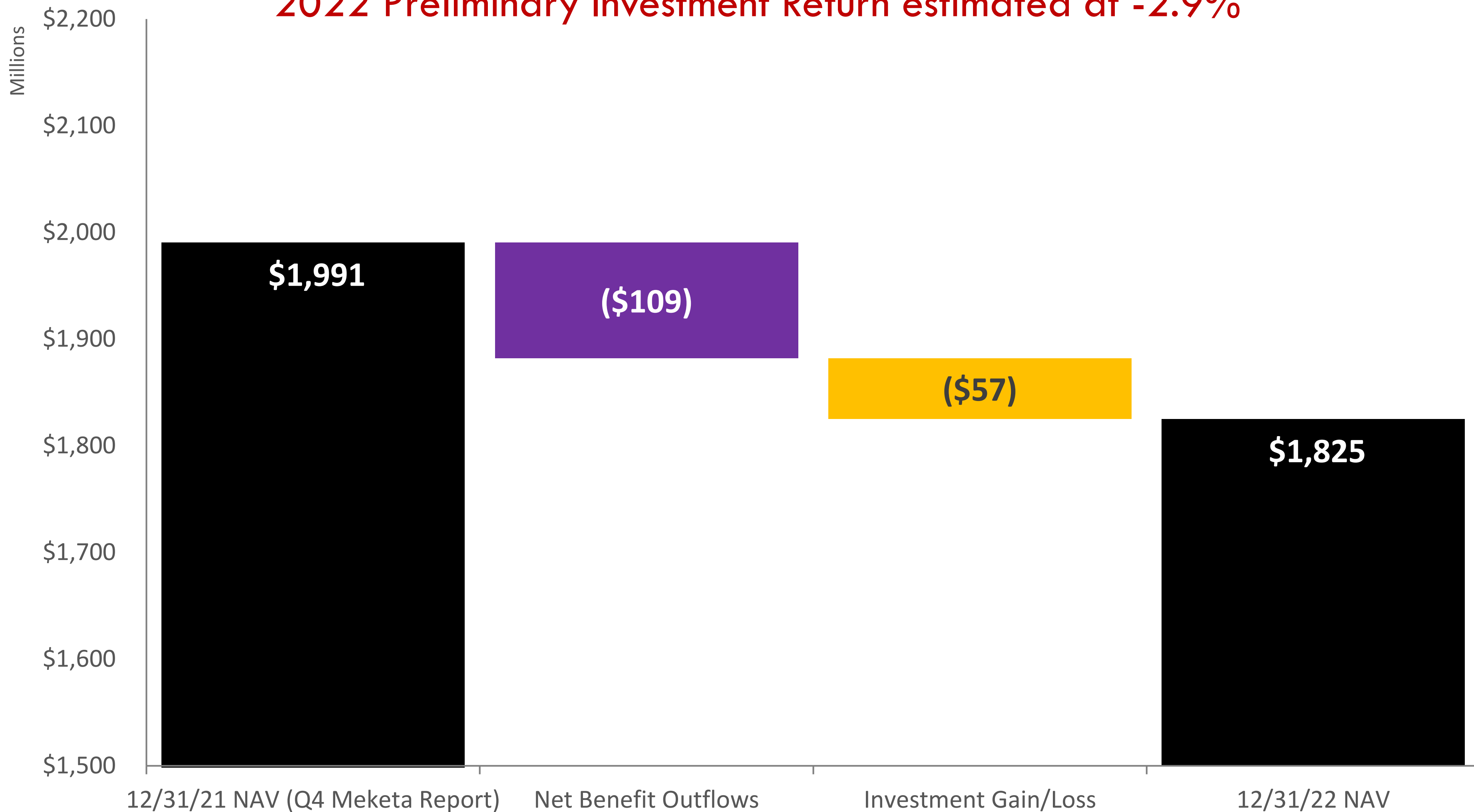
Asset Class Returns – JPM Guide to the Markets

															2008 - 2022	
2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Ann.	Vol.
Fixed Income 5.2%	EM Equity 79.0%	REITs 27.9%	REITs 8.3%	REITs 19.7%	Small Cap 38.8%	REITs 28.0%	REITs 2.8%	Small Cap 21.3%	EM Equity 37.8%	Cash 1.8%	Large Cap 31.5%	Small Cap 20.0%	REITs 41.3%	Comdty. 16.1%	Large Cap 8.8%	REITs 23.4%
Cash 1.8%	High Yield 59.4%	Small Cap 26.9%	Fixed Income 7.8%	High Yield 19.6%	Large Cap 32.4%	Large Cap 13.7%	Large Cap 1.4%	High Yield 14.3%	DM Equity 25.6%	Fixed Income 0.0%	REITs 28.7%	EM Equity 18.7%	Large Cap 28.7%	Cash 1.5%	Small Cap 7.2%	Small Cap 23.2%
Asset Alloc. -25.4%	DM Equity 32.5%	EM Equity 19.2%	High Yield 3.1%	EM Equity 18.6%	DM Equity 23.3%	Fixed Income 6.0%	Fixed Income 0.5%	Large Cap 12.0%	Large Cap 21.8%	REITs -4.0%	Small Cap 25.5%	Large Cap 18.4%	Comdty. 27.1%	High Yield -12.7%	REITs 6.6%	EM Equity 23.0%
High Yield -26.9%	REITs 28.0%	Comdty. 16.8%	Large Cap 2.1%	DM Equity 17.9%	Asset Alloc. 14.9%	Asset Alloc. 5.2%	Cash 0.0%	Comdty. 11.8%	Small Cap 14.6%	High Yield -4.1%	DM Equity 22.7%	Asset Alloc. 10.6%	Small Cap 14.8%	Fixed Income -13.0%	Asset Alloc. 6.1%	Comdty. 20.2%
Small Cap -33.8%	Small Cap 27.2%	Large Cap 15.1%	Cash 0.1%	Small Cap 16.3%	High Yield 7.3%	Small Cap 4.9%	DM Equity -0.4%	EM Equity 11.6%	Asset Alloc. 14.6%	Large Cap -4.4%	Asset Alloc. 19.5%	DM Equity 8.3%	Asset Alloc. 13.5%	Asset Alloc. -13.9%	High Yield 5.4%	DM Equity 20.0%
Comdty. -35.6%	Large Cap 26.5%	High Yield 14.8%	Asset Alloc. -0.7%	Large Cap 16.0%	REITs 2.9%	Cash 0.0%	Asset Alloc. -2.0%	REITs 8.6%	High Yield 10.4%	Asset Alloc. -5.8%	EM Equity 18.9%	Fixed Income 7.5%	DM Equity 11.8%	DM Equity -14.0%	Fixed Income 2.7%	Large Cap 17.7%
Large Cap -37.0%	Asset Alloc. 25.0%	Asset Alloc. 13.3%	Small Cap -4.2%	Asset Alloc. 12.2%	Cash 0.0%	High Yield 0.0%	High Yield -2.7%	Asset Alloc. 8.3%	REITs 8.7%	Small Cap -11.0%	High Yield 12.6%	High Yield 7.0%	High Yield 1.0%	Large Cap -18.1%	DM Equity 2.3%	High Yield 13.0%
REITs -37.7%	Comdty. 18.9%	DM Equity 8.2%	DM Equity -11.7%	Fixed Income 4.2%	Fixed Income -2.0%	EM Equity -1.8%	Small Cap -4.4%	Fixed Income 2.6%	Fixed Income 3.5%	Comdty. -11.2%	Fixed Income 8.7%	Cash 0.5%	Cash 0.0%	EM Equity -19.7%	EM Equity 1.0%	Asset Alloc. 12.4%
DM Equity -43.1%	Fixed Income 5.9%	Fixed Income 6.5%	Comdty. -13.3%	Cash 0.1%	EM Equity -2.3%	DM Equity -4.5%	EM Equity -14.6%	DM Equity 1.5%	Comdty. 1.7%	DM Equity -13.4%	Comdty. 7.7%	Comdty. -3.1%	Fixed Income -1.5%	Small Cap -20.4%	Cash 0.6%	Fixed Income 4.2%
EM Equity -53.2%	Cash 0.1%	Cash 0.1%	EM Equity -18.2%	Comdty. -1.1%	Comdty. -9.5%	Comdty. -17.0%	Comdty. -24.7%	Cash 0.3%	Cash 0.8%	EM Equity -14.2%	Cash 2.2%	REITs -5.1%	EM Equity -2.2%	REITs -24.9%	Comdty. -2.6%	Cash 0.4%

Source: Bloomberg, FactSet, MSCI, NAREIT, Russell, Standard & Poor's, J.P. Morgan Asset Management.
Large cap: S&P 500, Small cap: Russell 2000, EM Equity: MSCI EME, DM Equity: MSCI EAFE, Comdty: Bloomberg Commodity Index, High Yield: Bloomberg Global HY Index, Fixed Income: Bloomberg US Aggregate, REITs: NAREIT Equity REIT Index, Cash: Bloomberg 1-3m Treasury. The "Asset Allocation" portfolio assumes the following weights: 25% in the S&P 500, 10% in the Russell 2000, 15% in the MSCI EAFE, 5% in the MSCI EME, 25% in the Bloomberg US Aggregate, 5% in the Bloomberg 1-3m Treasury, 5% in the Bloomberg Global High Yield Index, 5% in the Bloomberg Commodity Index and 5% in the NAREIT Equity REIT Index. Balanced portfolio assumes annual rebalancing. Annualized (Ann.) return and volatility (Vol.) represents period from 12/31/2007 to 12/31/2022. Please see disclosure page at end for index definitions. All data represents total return for stated period. The "Asset Allocation" portfolio is for illustrative purposes only. Past performance is not indicative of future returns.
Guide to the Markets – U.S. Data are as of December 31, 2022.

2022 - Change in Market Value Bridge Chart

In Millions



The beginning 12/31/21 value is from the Q4 Meketa report and includes a one-quarter lag on private assets, adjusted for cash flows, so the return figure includes some significant Q4 2022 write-ups in the private equity portfolio.
Numbers may not foot due to rounding.

DALLAS POLICE & FIRE PENSION SYSTEM

Public Markets Performance Snapshot - Estimates

Public Markets (ex-Cash) currently make up 63.7% of DPFP Investment Portfolio.

Net of fees	Index	12/31/2022 NAV ($M)	MTD as of 12/31/22 Manager	MTD Index	MTD Excess	YTD as of 12/31/2022 Manager	YTD Index	YTD Excess	3 Year Trailing as of 12/31/2022 Manager	3 Yr Index	3 Yr Excess
Total Public Portfolio (ex-Cash)	**60% ACWI IMI 40% Global AGG**	**$1,163.4**	**-2.1%**	**-2.1%**	**-0.1%**	**-15.1%**	**-17.5%**	**2.4%**	**2.3%**	**0.5%**	**1.8%**
Global Equity	**MSCI ACWI IMI**	**$758.7**	**-3.1%**	**-3.8%**	**0.7%**	**-18.0%**	**-18.4%**	**0.4%**	**4.3%**	**3.9%**	**0.4%**
Boston Partners	MSCI World	$125.6	-1.8%	-4.3%	2.5%	-2.9%	-18.1%	15.3%	8.3%	4.9%	3.3%
Manulife	MSCI ACWI	$122.5	-3.3%	-3.9%	0.7%	-14.7%	-18.4%	3.7%	4.1%	4.0%	0.1%
Invesco (OFI)	MSCI ACWI	$117.9	-4.6%	-3.9%	-0.7%	-31.1%	-18.4%	-12.7%	0.5%	4.0%	-3.5%
Walter Scott	MSCI ACWI	$125.5	-2.2%	-3.9%	1.8%	-19.7%	-18.4%	-1.3%	4.5%	4.0%	0.5%
Northern Trust ACWI IMI Index[1]	MSCI ACWI IMI	$165.7	-4.4%	-3.8%	-0.5%	-17.9%	-18.4%	0.5%	4.3%	3.9%	0.4%
Eastern Shore US Small Cap[1]	Russell 2000	$48.3	-5.5%	-6.5%	1.0%	-27.0%	-20.4%	-6.6%	-0.9%	3.1%	-4.0%
Global Alpha[2]	MSCI EAFE Small Cap	$53.2	1.4%	1.1%	0.3%	-21.5%	-21.4%	-0.1%	-1.0%	-0.9%	-0.1%
EM Equity - RBC	**MSCI EM IMI**	**$83.4**	**-1.8%**	**-1.4%**	**-0.5%**	**-13.9%**	**-19.8%**	**5.9%**	**-1.4%**	**-1.8%**	**0.4%**
Public Fixed Income (ex-Cash)	**BBG Multiverse TR**	**$321.2**	**0.2%**	**0.6%**	**-0.4%**	**-9.7%**	**-18.9%**	**9.2%**	**-1.5%**	**-5.5%**	**4.0%**
S/T IG Bonds - IR+M	BBG 1-3YR AGG	$54.1	0.3%	0.2%	0.1%	-3.4%	-3.7%	0.2%	0.2%	-0.3%	0.5%
IG Bonds - Longfellow[1]	BBG US AGG	$66.2	0.1%	-0.5%	0.5%	-13.3%	-13.0%	-0.3%	-2.3%	-2.7%	0.5%
Bank Loans - Pacific Asset Mgmt.[3]	CS Leveraged Loan	$71.5	0.3%	0.5%	-0.2%	-0.5%	-0.8%	0.3%	2.4%	2.4%	0.0%
High Yield - Loomis Sayles[1]	BBG USHY 2% Cap	$68.0	-0.8%	-0.6%	-0.2%	-12.1%	-11.1%	-1.0%	-0.4%	0.0%	-0.4%
EM Debt - Metlife[2]	35% EMBI / 35% CEMBI / 30% GBI-EM	$61.3	1.1%	1.3%	-0.3%	-13.4%	-13.5%	0.2%	-4.0%	-4.0%	0.0%

Source: JPM Morgan custody data, manager reports, Investment Staff estimates and calculations. Numbers may not foot due to rounding.

[1] - 3 yr trailing performance is based on composite data due to inception date with DPFP being less than 3 years.

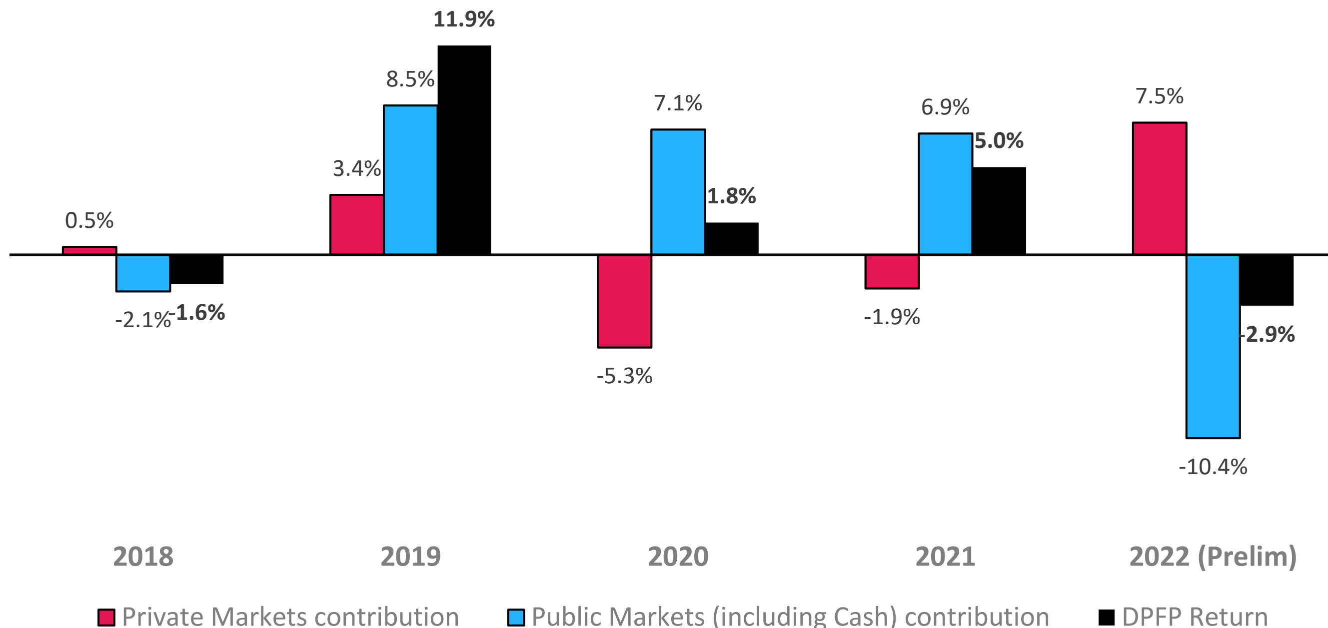
[2] - YTD and 3 yr trailing performance is based on composite data as this is new manager funded during 2022.

[3] - Benchmark for Bank Loans is proxied to S&P Leveraged Loans for current month performance.

In the September through December 2022 Portfolio Updates, there was a calculation error for the "Estimated YTD Total Public Portfolio (ex-Cash)" return. The calculation has been corrected for this report.

DALLAS POLICE & FIRE PENSION SYSTEM

Return Contribution from Public and Private Markets

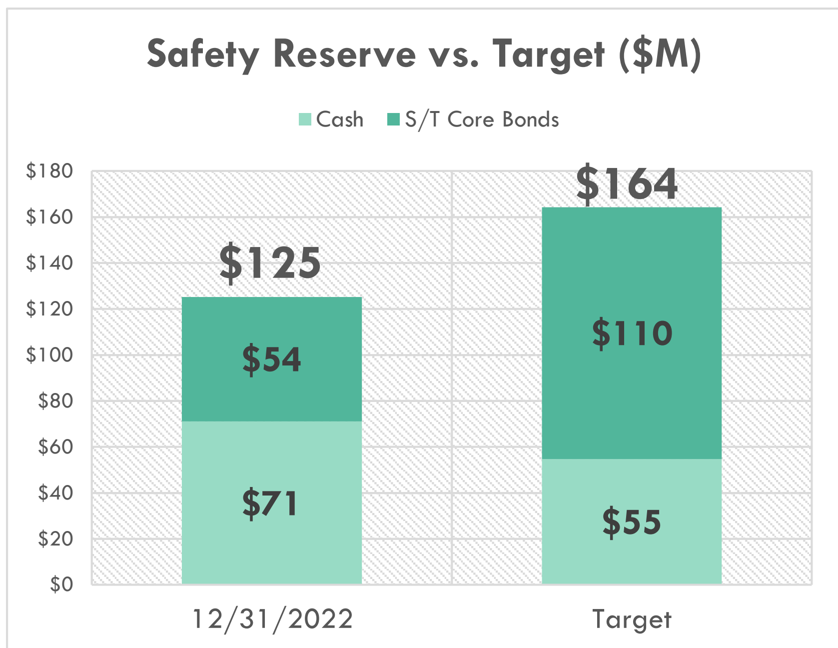


	2018	2019	2020	2021	2022 (Prelim)
Private Markets Avg. Allocation	50.1%	43.2%	41.0%	31.5%	30.8%
Private Markets Return	0.9%	7.9%	-12.9%	-6.1%	24.5%
Private Markets Return Contribution	0.5%	3.4%	-5.3%	-1.9%	7.5%
Public Markets Avg. Allocation	49.9%	56.8%	59.0%	68.5%	69.2%
Public Markets Return	-4.2%	15.0%	12.1%	10.1%	-15.1%
Public Markets Return contribution	-2.1%	8.5%	7.1%	6.9%	-10.4%
DPFP Total Return*	**-1.6%**	**11.9%**	**1.8%**	**5.0%**	**-2.9%**

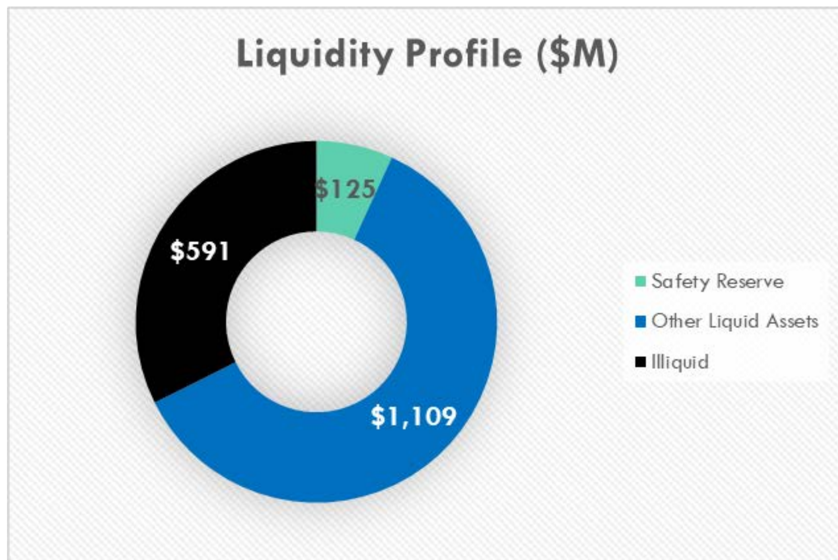
* - DPFP Total Return is a calculation derived from annual average market value of Public and Private markets, respectively. Typically matches actual DPFP annual return within 50 basis points.

DALLAS POLICE & FIRE PENSION SYSTEM

Safety Reserve Dashboard



Projected Net Monthly outflows of **$9.5M** per month. Safety Reserve of **$125M** would cover net monthly outflows for next **13 months** or through **Jan 2024.**



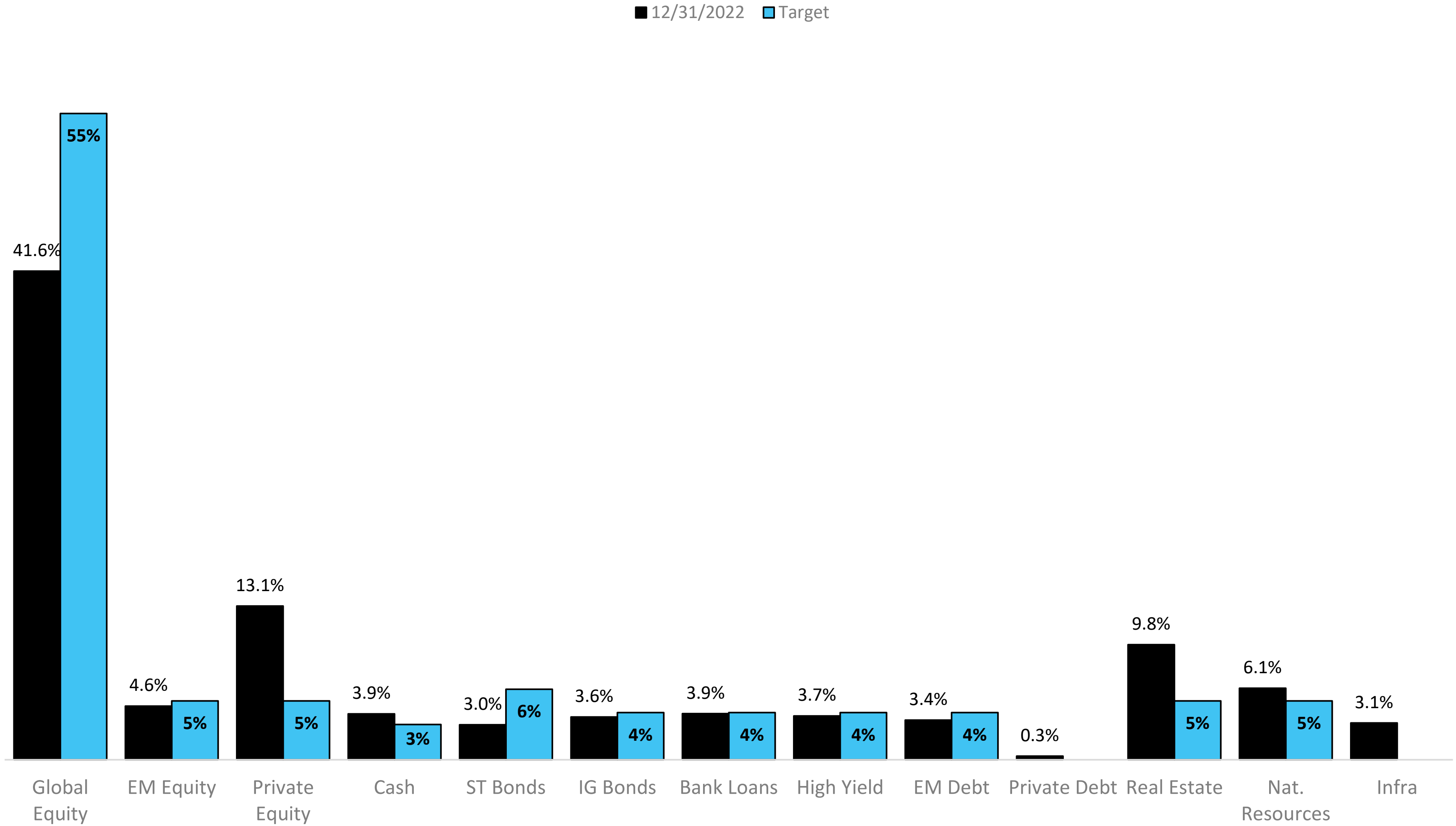
Expected Cash Activity	Date	Amount ($M)	Projected Cash Balance ($M)	Projected Cash (%)
	12/31/22		**$71.1**	**3.8%**
City Contribution	1/13/23	$8.8	$79.9	**4.3%**
City Contribution	1/27/23	$8.8	$88.7	**4.8%**
Pension Payroll	1/27/23	($27.8)	$60.9	**3.3%**
City Contribution	2/10/23	$8.8	$69.7	**3.7%**
City Contribution	2/24/23	$8.8	$78.5	**4.2%**
Pension Payroll	2/24/23	($27.8)	$50.7	**2.7%**
City Contribution	3/10/23	$8.8	$59.5	**3.2%**
City Contribution	3/24/23	$8.8	$68.3	**3.7%**
Pension Payroll	3/24/23	($27.8)	$40.5	**2.2%**

Projected Cash activity includes expected benefit contributions, payments, and material expected capital calls or expenses.

Numbers may not foot due to rounding

DALLAS POLICE & FIRE PENSION SYSTEM

Asset Allocation – Actual vs Target



Asset Allocation & Global Equity Detail

DPFP Asset Allocation	12/31/2022		Target			Variance	
	NAV	%	$ mil.	%	% of Target	$ mil.	%
Equity	**1,081**	**59.2%**	**1,186**	**65%**	**91%**	**-106**	**-5.8%**
Global Equity	759	41.6%	1,004	55%	76%	-245	-13.4%
Boston Partners	*126*	*6.9%*	*146*	*8%*	*86%*	*-20*	*-1.1%*
Manulife	*123*	*6.7%*	*146*	*8%*	*84%*	*-23*	*-1.3%*
Invesco (OFI)	*118*	*6.5%*	*146*	*8%*	*81%*	*-28*	*-1.5%*
Walter Scott	*126*	*6.9%*	*146*	*8%*	*86%*	*-21*	*-1.1%*
Northern Trust ACWI IMI Index	*166*	*9.1%*	*274*	*15%*	*61%*	*-108*	*-5.9%*
Eastern Shore US Small Cap	*48*	*2.6%*	*73*	*4%*	*66%*	*-25*	*-1.4%*
Global Alpha Intl Small Cap	*53*	*2.9%*	*73*	*4%*	*73%*	*-20*	*-1.1%*
Emerging Markets Equity - RBC	83	4.6%	91	5%	91%	-8	-0.4%
Private Equity*	239	13.1%	91	5%	261%	147	8.1%
Fixed Income	**398**	**21.8%**	**456**	**25%**	**87%**	**-58**	**-3.2%**
Cash	71	3.9%	55	3%	130%	16	0.9%
S/T Investment Grade Bonds - IR+M	54	3.0%	110	6%	49%	-55	-3.0%
Investment Grade Bonds - Longfellow	66	3.6%	73	4%	91%	-7	-0.4%
Bank Loans - Pacific Asset Management	72	3.9%	73	4%	98%	-1	-0.1%
High Yield Bonds - Loomis Sayles	68	3.7%	73	4%	93%	-5	-0.3%
Emerging Markets Debt - MetLife	61	3.4%	73	4%	84%	-12	-0.6%
Private Debt*	6	0.3%	0	0%		6	0.3%
Real Assets*	**347**	**19.0%**	**183**	**10%**	**190%**	**164**	**9.0%**
Real Estate*	178	9.8%	91	5%	196%	87	4.8%
Natural Resources*	111	6.1%	91	5%	122%	20	1.1%
Infrastructure*	57	3.1%	0	0%		57	3.1%
Total	**1,825**	**100.0%**	**1,825**	**100%**		**0**	**0.0%**
Safety Reserve ~$162M=18 mo net CF	125	6.9%	164	9%	76%	-39	-2.1%
*Private Market Assets	591	32.4%	274	15%		317	17.4%

Source: Preliminary JP Morgan Custodial Data, Staff Estimates and Calculations.
Numbers may not foot due to rounding

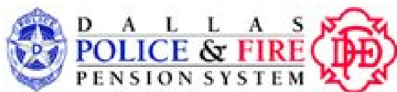
DALLAS POLICE & FIRE PENSION SYSTEM

2023 Board Investment Review Plan*

Staff presentations targeted for 15 minutes, Manager presentations 30 – 60 minutes.

Month	Review
March	• Real Estate: Clarion Presentation & other real estate review
April	• Real Estate: AEW Presentation
May	• Natural Resources: Hancock Presentation
June	• Natural Resources: Staff review of BTG Pactual (Timber)
August	• Infrastructure: Staff review of AIRRO and JPM Maritime
September	• Staff review of Public Fixed Income managers
October	• Staff review of Public Equity managers
November	• Staff review of Private Equity and Debt

*Presentation schedule is subject to change.



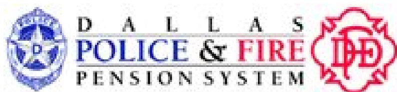
DISCUSSION SHEET

ITEM #D5

Topic: **Report on the Investment Advisory Committee**

Discussion: The Investment Advisory Committee met on December 15, 2022. The Committee Chair and Investment Staff will comment on Committee observations and advice.

Regular Board Meeting – Thursday, January 12, 2023



DISCUSSION SHEET

ITEM #D6

Topic: **Private Asset Cash Flow Projection Update**

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.072 of the Texas Government Code.

Discussion: Staff will provide the quarterly update on the private asset cash flow projection model first discussed at the February 2018 Board meeting. The cash flow model projects estimated contributions to, and distributions from, private assets through the end of 2024. These estimates are intended to assist the Board in evaluating the expected time frame to reduce DPFP's exposure to these assets and the implications for the public asset redeployment, overall asset allocation, and expected portfolio risk and return.

DALLAS
POLICE & FIRE
PENSION SYSTEM

Quarterly Private Asset Cash Flow Projection Update

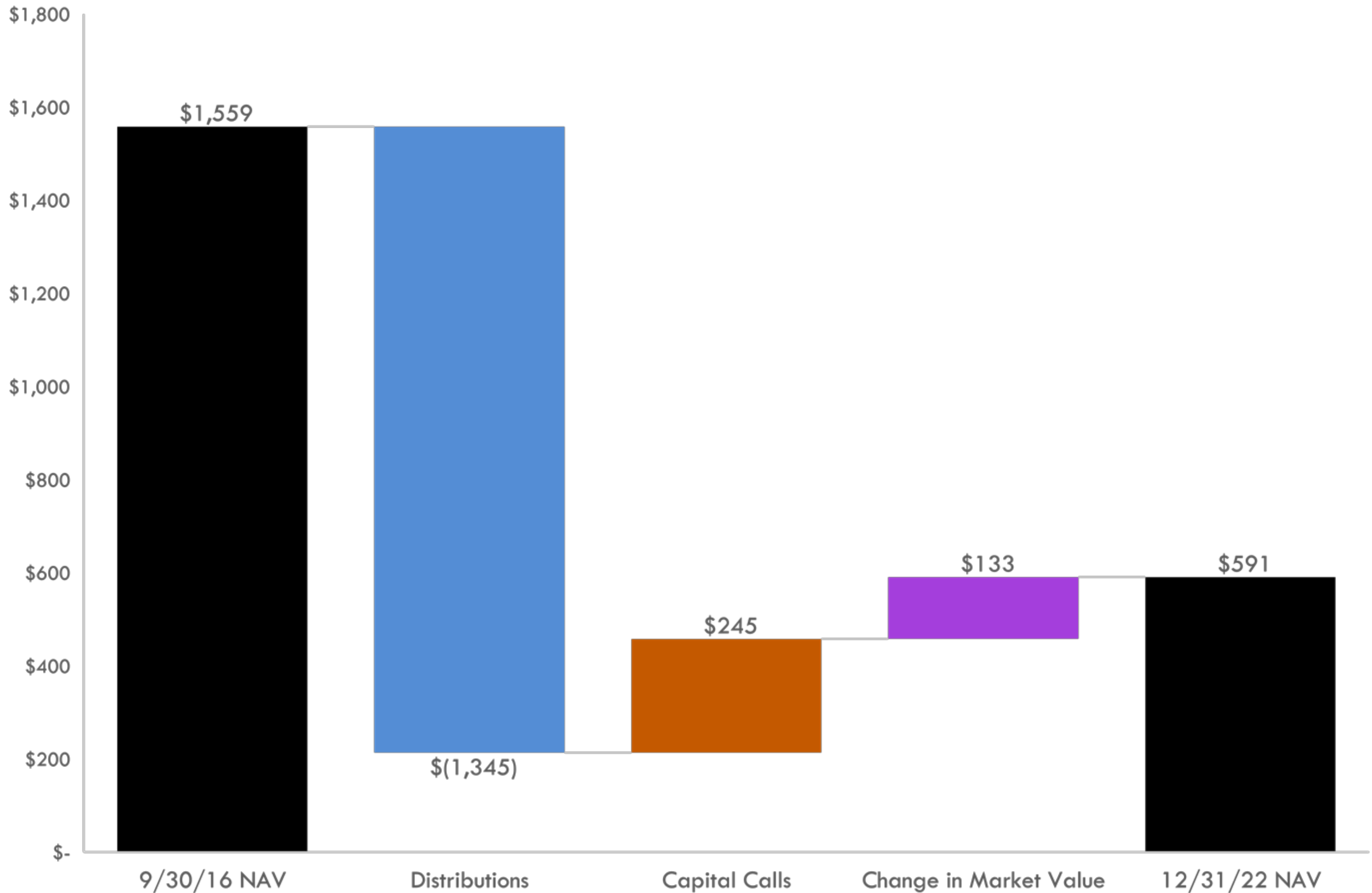
January 12, 2023

Private Asset Cash Flow Projections

Methodology Review

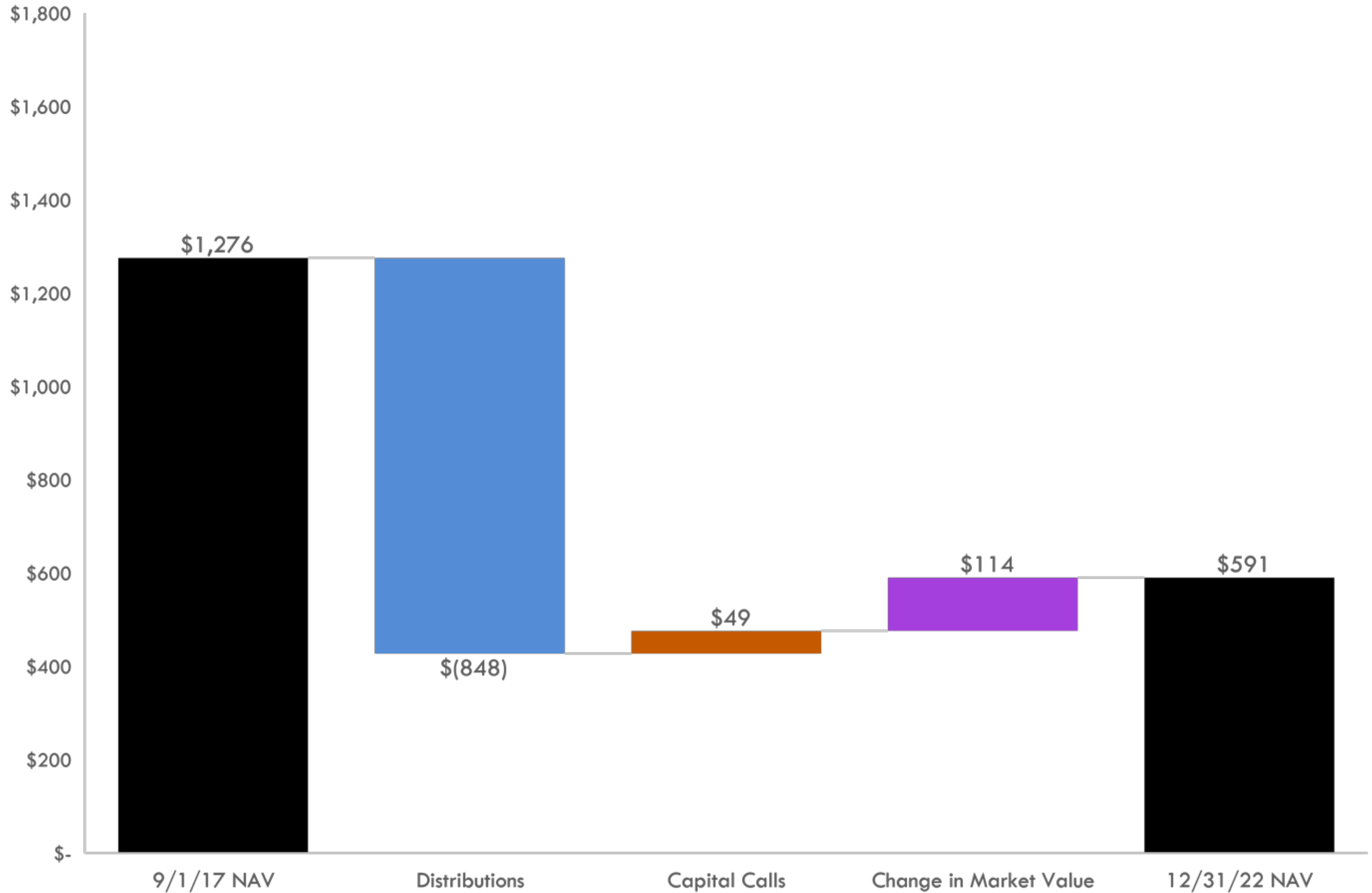
- Staff estimates capital calls and cash distributions from the Private Asset portfolio, built up by individual asset.
- DPFP has more control over direct investments in Real Estate and Natural Resources, therefore should have more accuracy in forecasting cash flows based on planned sales. Private Equity fund investments are controlled by GP's, therefore DPFP has little or no control over outcome – Staff incorporates GP insights but often uses an even distribution schedule over 2 years with these investments.
- **Cash flow estimates are inherently imprecise as they are often subject to events & forces outside of the manager's control.**

Private Asset Bridge Chart – Since 9/30/16



Numbers may not foot due to rounding.

Private Asset Bridge Chart – Since 9/1/17 (New Board Formation)



Numbers may not foot due to rounding.

Private Asset Quarterly Cash Flows – Q4 2022

TOTAL CAPITAL CALLS & CONTRIBUTIONS		**$71,037**
TRG AIRRO	Capital Call	$71,037

TOTAL DISTRIBUTIONS		**$55,177,350**
Distributions above $100K		
AEW	Note Distribution	$25,840,000
JPM Maritime	Distribution	$12,543,880
Lone Star CRA	Portfolio Company Sale	$9,411,765
Hearthstone	Spring Valley Note Payoff	$2,500,000
Huff Alternative	Distribution	$2,492,034
Riverstone	Distribution	$1,164,359
Clarion	CCH Lamar Income	$668,100
Hudson Clean Energy	Distribution	$354,173
L&B	Kings Harbor Residual	$150,000

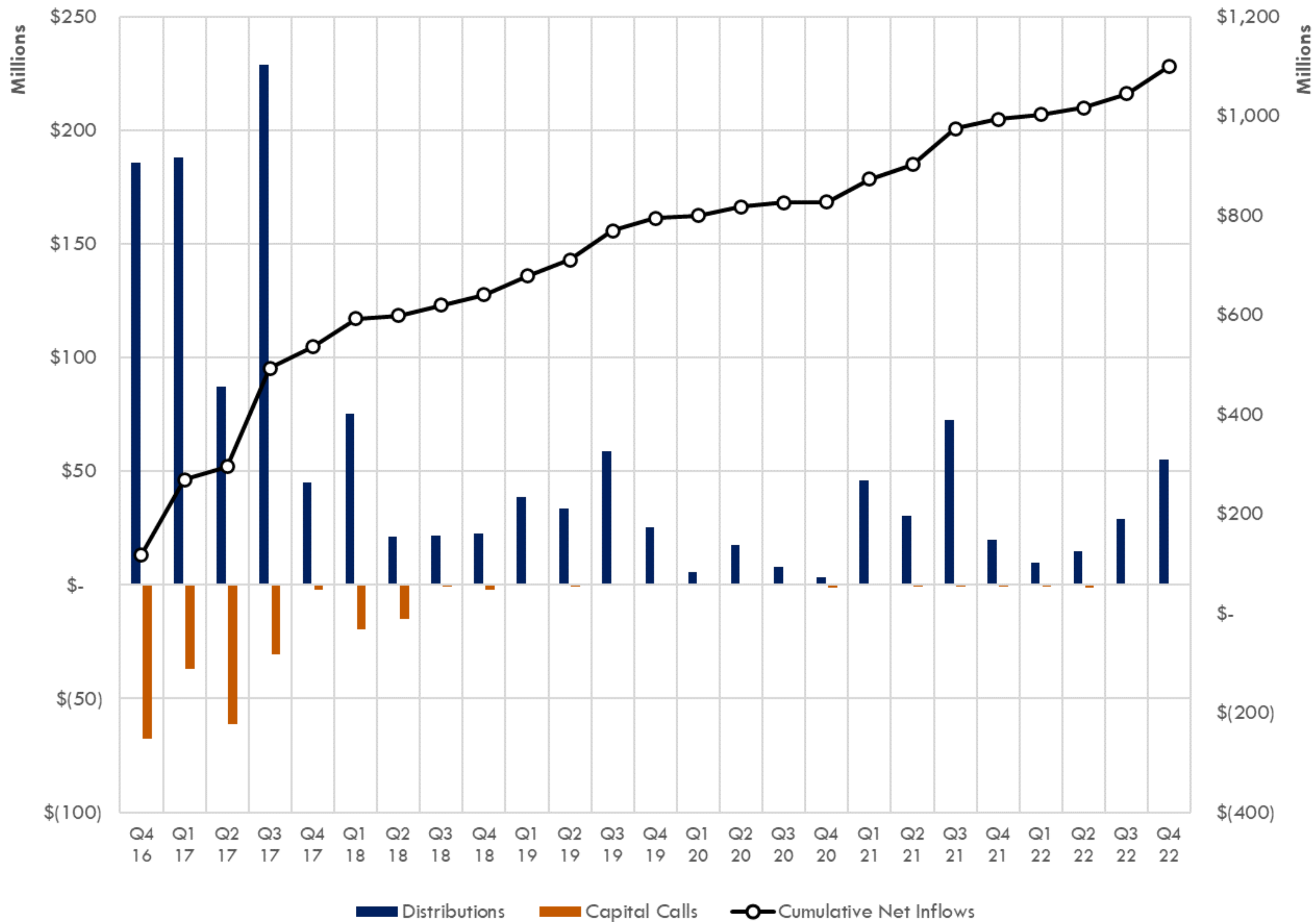
Numbers may not foot due to rounding.

2022 Actual vs. Targeted Private Asset Cash Flows

Private Asset Cash Net Inflows	2022 Actual	2022 Targeted	Notes:
Private Asset total	**106,412,596**	**166,933,758**	
Private Equity total	29,688,869	47,517,452	*Received expected proceeds from Huff Alternative. Proceeds from Lone Star and Industry Ventures were lower than projected.*
Private Debt total	1,418,916	6,533,513	*Riverstone proceeds were lower than expected and no distributions occurred from Highland fund in wind-down.*
Infrastructure total	16,064,206	29,511,450	*Maritime fund accounted for all of the proceeds received.*
Natural Resources total	1,331,000	21,561,509	*Agriculture income drove distributions. International Timber sales did not occur as projected.*
Real Estate total	57,909,604	61,809,834	*Sales within the AEW portfolio accounted for majority of proceeds. Kings Harbor sale proceeds received in July and Spring Valley seller note repaid early in December.*

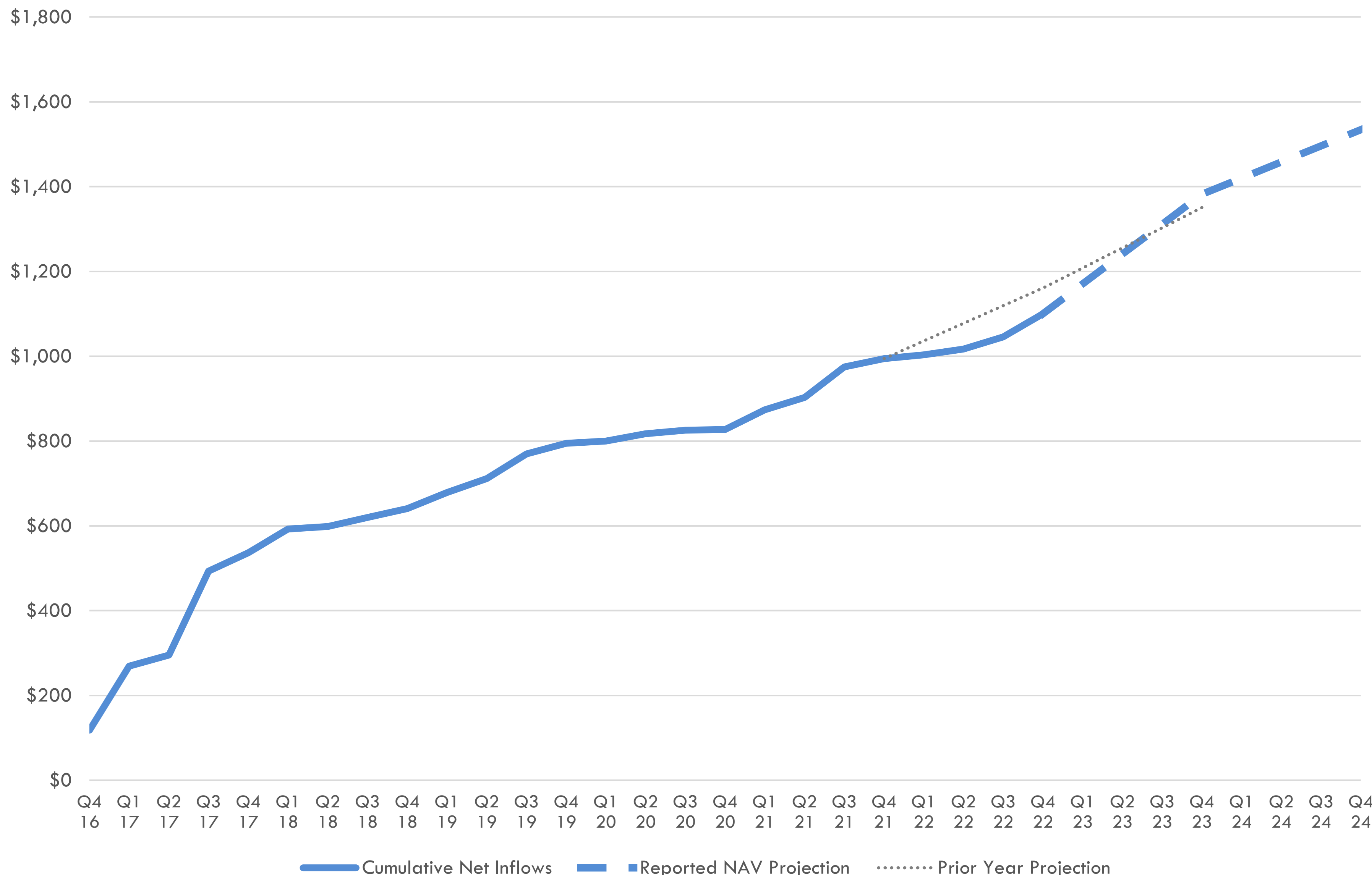
Numbers may not foot due to rounding.

Private Asset Quarterly Cash Flows – Since 9/30/16



Cumulative Actual and Projected Private Asset Net Inflows

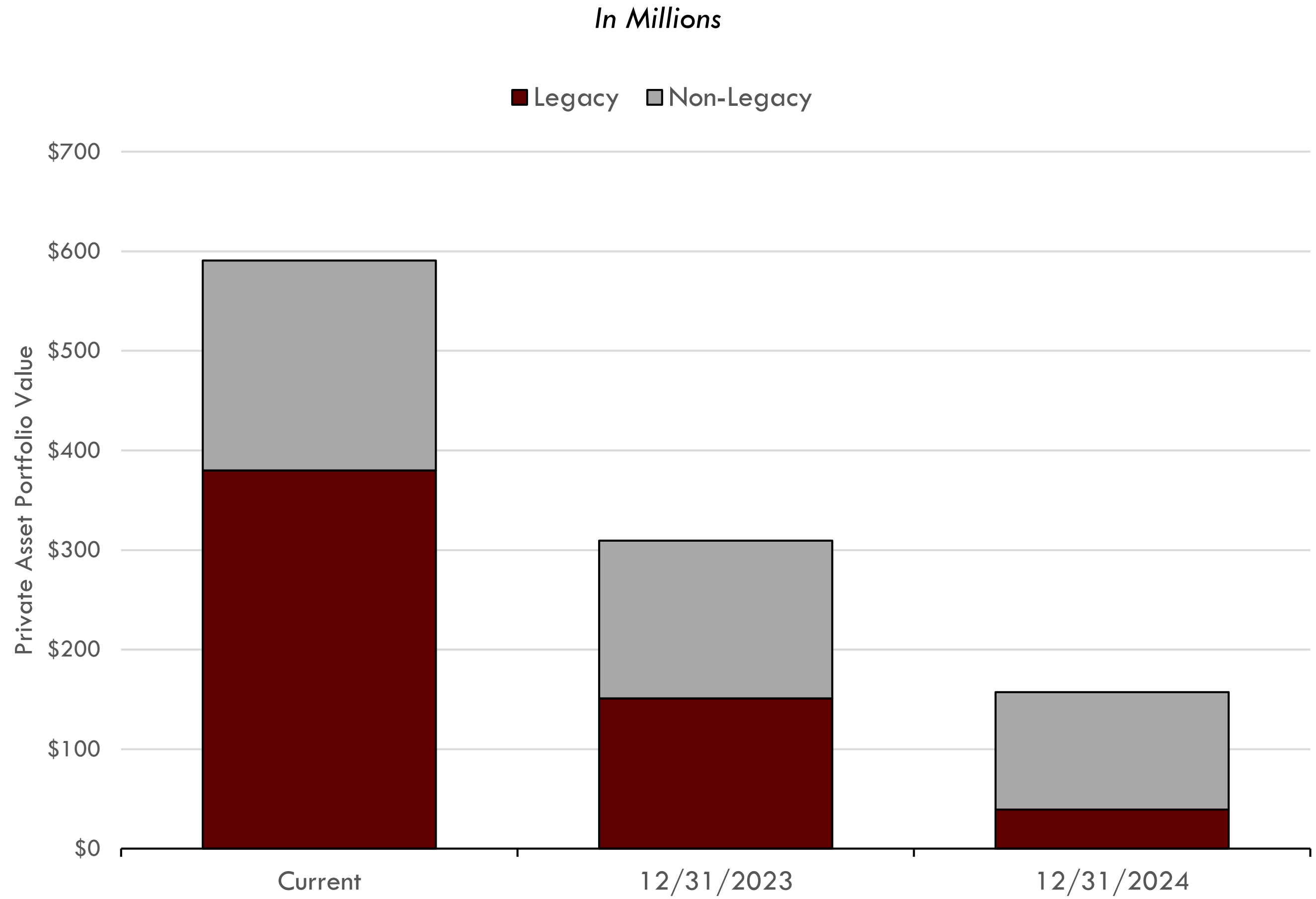
Private asset cash flow projections are based on either in-process/planned sales, if available, or a gradual disposition through 2024.



Private Asset Disposition Timeline & Composition

Private asset cash flow projections are based on either in-process/planned sales, if available, or a gradual disposition through 2024.

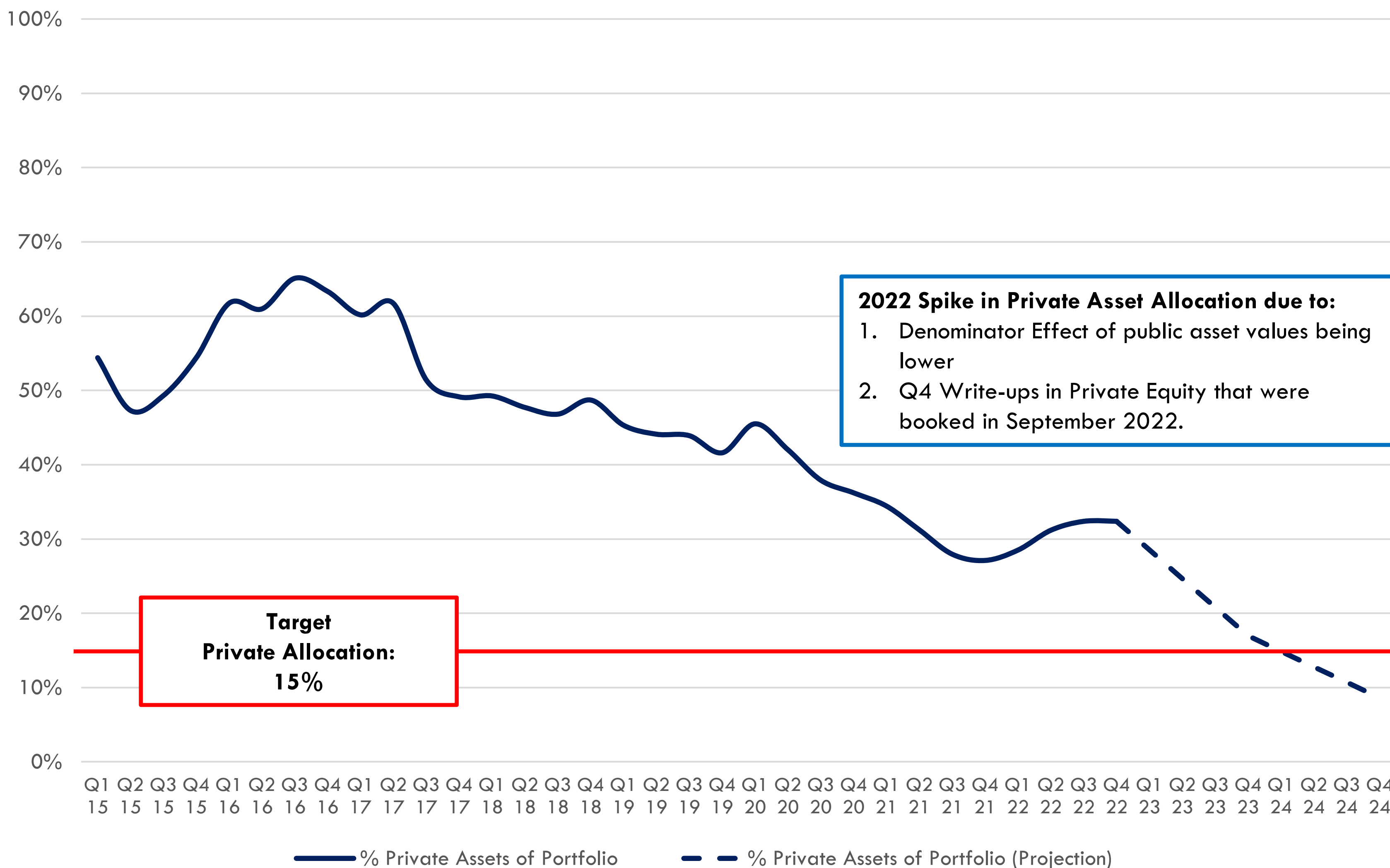
In Millions

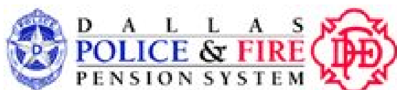


	Current	12/31/2023	12/31/2024
Legacy NAV (M)	$380	$151	$39
% of Private Portfolio	64%	49%	25%
% of DPFP Portfolio	21%	8%	2%

Private Asset Allocation Over Time

Private asset cash flow projections are based on either in-process/planned sales, if available, or a gradual disposition through 2024.
Assumes 100% of private asset proceeds are reinvested into liquid investments and flat fund NAV





DISCUSSION SHEET

ITEM #D7

Topic: **Possible Amendment to the Investment Policy Statement**

Discussion: At the August Board meeting, Meketa responded to a Board request on ownership diversity's metrics on recent manager searches advised on or conducted by Meketa. As part of the discussion, the Board discussed whether DPFP should have a formal policy to ensure the inclusion of diverse or emerging managers in future manager searches. The Board directed that staff seek IAC input on this. Staff discussed proposed policy language and received feedback from the IAC at the December 15th meeting. If the Board wishes to proceed, the below language could be incorporated in the Investment Policy Statement in Section 7 – Investment Manager Search, Selection and Monitoring.

Emerging and Diverse Managers

Strategic Purpose and Objective: Over the long term, inclusion of Emerging and Diverse Managers as part of external investment management is expected to enhance the expected investment performance of the System. Such relationships shall exhibit strong alignment of interest with investors and seek to provide DPFP with long-term access to the next generation of investment talent. Staff shall seek to find smaller and diverse managers that can benefit the System by enhancing its risk-adjusted returns, net of expenses.

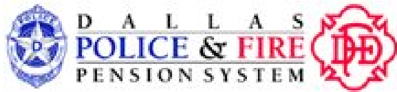
DISCUSSION SHEET

ITEM #D7
(continued)

On all public active manager searches, staff will request an RFP from at least one Emerging or Diverse Manager, as long the firm meets the minimum criteria outlined in the search process. The Manager must either:

1. *Have economic ownership of more than 50% of any combination of the following groups: female, veteran, disabled and/or minority (non-white), or*

2. *If said ownership of the groups above is below 50%, then firm must manage less than $2 billion in total assets and must have been founded no more than 10 years prior.*



DISCUSSION SHEET

ITEM #D8

Topic: **Consultant Search Process**

Discussion: Meketa was hired as DPFP's general investment consultant in April 2018. At the time Meketa was hired, DPFP did not expect to make any new private market investments over the near-term given DPFP's over-allocation to private markets. Because of this, Meketa was not engaged to provide any direct private market services outside of performance reporting, although Meketa does have the capability to advise on private markets. Staff plans to conduct a consultant search in early 2023 as the relationship with Meketa will be at the 5-year mark and staff expects the need to add some form of private market consulting services.

At the December 15th IAC meeting, staff discussed the consultant RFP scope and timing with the committee, as well as the need to establish a sub-committee of Board and IAC members to advise staff relating to the consultant search process. A draft search timeline is attached. Board members Nancy Rocha and Ken Haben, and IAC members Rakesh Dahiya, Tom Tull and Ryan Bailey indicated their interest in serving on the sub-committee.

Staff Recommendation: **Form** a sub-committee to advise staff in regard to the planned consultant search process and **appoint** Board members Nancy Rocha and Ken Haben, and IAC members Rakesh Dahiya, Tom Tull and Ryan Bailey to the sub-committee.

Draft Consultant Search Timeline

December 15, 2022 IAC Meeting

- Discuss Consultant search process and IAC members willing to serve on search sub-committee.

January 2023 Board Meeting

- Discuss Consultant search sub-committee members and search timeline with the Board.
- Board appointment of consultant search sub-committee

February 1, 2023

- Issue RFP to selected consulting firms

February 28, 2023

- RFP Submission Deadline

March 2023

- Staff review of RFPs and interview of selected firms

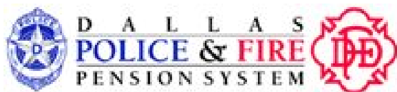
March/April 2023

- Search sub-committee interviews finalist firms

April/May 2023

- Board approval of recommended firm(s)

DALLAS POLICE & FIRE PENSION SYSTEM

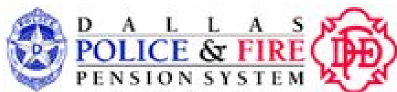


DISCUSSION SHEET

ITEM #D9

Topic: **Legal issues - In accordance with Section 551.071 of the Texas Government Code, the Board will meet in executive session to seek and receive the advice of its attorneys about pending or contemplated litigation or any other legal matter in which the duty of the attorneys to DPFP and the Board under the Texas Disciplinary Rules of Professional Conduct clearly conflicts with Texas Open Meeting laws.**

Discussion: Counsel will brief the Board on these issues.



DISCUSSION SHEET

ITEM #D10

Topic: **Executive Director Performance Evaluation**

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.074 of the Texas Government Code.

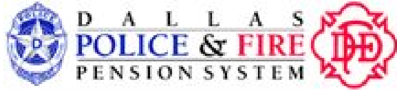
Discussion: The Board will review performance and provide recommendations concerning yearly objectives, goals, and performance.

DISCUSSION SHEET

ITEM #E1

Topic: **Public Comment**

Discussion: Comments from the public will be received by the Board.



DISCUSSION SHEET

ITEM #E2

Topic: **Executive Director's report**

a. Associations' newsletters
- NCPERS Monitor (January 2023)
- NCPERS PERSist (Winter 2023)

b. Open Records

c. Staffing Update

Discussion: The Executive Director will brief the Board regarding the above information.

THE NCPERS
MONITOR
The Latest in Legislative News
January 2023

In This Issue

3 Executive Director's Corner

Photo illustration © 2023, alamy.com

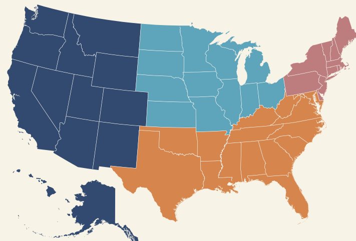
As we kick off 2023, it's a busy time of year in Washington. Newly elected officials are being sworn in and the 118th Congress is convening for the first time.

5 End-of-Year Wrap Up

Photo illustration © 2023, istock.com

In the final days of the 117th Congress, the House and Senate gave approval to a massive $1.7 billion, end-of-year omnibus appropriations bill.

9 Around the Regions



This month, we will highlight West Virginia, Illinois, Texas, and California.

The Politicization of ESG Investing

Photo illustration © 2023, shutterstock.com

ESG is the latest polarizing issue to divide red and blue states, but the practice of using Environmental, Social, and Governance (ESG) factors as part of an investing framework is nothing new.

Pensions were early adopters of socially responsible investing in the 1950s, as Electrical and Mine Workers Unions allocated capital to affordable housing and health facilities. Even though ESG investing has been around for nearly 70 years, the term did not become popular until the early 2000s. Sustainable investing began to receive increased attention following the Paris Climate Agreement in 2016. In the past few years ESG has only become more mainstream, with a record $649 billion allocated to ESG-focused funds in 2021.

As ESG investing becomes more popular, though, the practice has become more controversial and increasingly politicized in the U.S. With the recent DOL ruling that permits retirement plan fiduciaries to use ESG strategies and Republicans newly in control of the House, the uproar is unlikely to die down anytime soon.

Battles over ESG have already begun on a state level after a group of attorneys general sent a letter to BlackRock arguing its ESG stance is harming state pension plans. Since then, red states have divested over $4 billion from BlackRock (but the firm has taken in $133 billion in 2022 from U.S. investors).

Despite the backlash against ESG in these conservative states, the impact on how pension funds can invest in ESG has been relatively minimal because in many states funds are controlled by the legislature or state commission.

Alabama, Indiana and Kentucky, for example, have not changed investment strategies to eliminate sustainable investments, according to state pension officials. And in Florida, where Governor Ron DeSantis banned state pension funds from screening for ESG risks, it was reported that the Florida State Board of Administration voted in favor of more than 40 percent of social-related shareholder resolutions and nearly 30 percent of environmental-related shareholder resolutions in the last fiscal year.

On the other end of the spectrum, progressives are calling for BlackRock and other asset managers to do more, particularly in light of increasing reports of 'greenwashing,' or practices that mislead consumers and investors by falsely portraying a product or investment as socially responsible. Several asset managers—including Goldman Sachs and Vanguard—have been fined for greenwashing.

Meanwhile, pension funds that have been long-time advocates of integrating ESG risks and opportunities into their investment strategies are defending the practice.

At CalPERS November 16 board meeting, CEO Marcie Frost highlighted that the fund's ESG strategy has produced investment opportunities—including $19 billion in global equity—and has significantly reduced the fund's carbon intensity over the past seven years. "Applying the lens of ESG is not a mandate for how to invest. Nor is it an endorsement of a political position or ideology," Frost said. "Those who say otherwise are actually advocating for investors like CalPERS to put on blinders ... to ignore information and data that might otherwise help build on the retirement security of our 2 million members."

Without regulatory guidance on what ESG investing means, though, the practice remains vulnerable to attacks and misunderstanding by the public. Fewer institutional investors are utilizing ESG frameworks when making investment decisions, according to the Callan ESG Survey. In 2022, only 35 percent of respondents indicated using ESG factors to make investment decisions compared to 49 percent in 2021.

NCPERS anticipates ESG will continue to be an important issue to watch this year on both a state and federal level. We'll be discussing ESG investing further at our Legislative Conference on January 22-24 in Washington, DC. ◆

NCPERS Executive Director's Corner

Fresh Faces in Washington

Photo illustration © 2023, alamy.com

As we kick off 2023, it's a busy time of year in Washington. Newly elected officials are being sworn in and the 118th Congress is convening for the first time.

Here at NCPERS, we're preparing our 2023 policy agenda as we get ready for this month's Legislative Conference and Pension Communications Summit. We're also welcoming two new employees: Bridget Early, our Director of Membership and Strategic Alliances, and Destini Striggles, our Member Services Coordinator. While they're both new to NCPERS, they're not new to public pension advocacy. Bridget previously led the National Public Pension Coalition, and Destini joins us from the National Institute on Retirement Security.

But there are many fresh faces in Washington who are less familiar with the benefits of public pensions, and educating these new members will be a priority this year.

Last month, we hosted a webinar where Bridget Early and Tony Roda reflected on the state and federal developments that impacted public pensions in 2022 and the issues to watch in 2023. An analysis done prior to the election showed that 32 of the top legislative leadership positions across the country were going to include new leaders. As Bridget pointed out, not only will we have new lawmakers, but new legislative leaders who are going to determine committee assignments and caucus priorities. This will be an important area to focus on this year, and certainly a topic we'll be speaking to later this month at the Legislative Conference.

There are many fresh faces in Washington who are less familiar with the benefits of public pensions, and educating these new members will be a priority this year.

A potential positive for the coming year is that many public sector employers are recognizing the positive impact that defined benefit pension plans can have on staff retention.

In 2022, Alaska in particular saw the negative impacts of closing their DB plan. "There's nothing really keeping teachers and public employees in Alaska because there's nothing to build towards when it comes to a DB plan," Bridget noted. These recruitment and retention issues are costing the state around $20 million per year on top of the loss of secure revenue that was going in with the previous plan design, she estimated. House Bill 55, which would create a new pension fund for police and firefighters, advanced last year. As staff recruitment and retention continues to be a major issue across industries, we're hopeful there will be more positive momentum.

With the increasing politicization of ESG (which you can read more about in this issue of *The Monitor*), it's no surprise that we're beginning to see an increase in lawmakers trying to legislate how investments are made. The American Legislative Exchange Council has already developed a framework to 'fight' ESG investment schemes.

A potential positive for the coming year is that many public sector employers are recognizing the positive impact that defined benefit pension plans can have on staff retention.

We anticipate this will continue to play out in 2023. During last month's webinar, Tony said "I expect there to be legislation in the House on ESG…the House Republicans see ESG as great political fodder, and I think they're going to use the issue throughout Congress."

NCPERS will of course continue to keep members up to date on the latest state and federal issues impacting public pensions. I encourage you to join us in Washington on January 22-24 at NCPERS Legislative Conference to learn more about the policies that may impact your fund this year. ◆

2023 PENSION COMMUNICATIONS SUMMIT

January 23 – 24

Renaissance Washington, DC Hotel

Washington, DC

Save by registering in advance. Early-bird registration ends January 5.

End-of-Year Wrap Up

By Tony Roda

Photo illustration © 2023, istock.com

In the final days of the 117th Congress, the House and Senate gave approval to a massive $1.7 billion, end-of-year omnibus appropriations bill, which President Biden signed into law on December 23, 2022. The major retirement bill, which is commonly known as the SECURE Act 2.0, was included in the omnibus funding bill.

NCPERS and its fellow stakeholders in the public pension community spent countless hours working on this legislation, particularly in seeking to remove an administrative burden on our plans that has prevented many retired first responders from being eligible for the income exclusion under the Healthcare Enhancement for Local Public Safety Act (HELPS) and in ensuring that problematic proposals were kept out of the bill. I am pleased to report that we were successful on both counts.

The key provisions of the SECURE Act 2.0 affecting public safety employees are as follows:

- Make the requirement for direct payment by a retirement system under HELPS optional instead of mandatory;
- Exclude from income certain disability payments to retired first responders;
- Modify the exemption from the early withdrawal penalty for first responders from "age 50" to "age 50 or 25 years of service under the plan, whichever is earlier"; and
- Extend the exemption from the early withdrawal penalty to certain state and local corrections employees.

Additional provisions of interest to state and local governmental retirement plans include the following:

- Increase the age trigger for Required Minimum Distributions from defined benefit and defined contribution plans to age 73 in 2023 and then to 75 in 2033;
- Increase the annual limit on catch-up contributions in defined contribution plans to $10,000 for those age 60, 61, 62, and 63;
- Permit employer matching contributions on account of student loan payments;
- Provide flexibility for plan fiduciaries when seeking to recoup inadvertent retirement plan overpayments;
- Eliminate the first day-of-the-month rule for 457(b) plans to provide more flexibility for participants to make changes in elective deferral amounts; and
- Require the Roth method (contributions must be made with after-tax dollars) for catch-up contributions for those who earned more than $145,000 from the employer sponsoring the retirement plan.

Also of interest to our plan fiduciaries, in late November the U.S. Department of Labor released its final regulation on fiduciary responsibilities related to environmental, social, and governance

(ESG) investing and proxy voting and shareholder rights. The final regulation was promulgated under the authority of the Employee Retirement Income Security Act (ERISA). ERISA does not govern state and local governmental retirement plans. However, state and local officials, public pension boards, investment committees, and in-house and outside counsel often take DOL's regulatory pronouncements into consideration as they develop fiduciary standards and guidelines for investment-related decisions.

It's difficult to read any investment or financial media without seeing articles devoted to ESG investing. It has become a topic of heated debate. The bottom line, however, is that pension plan trustees and other fiduciaries must adhere to their basic fiduciary responsibilities of loyalty and prudence (including the duties of care, skill, and diligence) when making investment decisions.

The final regulation released by the Biden Administration makes clear at the outset that a fiduciary shall discharge their duties "…for the exclusive purpose of providing benefits to participants and their beneficiaries…" Furthermore, the regulation states that, "A fiduciary may not subordinate the interests of the participants and beneficiaries…and may not sacrifice investment return or take on additional investment risk to promote benefits or goals unrelated to interests of the participants and beneficiaries in their retirement income or financial benefits under the plans."

The final regulation also moves away from the standard included in the proposed regulation, which was "(t)he projected return of the portfolio relative to the funding objectives of the plan, which may often require an evaluation of the economic effects of climate change and other environmental, social, or governance factors on the particular investment or investment course of action." (Emphasis added.) While the proposed standard was still discretionary because of the use of the word "may," it would have taken us right to the brink of a regulatory requirement that in order to meet the fiduciary duty of prudence a fiduciary must consider ESG factors in all investment decisions.

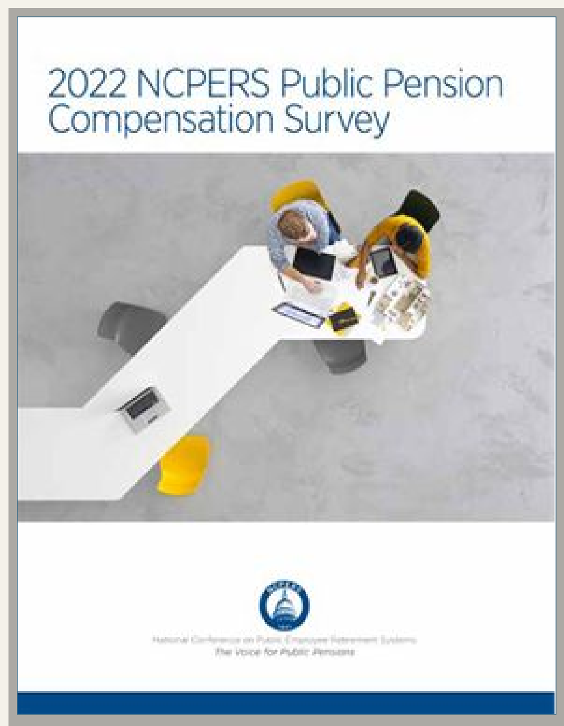
Instead, the final regulation, in response to commenters who said the proposed language was a de facto mandate to analyze all investments through the ESG lens, replaced that standard with the following:

- Fiduciary's determination…must be based on factors…relevant to a risk and return analysis; risk and return factors may include the economic effects of climate change and other ESG factors; whether any particular consideration is a risk-return factor depends on individual facts and circumstances.

Order your copy of NCPERS 2022 Public Pension Compensation Survey today.

Access in-depth compensation and benefits data from more than 150 public pension funds representing more than 9 million active and retired individuals.

LEARN MORE



DOL's proposed regulation also provided numerous examples of ESG factors, including a corporation's exposure to the real and potential economic effects of climate change including exposure to the physical and transitional risks of climate change, board composition, executive compensation, transparency, and workforce diversity. The final regulation does not include examples of ESG factors.

Regarding fiduciary duties related to proxy voting, the final regulation states that the fiduciary duty to manage plan assets includes the management of shareholder rights, such as the right to vote proxies.

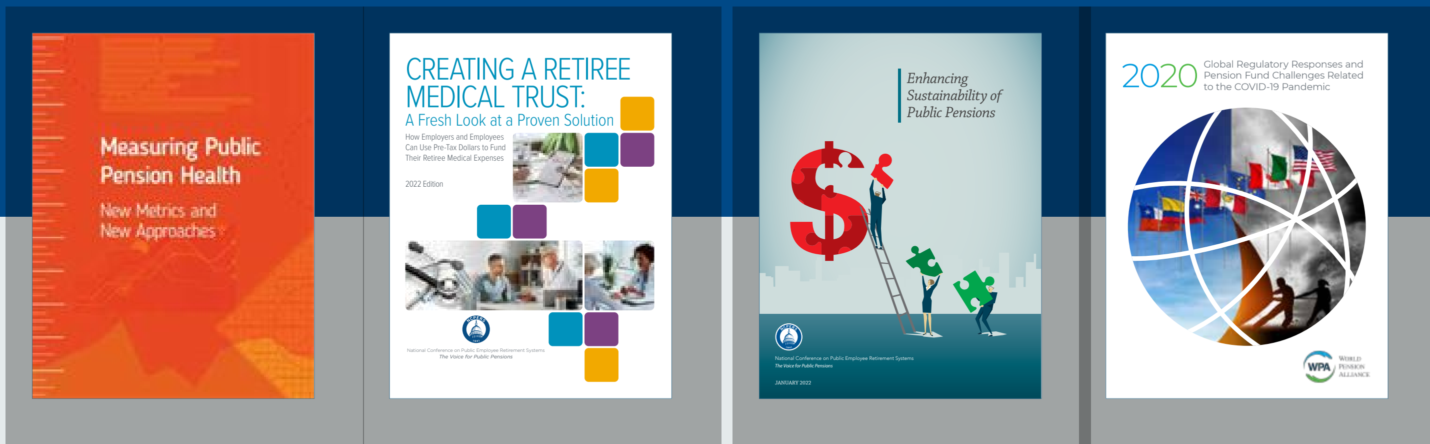
Plan trustees and other fiduciaries must pay close attention to the regulatory framework in their specific states and localities surrounding the use of ESG factors in investment decisions. It is unclear at this early stage whether some states and localities will enact laws parallel to the federal ERISA-based regulation just released.

I hope everyone enjoys the holiday season with family and friends and gets some well-deserved rest and relaxation.

Happy Holidays! ◆

Tony Roda is a partner at the Washington, D.C. law and lobbying firm Williams & Jensen, where he specializes in legislative, regulatory, and fiduciary matters affecting state and local pension plans. He represents the National Conference on Public Employee Retirement Systems and state-wide, county, and municipal pension plans in California, Colorado, Georgia, Kentucky, Ohio, Tennessee, and Texas. He has an undergraduate degree in government and politics from the University of Maryland, J.D. from the Catholic University of America, and LL.M (tax law) from the Georgetown University Law Center.

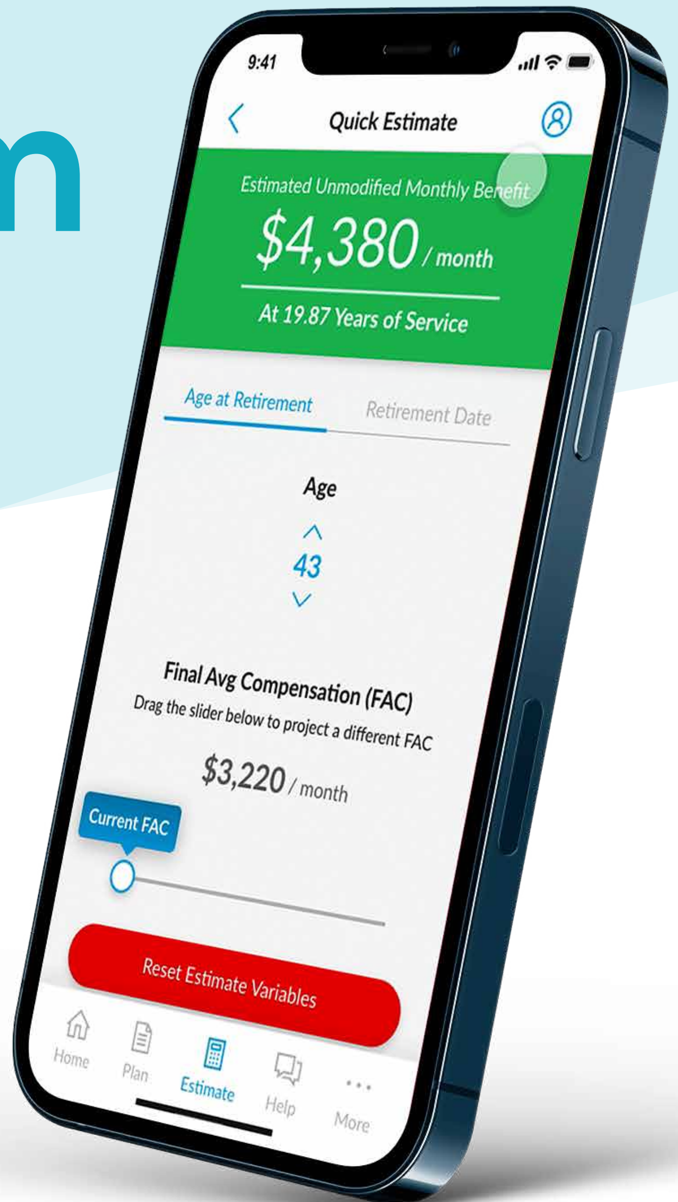
Don't miss the latest research from NCPERS.



Find new metrics and approaches for measuring public pension health, research on how employers and employees can use pre-tax dollars to fund retiree medical expenses, and more.

LEARN MORE

NCPERS PensionX Digital Platform



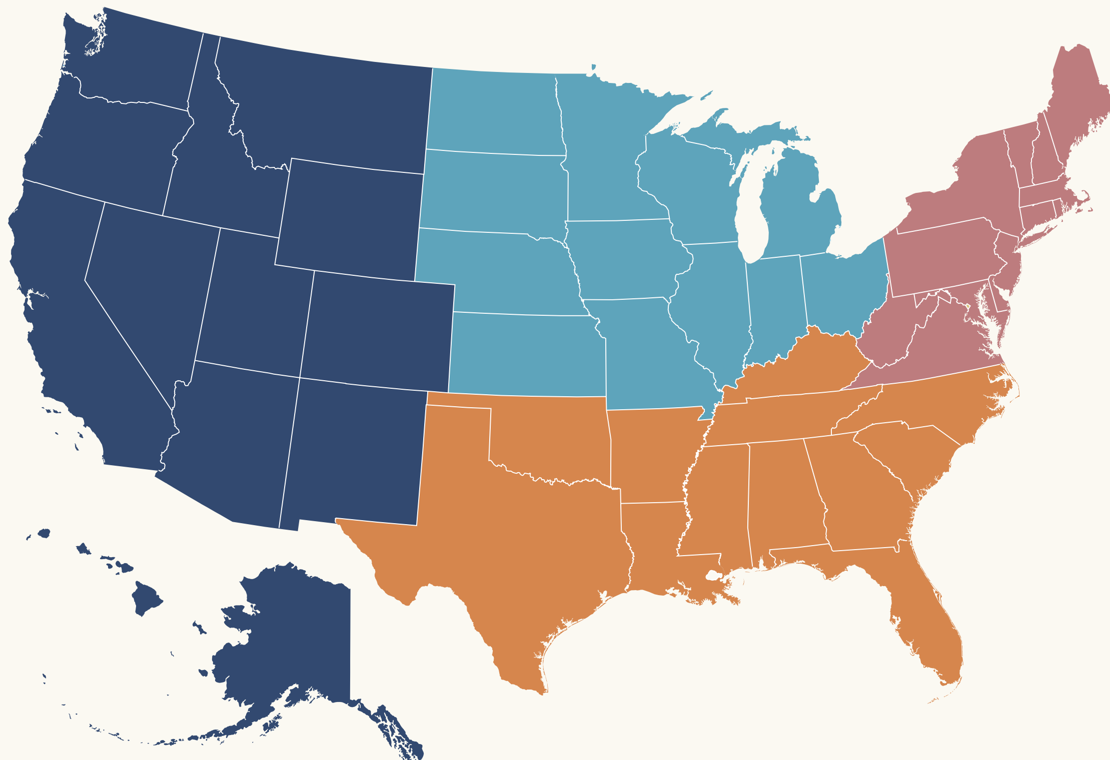
NCPERS has partnered with Digital Deployment to offer its members a **10% DISCOUNT** on PensionX, the premier digital platform that securely enables pensions to engage with active and retired participants via a mobile self-service app and portal.

pensionX

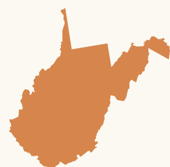
Learn more about this new NCPERS member benefit at ncpers.org/pensionx

NCPERS Around the Regions

This month, we will highlight West Virginia, Illinois, Texas, and California.



NORTHEAST: West Virginia



West Virginia legislators are considering a cost-of-living increase and one-time supplemental payment of $1,500 to state retirees in the Public Employees Retirement System (PERS) and the Teachers Retirement System (TRS).

Attorney Phillip Childs explained during December's interim meeting of the Joint Standing Committee on Pensions and Retirement that, with this possible legislation, retirees with a monthly annuity of $1,000 or less and who have reached age 70 with at least 20 years of service by July 1, 2023 would be eligible for the one-time supplemental payment.

Retirees who make less than $1,000 per month and have reached the age of 70 with at least 25 years of service by July 1, 2023 would qualify for the cost-of-living increase.

Jeff Fleck, executive director of the Consolidated Public Retirement Board, said the total cost for the legislation, currently titled "Senate Bill X" would be $26.5 million.

In June, the Committee heard presentations from several advocacy groups as the cost-of-living increase and supplemental payments were being considered.

"The state will end the fiscal year with a $1.3 billion surplus and the legislature has already appropriated $793 million, leaving our state with a little over $500 million in surplus … We simply must not miss this opportunity to recognize the significant contributions of our state's retirees – not when we have the funds, an unprecedented blessing, that you can choose to use to create meaningful relief to these retirees," said Jane Marks, AARP state president.

NCPERS Around the Regions

MIDWEST: Illinois

In the November 2022 elections, 58 percent of Illinois voters cast their ballot in favor of Amendment 1, also known as the Workers' Rights Amendment.

This controversial amendment prohibits state lawmakers from passing "right-to-work" laws and adds protections to the Illinois state constitution for workers seeking to unionize. Labor groups strongly supported Amendment 1 while groups such as the Illinois Manufacturer's Association claimed it would make hiring more challenging and lead to tax increases.

The passing of the amendment comes just four years after the *Janus v. AFSCME* Supreme Court ruling that determined applying public sector union fees to non-members is a violation of the First Amendment.

Amendment 1 is expected to have a widespread impact on bargaining rights in both the public and private sectors. However, given the broad language of the amendment, questions remain about who is permitted to bargain and the scope of such bargaining.

The amendment allows for employees right to bargain to "protect their economic welfare and safety at work," but it does not specifically define what economic welfare means and, some argue, may extend beyond traditional terms in the National Labor Relations Act.

Although the amendment has now been added to Illinois' state constitution, there continues to be backlash from conservative think tanks and organizations in favor of "right-to-work" laws.

SOUTH: Texas

In 2021, House Bill 3898 was enacted in Texas to establish new expectations for public pensions to aim for 30- or 25-year amortization periods before triggering a remediation plan, reducing the target period from 40 years. The Texas Pension Review Board determined this was the "most appropriate" measure of public retirement system's health.

A new report from the Texas Association of Public Employee Retirement Systems (TEXPERS) highlights the progress public pensions in the state have made in reducing amortization periods. The report also notes that amortization periods are not the only measure of pension fund health.

Fifty-one pension systems for police, firefighters, and municipal employees maintained amortization periods of 25 years or less, compared to 45 systems in the 2020 report. Additionally, the number of systems with a zero-year amortization period doubled in that timeframe. This means ten systems' assets matched their benefit promise liabilities.

Only 29 pension funds were the 'warning range' of 25- to 40-year amortization periods—almost a 20 percent decrease from the previous report.

Art Alfaro, TEXPERS' Executive Director, commented in the release, "Like the last report in 2020, the most promising testament to pension fund management is that amortization periods continued to improve despite while there were serious continuing efforts to lower target rates for investment returns. With the market declines of 2022, this conservative effort will keep pension funds healthy."

May 21–24, 2023
New Orleans, LA
2023
ANNUAL CONFERENCE & EXHIBITION
ACE
Including NCPERS University Programs
TEDS and NAF, May 20–21, 2023

NCPERS Around the Regions

WEST: California

California Public Employees' Retirement System (CalPERS) announced changes to its investment policies for private assets in November. Of note, the $443.2 billion pension fund increased the amount certain staff members can invest without board approval.

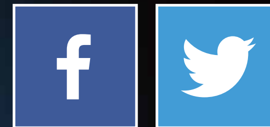
For example, the new policy increases the CIO's commitment and disposition limit in infrastructure to $6 billion from $2 billion. Additionally, prudent person opinions are now required only for transactions that are greater than $250 million for both CIO and managing investment director investment decisions.

Nicole Musicco, chief investment officer at CalPERS, said the policy changes were made to allow for staff to be more agile and responsive as they anticipate continued volatile market conditions in the year ahead. She added that staff wanted to "really make sure we have the appropriate tools in place to execute on the strategic asset allocation that we endeavored starting in July."

The pension fund also announced its decision to consolidate its growth and innovation program with the private equity asset class unit. The private equity unit will be led by Anton Orlich, who was appointed as managing investment director for growth and innovation in October.

Orlich is also tasked with increasing the fund's private equity assets allocation to 13 percent, following a 21.3 percent return from the asset class for the fiscal year ending June 30. ◆

Don't Miss NCPERS' Social Media



The Voice for Public Pensions

Calendar of Events 2023

Photo Illustration © 2023 GPA Photo Archive

January

Legislative Conference

January 22–24
Renaissance Washington, DC
Washington, DC

Pension Communications Summit

January 23–24
Renaissance Washington, DC
Washington, DC

May

NCPERS Accredited Fiduciary (NAF) Program

May 20–21
Marriott New Orleans
New Orleans, LA

Trustee Educational Seminar (TEDS)

May 20–21
Marriott New Orleans
New Orleans, LA

Annual Conference & Exhibition (ACE)

May 21–24
New Orleans, LA

June

Chief Officers Summit

June 19-21
Denver, CO

View all upcoming NCPERS conferences at www.ncpers.org/future-conferences.

2023-2024 Officers

Kathy Harrell
President

Carol G. Stukes-Baylor
Secretary

Dale Chase
First Vice President

Will Pryor
Treasurer

James Lemonda
Second Vice President

Daniel Fortuna
Immediate Past President

Executive Board Members

Dan Givens
Florida

John Neal
Arkansas

David Harer
Alabama

Frank Ramagnano
Canada

Michael Linynsky
Maryland

Tom Ross
Massachusetts

David Kazansky
New York

Ralph Sicuro
Pennsylvania

Sherry Mose
Texas

Ginger Sigler
Oklahoma

The Voice for Public Pensions

The Monitor is published by the National Conference on Public Employee Retirement Systems.
Website: www.NCPERS.org • E-mail: info@ncpers.org

PERSist

The Voice for Public Pensions

Winter 2023 | Volume 36 | Number 1

NCPERS Message

Have Increased Allocations to Alternatives Helped or Hurt Long-Term Investment Performance?

US public pension plans have steadily increased allocations to alternatives over the last twenty years, but has this shift helped or hurt? New research from the Center of Retirement Research (CRR) at Boston College examines the impact of the asset class on pension funds' long-term investment performance.

According to the study, state and local pension funds' aggregate allocations to alternatives in 2022 was 34 percent, up from only nine percent in 2001. This shift towards alternatives has drawn some criticism, as the asset class can be seen as less transparent and more risky compared to equities.

The new research from CRR suggests that, while they have not helped overall returns, alternatives may have helped reduce overall volatility.

Since pensions are long-term investors, the lead researcher, Jean-Pierre Aubry, used regression analysis to look at three periods: 2001-2009 (before and during the great financial crisis), 2010-2022 (post-crisis) and 2001-2022 (pre- and post-crisis). He found that "relative to traditional equities, holding 10 percent more of the plan's portfolio in alternatives is associated with a 66-basis-point increase in the portfolio return from 2001 to 2009 and a 33-basis-point decrease in the return from 2010-2022…the allocation to alternatives had no statistically significant impact on returns when looking over the whole period from 2001 to 2022."

Aubry also found that alternatives did not appear to impact the volatility of reported returns between 2001-2009, but plans with greater allocations to alternatives have had lower volatility in their annual returns since 2010 and during the 2001-2022 period.

In this volatile market, though, there appears to be continued enthusiasm from institutional investors towards alternatives. A

November 2022, Number 22-20

CENTER for RETIREMENT RESEARCH at BOSTON COLLEGE

PUBLIC PENSION INVESTMENT UPDATE: HAVE ALTERNATIVES HELPED OR HURT?

By Jean-Pierre Aubry*

Introduction

Fiscal year 2022 was a difficult one for state and local pension plans, with the decline in the stock market erasing much of the gains from 2021. And, recent media reports by *Pensions and Investments*, the *Wall Street Journal*, and others have suggested that alternative investments are one reason why reported returns don't look worse.[1] But focusing on the short-term impact of specific asset classes ignores the fact that public pensions are long-term investors. The key question is: have alternatives helped or hurt pension funds' long-term investment performance?

The discussion proceeds as follows. The first section reports the long-term performance of public plans since 2001 – including the poor results of 2022. The second section documents public plans' increasing reliance on alternative investments since 2001. The third section examines how the shift towards more alternatives has affected the overall investment performance of public plans. The final section concludes that the performance of pension funds since 2001 has fallen short of actuarial expectations and that the increasing reliance on alternatives certainly has not helped, although it may have dampened reported volatility.

Update on Public Pension Investment Returns

In FY 2021, all state and local plans exceeded their actuarially assumed return, with an average return of about 27 percent compared to the average assumed return of about 7 percent.[2] However, during FY 2022 the financial markets dropped substantially – with public pensions averaging a negative return of 5.5 percent (see Figure 1 on the next page).[3] The dramatic whipsaw in fortunes exemplifies how short-term returns can be problematic for gauging whether pension fund investment performance is adequate. In fact, reviewing performance since 2001 shows that the returns in 2021 and 2022 – while dramatic – continue a historical pattern in which returns come in above the average assumed return about as often as they fall below.

Given the pattern of annual returns above and below expectations since 2001, one might think that performance over the period has roughly met expectations. However, the year-by-year data do not provide an accurate picture of plans' long-term performance. Calculating the annualized return (i.e., the geometric return) from 2001-2022, public plans have averaged only 5.9 percent over the last 22 years.[4] And, while

* Jean-Pierre Aubry is associate director of state and local research at the Center for Retirement Research at Boston College. The author thanks Oliver Shih for excellent assistance in data and research.

new survey from Cerulli Associates found that 44 percent of North American institutional investors say they're likely to increase allocations to alternative investments, citing high inflation (89 percent) and expectations of lower returns (86 percent).

NCPERS tracks public pensions' allocations to each asset class in our annual Public Retirement Systems Study. We'll see how target allocations to alternatives have shifted from 2021 to 2022 in the latest report, which will be released in early 2023.

Alternatives can play an important role in a diversified portfolio, and NCPERS will continue to share the latest research on their impact on long-term investment performance. In 2023, we will also be hosting a webinar on the topic—stay tuned for details. ◆

In This Issue

3 Managing Cybersecurity Risk in the Investment Area – a Focus on the Capital Call Business Process

Understanding how threat actors can compromise the Capital Call process, establishing controls to check the legitimacy of a transaction, and working with investment groups is crucial to protecting a fund's assets.

5 Why Pension Consolidation is Gaining Traction Across the Globe

Global funds are continuing to rethink their pension models. This article explores successful models of pension consolidation around the world.

7 Navigating the Financial Vortex: From Retirement Readiness to Retirement Income

Goldman Sachs Asset Management's Retirement Survey & Insights Report 2022 takes a closer look at the diverse needs of two types of investors—those still working and those who have already retired—and the unique challenges they face in today's environment.

10 Diverse Manager Investing: Performance, Growth, and Access to Information

The diverse investment manager market continues to grow as LPs increasingly take note of the alpha potential and expanding opportunity set. While market headwinds are creating a challenging fundraising environment for managers, there is more research, resources, and information available to help LPs invest with intention.

14 Why Pension Fund Portfolios May Deliver Unpleasant Surprises

The Risk Report: 2022 Edition uncovers the prominence of uncompensated versus compensated risks in institutional portfolios—and what might be diluting their potential for excess returns.

17 Securities Class Action Settlements and SEC Fair Funds: What's the Difference?

Securities class action settlements and Securities and Exchange Commission (SEC) Fair Funds may look similar, however, the actors involved – and their motivations – differ in fundamental ways resulting in challenges for participating institutional investors.

19 The Rule of Three: Inflation, Recession, Growth

The number three is pervasive through some of society's greatest stories—there were three little pigs, three musketeers, and three stooges, for example. In keeping with that concept, here are my big three for investors to consider: recessionary fears, high inflation, and slowing growth.

21 Why Mortality Improvement Scales Matter

For the first time since the Society of Actuaries (SOA) began publishing annual mortality improvement scales for pension plans in 2014, it did not release an updated scale in 2022.

Managing Cybersecurity Risk in the Investment Area – A Focus on the Capital Call Business Process

By: Peter Dewar and Joe Potischman, Linea Secure

Photo illustration © 2023 shutterstock.com

When pension funds have taken a position on an investment asset and need to fund that position, they engage in a business process known as a Capital Call. In doing so, a communication stream is initiated, and the transfer of funds process begins where an investment manager requests funding of the position by notifying the Chief Investment Officer or a representative from the investments department. This starts an internal process whereby funds are transferred many times from custodial accounts to external parties.

There are frequent places for potential threat actors to insert themselves into the communication stream with the end goal of eventually redirecting the funds to themselves. Understanding how threat actors can compromise the Capital Call process, establishing controls to check the legitimacy of a transaction, and working with investment groups is crucial to protecting a fund's assets.

Potential Risks in the Capital Call Process

There may be the case that a threat actor has already compromised the email of a fund employee involved in the funding process via a phishing attack. They may not strike right away, but as advanced persistent threat actors tend to do, they wait for an opportunity to take advantage of their escalated access. For instance, they can read the minutes of closed investment committee meetings to understand what positions the funds are looking to take. Once they know the investment positions, they can insert themselves into the communication stream and request a transfer of funds themselves.

There are frequent places for potential threat actors to insert themselves into the communication stream with the end goal of eventually redirecting the funds to themselves.

A less sophisticated threat actor can attempt to impersonate the investment manager or other staff as well to compromise a staff member. They may present themselves as the Chief Investment Officer asking the Chief Financial Officer to transfer funds to an external account or they may present themselves as a third-party representative.

While no one wants to believe they could be subjected to insider threats by those on their staff, fund employees can manipulate internal transactions in their favor. In fact, the insider threat is the second largest cybersecurity risk to organizations, second only to phishing attempts. If an employee is privy to valuable insider information, they can use this knowledge to compromise internal controls and redirect funds to their benefit or provide the information to an external collaborator for them to act on.

Establishing Cybersecurity Controls to Prevent Fraud

If a fraudulent Capital Call transaction is processed and remains undetected, it can be hard to trace and recover financial transactions over time. Having the right cybersecurity controls in place can help prevent these transactions from occurring or stop ones in progress. Some controls that can be implemented by organizations include:

- Role-based separation of duties to ensure that no one person can see the Capital Call process all the way through
- Continuous background checks to see if the financial situation has changed for staff
- Confirmations from multiple parties via an encrypted communication channel

It is important to make sure that these controls are not just present at the pension fund but with third-party investment partners as well, so it is advisable to have an agreement with investment managers for the management of cybersecurity risk. Many investment firms often operate on an opaque level regarding back-office operations and many of these firms may not have gone through the Service Organization Controls (SOC) accreditation process. The pension fund working with third-party firms should validate that due diligence is being performed internally at these service organizations. ◆

__Peter Dewar, President__ has over 25 years of experience in cybersecurity and leads the cybersecurity practice for the Linea group of companies that provide services across the United States and Canada. Under his leadership Linea has developed a Pension Cyber Security Framework (PCSF) to complement the generalized standards for protecting information systems. The PCSF focuses on the business process employed, services provided, and technology utilized by pension and benefits organizations, and devises controls to minimize and mitigate the inherent cybersecurity risk experienced by the industry.

Peter has a Master's degree in Information Systems from the George Washington University, a Bachelor's degree in Information Systems from the University of the District of Columbia, is a Certified Information Systems Security Professional (CISSP), Certified Data Privacy Security Engineer (CDPSE), and has received certificates of achievements from the Harvard Kennedy School of Government, Gartner CIO Academy, and International Foundation of Employee Benefit Plans.

__Joe Potischman, Marketing Specialist__ is the marketing specialist for Linea Secure with over 5 years of experience in the professional services industry. With his work, Linea has been able to present at over 15 separate engagements and has been published by multiple pension and benefit associations. Joe has a Master's degree in Communication, Culture & Technology from Georgetown University and a Bachelor's degree in Intercultural Communication from the State University of New York at Geneseo. He has also received a Certificate of Achievement in Public Plan Policy from the International Foundation of Employee Benefit Plans (IFEBP). Prior to working for Linea, he managed, CommLawBlog, an award-winning blog on Communications Law & Policy.

NCPERS Custodian Bank

Why Pension Consolidation is Gaining Traction Across the Globe

By: Jeff Porta, Northern Trust Corporation

Photo illustration © 2023 shutterstock.com

Strength in numbers is one of the reasons pension consolidation is trending around the globe. The challenges facing smaller funds, including oversight, cost, maintenance and management, can hinder asset performance. Plus, smaller funds may have limited access to asset managers or types of investments that improve diversification and returns. By consolidating, funds can reduce costs while increasing efficiency.

Around the world, there are successful models of pension consolidation. The Netherlands, the UK, Australia and Canada have been bringing their retirement assets together for years, and in the Middle East, consolidation is growing in popularity.

The Netherlands is a pioneer of pension consolidation, with the total number of pension funds decreasing from about 1,000 in 2000 to less than 200 in 2022.[1] The vast majority[2] (94%) of its pensions are in defined benefit (DB) schemes, but in 2023 will transition to two types of defined contribution (DC) contracts.

In the U.K., occupational DC pension plans decreased by nearly 40% from 45,150 funds in 2011 to 27,700 in 2021.[3] On the DB side, more than 80 local government pension funds pooled their assets in 2018[4,5] into eight separate pools and are expected to consolidate to three pools by 2030.[6,7]

Around the world, there are successful models of pension consolidation.

With significant growth in its superannuation funds, Australia has one of the world's largest pension pools.[8] Growing performance scrutiny and pressure on smaller funds has increased. APRA, Australia's prudential regulator for the financial services industry, said in 2021 that funds with assets less than A$30 billion are "uncompetitive".[9]

As another pioneer of the large public pension fund model, Canada's Ontario Teachers' Pension Plan has approximately $242 billion in net assets. Looking at the success of this model, 72% of Canadian pension funds surveyed in 2021 were considering consolidation.[10]

In the Middle East in 2021, aiming to cut costs, help investment returns and increase efficiency, Oman merged eight pension funds into two.[11]

And in the U.S., the State of Illinois enacted the Pension Consolidation Act in 2020, merging municipal fire and police pension plans into the Illinois Firefighters' Pension Investment Fund and the Illinois Police Officers' Pension Investment Fund.

Global funds are continuing to rethink their pension models. When considering the increased efficiency and cost savings of a consolidated pool, it is a trend worth watching. ◆

Footnotes:

1. Netherlands: Pension transition drives consolidation | Country Report | IPE
2. https://www.thinkingaheadinstitute.org/content/uploads/2021/02/GPAS_2021.pdf
3. Defined contribution pension market consolidation continues, TPR's latest figures show | The Pensions Regulator
4. https://mycouncil.surreycc.gov.uk/documents/s73145/14%20-%20Annual%20Report%202019-20%20-%20Annexe%201.pdf
5. http://www.lgpsboard.org/index.php/schemedata/scheme-annual-report
6. https://www.lgcplus.com/investment/lgps-pools-expected-to-further-consolidate-18-07-2019/
7. http://www.lgpsboard.org/index.php/schemedata/scheme-annual-report
8. Australia's top pension fund warns against tapping savings to fix economy | Reuters
9. Australian Pension Fund Chairman Urges Caution on Consolidation - Bloomberg
10. 72% of Canadian pension funds considering consolidation options: survey | Benefits Canada.com
11. Pensions, sovereign wealth funds, and industrial policy in the Gulf: A look at fund consolidation | Middle East Institute (mei.edu)

Jeff Porta *is a Senior Vice President and the Practice Executive in our Asset Servicing Business Unit. In this capacity, Jeff is responsible for leading teams of client facing professionals who serve the financial needs of our public and corporate pension funds, taft-hartley, healthcare, foundation, endowment and religious institutional clients. Jeff's responsibilities span the full spectrum of the business, with the goal of providing outstanding client experiences, sustainable growth of the business and mentoring and providing career opportunities for Northern Trust partners.*

Jeff received a B.S. degree in finance from Babson College, Wellesley, Massachusetts.

2023 LEGISLATIVE CONFERENCE
January 22 – 24
Renaissance Washington, DC Hotel
Washington, DC
Save by registering in advance. Early-bird registration ends January 5.

Navigating the Financial Vortex: From Retirement Readiness to Retirement Income

By: Chris Ceder, Senior Retirement Strategist at Goldman Sachs Asset Management

Photo illustration © 2023 shutterstock.com

Rising interest rates, high inflation and market volatility are making it challenging for many investors to generate sustainable income and putting a strain on their finances. Goldman Sachs Asset Management's Retirement Survey & Insights Report 2022 takes a closer look at the diverse needs of two types of investors—those still working and those who have already retired—and the unique challenges they face in today's environment.

Realities of Retirement

We surveyed 1,566 individuals and found more than half (51%) of retirees we spoke to report that their current income is less than 50% of their pre-retirement income. Reaching retirement with sufficient savings is only getting more difficult for working generations, as many fear they will fall short of the savings needed for a comfortable retirement. Those drawing closer to retirement are considering various options to help generate income once they've stopped working full time, with part-time work being the preferred method for many. This suggests that many respondents who can still work after retiring want to have more control over their ability to generate income during retirement. Having some income can add a sense of security, particularly in volatile times.

The Forgotten Generation

Generation X is being forced to juggle competing financial priorities while trying to save for retirement. Often viewed as the "sandwich generation"—in the prime of their careers and at a critical stage for retirement savings and preparation—the members of Gen X are homeowners, parents, and caretakers. They are most likely to have significant retirement balances and therefore are most susceptible to market volatility and inflation. Unsurprisingly, a significant portion (65%) of Gen X reported being stressed about managing their retirement savings and more than half said they feel they are behind schedule.

Retiree Top Concerns

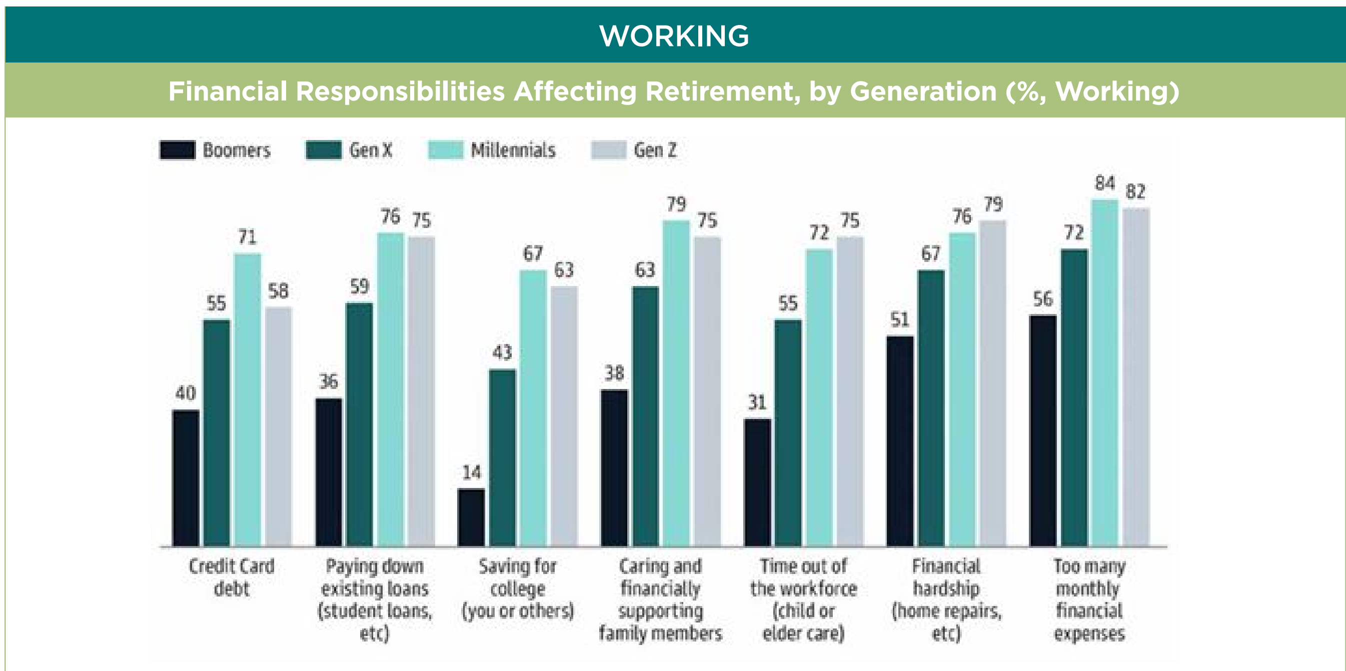
Retirees face a confluence of factors in retirement that can affect their ability to generate income. Their most pressing concern today is inflation (71%). Many have reduced spending as prices for goods and services rise to avoid depleting their savings. Retirees were also concerned about meeting future healthcare needs (51%) and about potential reductions in Social Security (46%). Notably, relative to last year's report, concerns were up across the board across all factors measured highlighting the higher sense of concern retirees feel in this market environment.

Growing Appetite for Advice

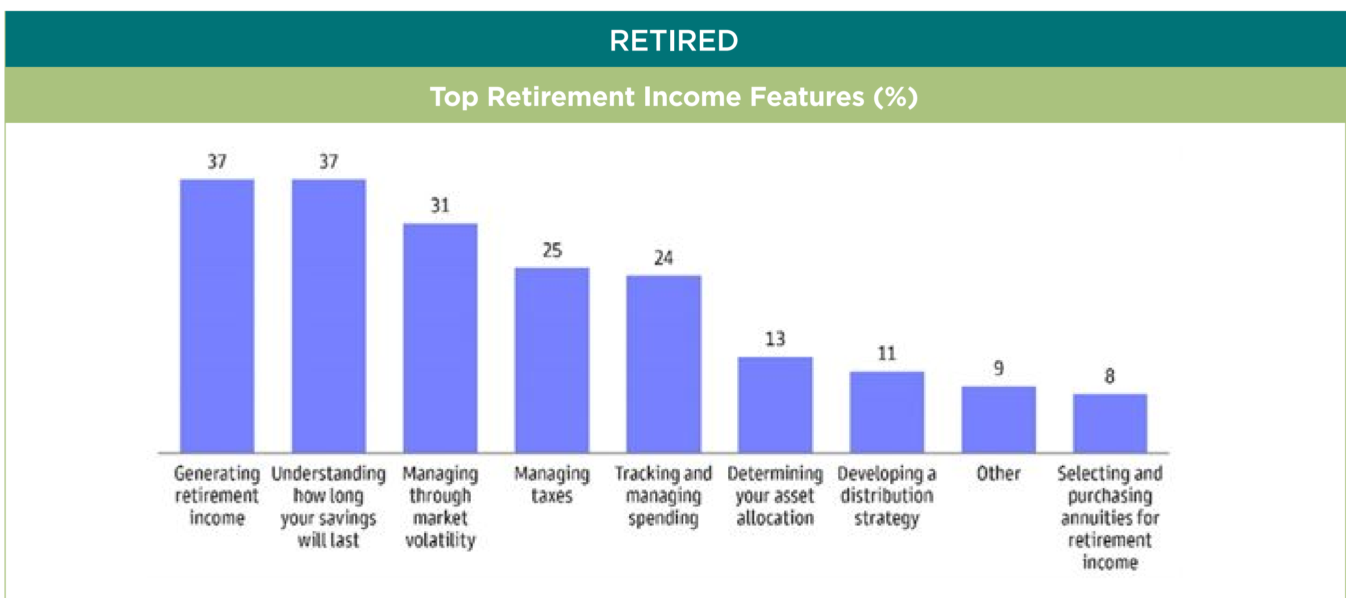
The challenges associated with adequately saving for retirement over a 40-year career has driven many to seek financial help. Nearly all working respondents (95%) and more than three-quarters of retired respondents (79%) believe financial help is important for successfully managing retirement savings, income and investments. This includes counseling, advice and guidance. Sponsors seeking to expand their plan offerings may want to consider addressing the unique needs their plan participants face and provide resources to personalize their savings and investing strategy to meet individuals where they are on their retirement savings journey.

Planning for and Living in Retirement

How strongly did the below affect your ability to save for retirement? (Select from extremely, very, moderately, slight and did not affect)[1]



What are the top challenges you face managing your retirement income and investments that you would like advice / guidance?



DISCLOSURES

[1] Survey participants were asked to select responses based on what has extremely, very, moderately, slightly or no impact on their ability to save for retirement. We are reporting extremely, very and moderate responses.

THESE MATERIALS ARE PROVIDED SOLELY ON THE BASIS THAT THEY WILL NOT CONSTITUTE INVESTMENT ADVICE AND WILL NOT FORM A PRIMARY BASIS FOR ANY PERSON'S OR PLAN'S INVESTMENT DECISIONS, AND GOLDMAN SACHS IS NOT A FIDUCIARY WITH RESPECT TO ANY PERSON OR PLAN BY REASON OF PROVIDING THE MATERIAL OR CONTENT HEREIN. PLAN FIDUCIARIES SHOULD CONSIDER THEIR OWN CIRCUMSTANCES IN ASSESSING ANY POTENTIAL INVESTMENT COURSE OF ACTION.

The views expressed herein are as of 10/12/2022 and subject to change in the future. Individual portfolio management teams for Goldman Sachs Asset Management may have views and opinions and/or make investment decisions that, in certain instances, may not always be consistent with the views and opinions expressed herein. Views and opinions expressed are for informational purposes only and do not constitute a recommendation by Goldman Sachs Asset Management to buy, sell, or hold any security. This information discusses general market activity, industry or sector trends, or other broad-based economic, market or political conditions and should not be construed as research or investment advice.

CONFIDENTIALITY

No part of this material may, without Goldman Sachs Asset Management's prior written consent, be copied, photocopied or duplicated in any form, by any means, or (ii) distributed to any person that is not an employee, officer, director, or authorized agent of the recipient.

© 2022 Goldman Sachs. All rights reserved. 300862-OTU-1714462

Chris Ceder *is a retirement strategist at Goldman Sachs Asset Management focused on retirement and financial wellness client strategies as well as providing retirement research and insights for advisors and clients. Chris previously worked in the Goldman Sachs Human Capital Management for 15 years managing the Goldman Sachs' retirement plans and financial wellness program where his responsibilities included managing strategy, design and operations for Americas retirement plans, along with global oversight of retirement plan governance for retirement programs. Chris received his MBA from Columbia University and received a BS in Business & Economics from Villanova University.*

May 21–24, 2023

New Orleans, LA

2023

ANNUAL CONFERENCE & EXHIBITION

ACE

Including NCPERS University Programs

TEDS and NAF, May 20–21, 2023

NCPERS Asset Manager

Diverse Manager Investing: Performance, Growth, and Access to Information

By: Derek Jones, Managing Director, Private Equity Investments, GCM Grosvenor

Photo Illustration © 2023 sistock.com

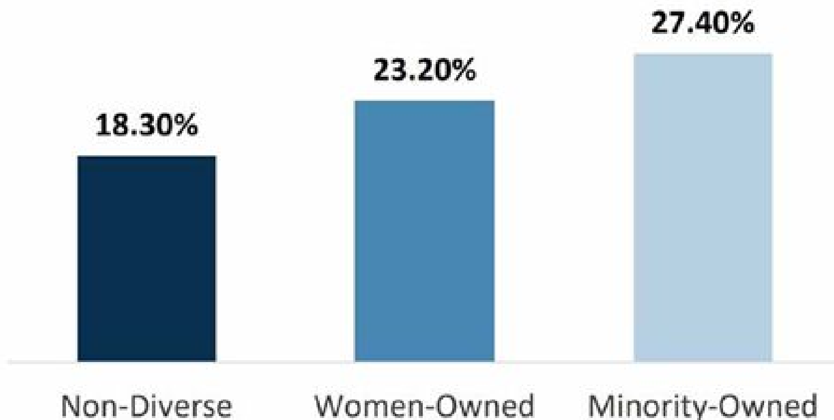
The diverse manager market continues to grow as LPs increasingly take note of the alpha potential and expanding opportunity set offered by these managers. Although this number remains low relative to total industry AUM, there is more research, resources, and information available to help LPs invest with intention. And, while market headwinds are creating a challenging fundraising environment for managers, the work of industry stakeholders is providing the tailwinds to further incentivize investors to allocate for impact.

The diverse manager market is no longer a niche segment. **Recent growth of women- and minority-owned private equity firms outpaced that of their non-diverse counterparts.**

Further, since 2012, the number of funds in the GCM Grosvenor universe of diverse private equity managers has grown 10x and commitment dollars have grown nearly 12x.

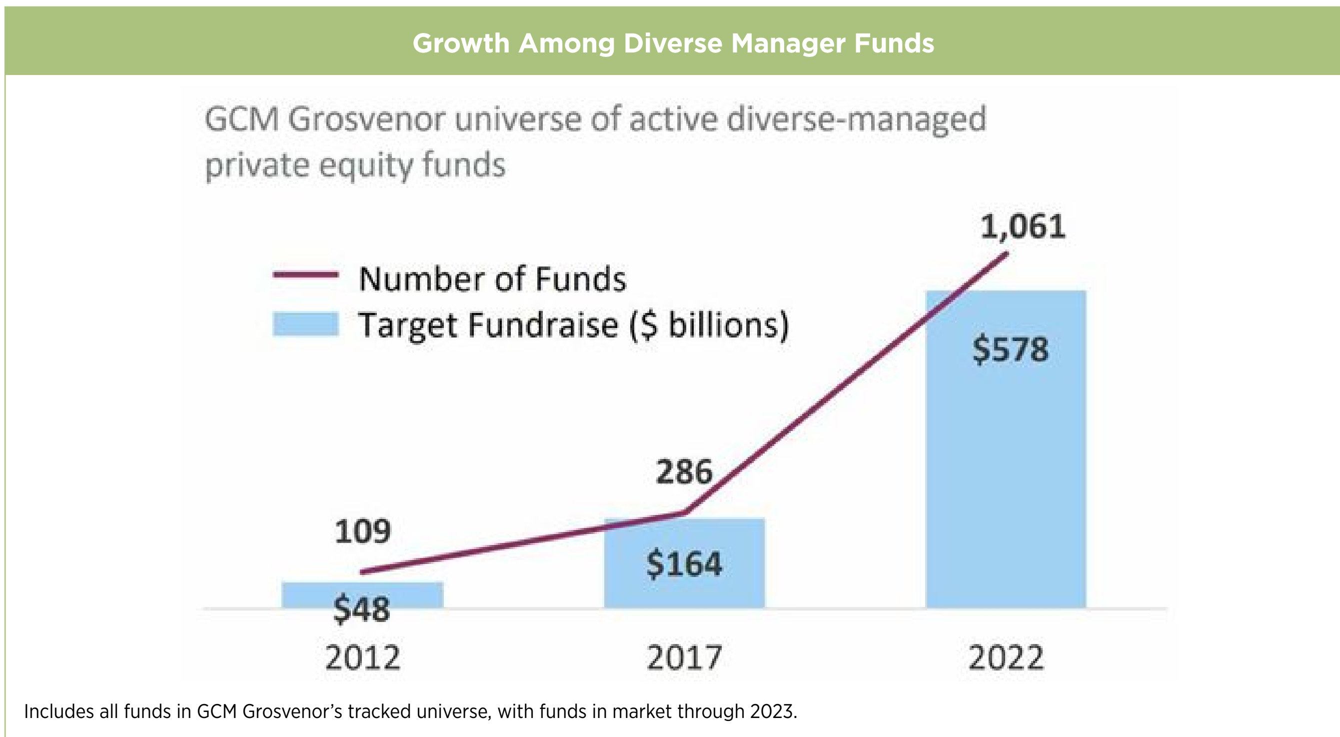
In its 2021 report, “Examining the Returns,” the National Association of Investment Companies (NAIC) showed that **diverse managers have demonstrated consistent outperformance**. Among the findings, the NAIC diverse manager index produced higher net MOICs than the Burgiss Median Quartile in 83.3% of the vintage years studied.

Diverse Firms Growing More Than Non-Diverse



Source: Knight Foundation and Bella Research.

Growth Among Diverse Manager Funds

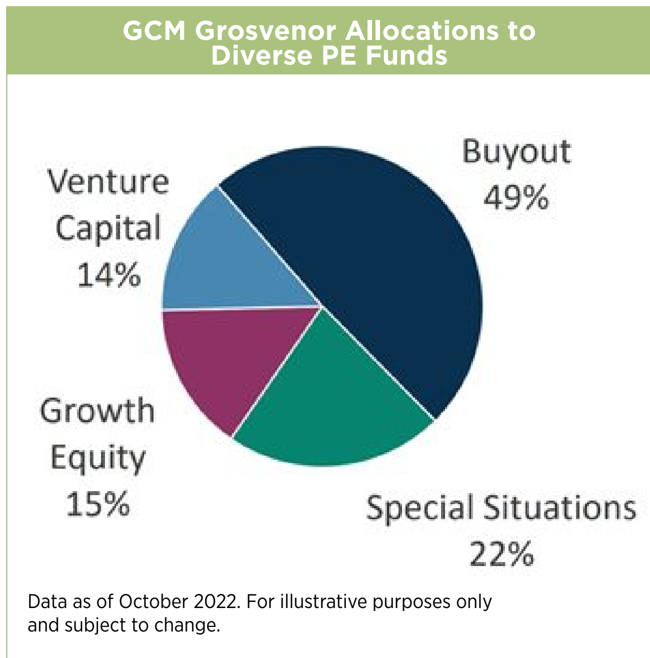


Includes all funds in GCM Grosvenor's tracked universe, with funds in market through 2023.

Looking at sources of performance, a common misconception is that diverse managers are limited to venture capital firms. While the diverse manager market skews toward venture capital, **LPs have more ways to capture alpha than they may think**. Thus, at GCM Grosvenor, we allocate to more middle- and lower-middle-market buyout managers than the overall market.

In addition, beyond primary funds, there are opportunities for alpha generation through co-investing, anchor/seed investing, and by investments in a diverse manager at the GP level.

GCM Grosvenor Allocations to Diverse PE Funds



Data as of October 2022. For illustrative purposes only and subject to change.

Better information from several sources is helping guide the judgement of institutional investors seeking to invest with diverse managers.

- Advisors are increasingly providing LPs with access to diverse managers along with the expertise to implement investments.
- Dozens of industry organizations are contributing to the advancement of diverse professionals and diverse-led firms. Their objectives are in alignment with interested LPs, and they are providing information and resources that promote better decision-making.
- Industry stakeholders are working toward a universal definition of "diverse," which would promote a more efficient marketplace, better-informed LPs, and, ultimately, increased allocations.

Meanwhile, regulations, policies, and other **industry initiatives are expected to buffer the diverse manager industry**, boost its appeal, and incentivize more LPs to allocate to diverse managers. Many states, agencies, and plans themselves are rolling out programs designed to enact positive change and further investment. In addition, industry organizations including ILPA, the PRI, and the CFA Institute have launched initiatives to help LPs better understand and invest with diverse managers.

While we are encouraged by the abundance of talent in the diverse managers industry, we recognize the headwinds. For one, the "denominator effect" may hinder the fundraising of diverse managers, particularly in private markets, as institutional investors take actions to rebalance their portfolios. In addition, during times of market stress, LPs may not be as keen to invest with early-stage managers, which includes many diverse managers. Instead, these

LPs may invest with those they know or limit their allocations to more established diverse managers.

But we remain optimistic, given that these and other issues are front-of-mind and are being addressed by LPs, GPs and other stakeholders. ◆

Read the full version of this article on our website here.

Derek Jones, Managing Director, Private Equity Investments, GCM Grosvenor is a member of the Private Equity, Real Estate, and Infrastructure Investment Committee and the Diversity, Equity, and Inclusion Committee. He also heads the firm's private equity diverse manager practice. His responsibilities include deal sourcing and investment underwriting activities. Prior to joining GCM Grosvenor, Mr. Jones was a Managing Partner at Oncore Capital, as well as a General Partner at Provender Capital. Mr. Jones received his Bachelor of Arts in Economics from American University and his Master of Business Administration in Finance from New York University.

Disclaimer:

Investments in alternatives are speculative and involve substantial risk, including market risks, credit risks, macroeconomic risks, liquidity risks, manager risks, counterparty risks, interest rate risks, and operational risks, and may result in the possible loss of your entire investment. For informational purposes only and not intended to serve as a forecast, a guarantee of future results, investment recommendations or an offer to buy or sell securities by GCM Grosvenor. Investment strategies mentioned are not personalized to your investment objectives, and differences in account size, the timing of transactions and market conditions prevailing at the time of investment may lead to different results. Certain information included herein may have been provided parties not affiliated with GCM Grosvenor and GCM Grosvenor has not independently verified such information. **Past performance is not necessarily indicative of future results. No assurance can be given that any investment will achieve its given objectives or avoid losses.**

2023 PENSION COMMUNICATIONS SUMMIT

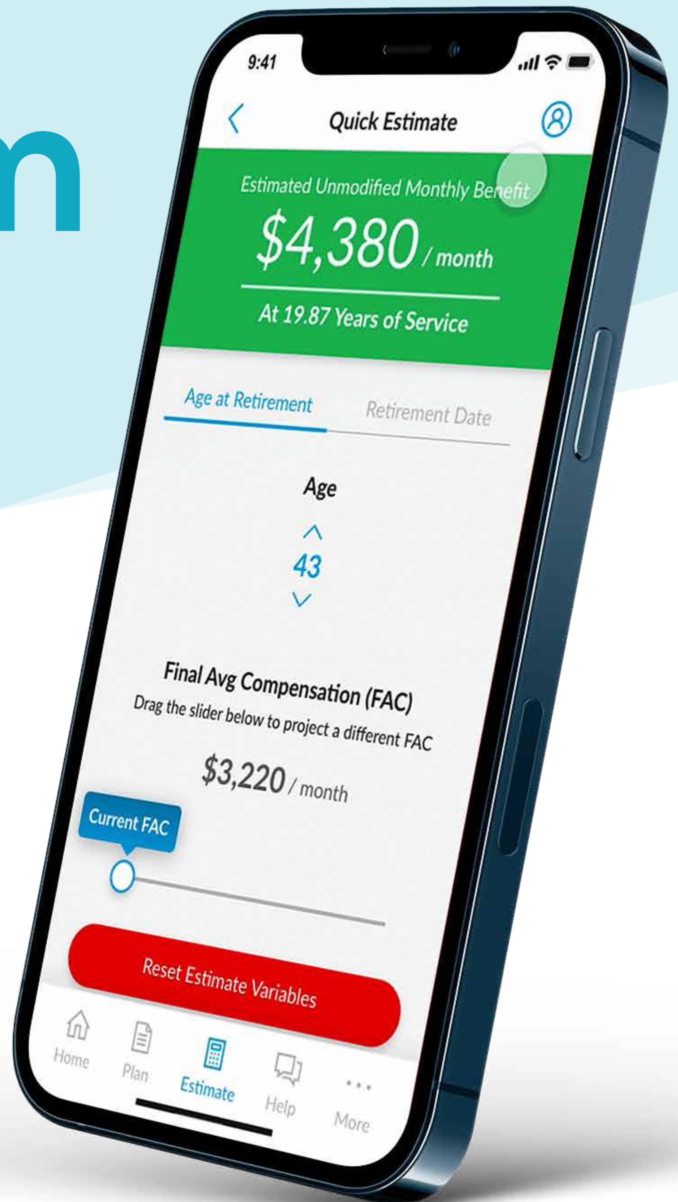
January 23 – 24

Renaissance Washington, DC Hotel

Washington, DC

Save by registering in advance. Early-bird registration ends January 5.

NCPERS PensionX Digital Platform



NCPERS has partnered with Digital Deployment to offer its members a **10% DISCOUNT** on PensionX, the premier digital platform that securely enables pensions to engage with active and retired participants via a mobile self-service app and portal.

pensionX

Learn more about this new NCPERS member benefit at ncpers.org/pensionx

NCPERS Asset Manager

Why Pension Fund Portfolios May Deliver Unpleasant Surprises

By: Bob Parise, Practice Lead, Public Funds and Taft-Hartley Plans, Northern Trust Asset Management

In order to analyze their portfolios to determine reasons for outcomes that differ from intended results, pension funds regularly partner with Northern Trust Asset Management. To help pension funds and other institutional investors better understand risks in their portfolios, we surfaced six common drivers of unexpected results in the inaugural Risk Report, published in 2020. Two years later, with the additional analysis of $50 billion of assets, the 2022 edition of the report provides an updated view on how institutional portfolios have evolved in a vastly different market environment.

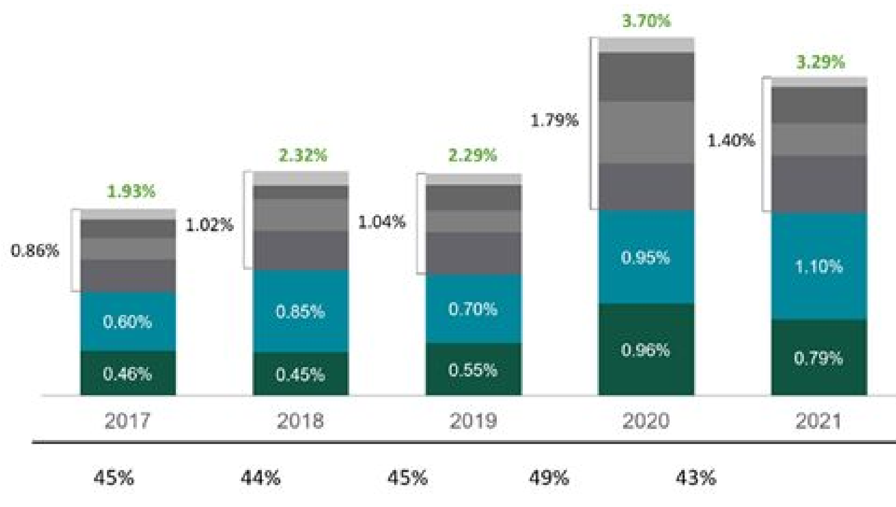
Photo illustration © 2023 shutterstock.com

The Risk Report: 2022 Edition uncovers the prominence of uncompensated versus compensated risks in institutional portfolios—and what might be diluting their potential for excess returns.

Pensions Are Taking Risks...Just Not All the Good Kind

Active risk is necessary to generate excess returns, but not all risks are created equal. Some have been historically proven to generate

EXHIBIT 1: AVERAGE ACTIVE RISK IN EQUITY PORTFOLIOS



Source: Northern Trust Asset Management

excess returns over long periods (compensated risks) and some have not (uncompensated risks):

- Compensated risks include exposures to small-size, low-volatility, high-momentum, high-value, high-dividend and high-quality securities — all of which have historically outperformed over time, based on academic studies.[1]
- Uncompensated risks include exposures to changes in foreign currencies, styles such as large-cap and low-value (expensive), country- or region-specific exposures, and significant over-/under-weights to sectors.

We found that institutional investors across segments took nearly two times more uncompensated risks — or risks that are not sufficiently rewarded by return — than compensated risks. Uncompensated risks made up nearly 50% of total portfolio active risk, resulting in benchmark-like returns or underperformance, as shown in Exhibit 1. At times, investors took these risks intentionally, but we found most times they did not and consequently surprised them.

The Cancellation Effect Can Impact Outcomes

While adding managers into the portfolio lineup can potentially reduce overall risk, our analysis showed risks that were ultimately reduced were often different from what was intended as managers frequently cancelled each other out.

We found that institutional investors across segments took nearly two times more uncompensated risks — or risks that are not sufficiently rewarded by return — than compensated risks.

For example, one manager may take a 3% overweight position in a company while another manager is 3% underweight, effectively cancelling each other out. Or, a high-value bias in one strategy is offset by a high growth bias in another strategy.

This is known as the *cancellation effect* and is caused by unknown, offsetting exposures among underlying holdings that continue to deteriorate away the ability to generate excess returns. In 2020 and 2021, 50% of the active risk generated by higher-active risk managers was lost at the portfolio level due to the cancellation effect.

Capturing just 50% of targeted active risk while paying 100% of the manager fees effectively translates into paying two times more for each realized basis point of active risk than originally thought. Exhibit 2 shows risk taken by underlying investment managers versus aggregated institutional portfolios.

EXHIBIT 2: AVERAGE ACTIVE RISK BY CALENDAR YEAR UNDERLYING INVESTMENT MANAGERS VS. AGGREGATED INSTITUTIONAL PORTFOLIOS

Source: Northern Trust Asset Management

Conclusion

Our comprehensive work with large institutions across the globe provided a distinct opportunity to uncover key trends across various asset pools. The aggregation of this analysis led to six key discoveries by our experts, two of which we explored above. For more findings, download *The Risk Report: 2022 Edition*. ◆

IMPORTANT INFORMATION

For disclosure information please see page 18 of The Risk Report.

© 2022 Northern Trust Corporation. Head Office: 50 South La Salle Street, Chicago, Illinois 60603 U.S.A.

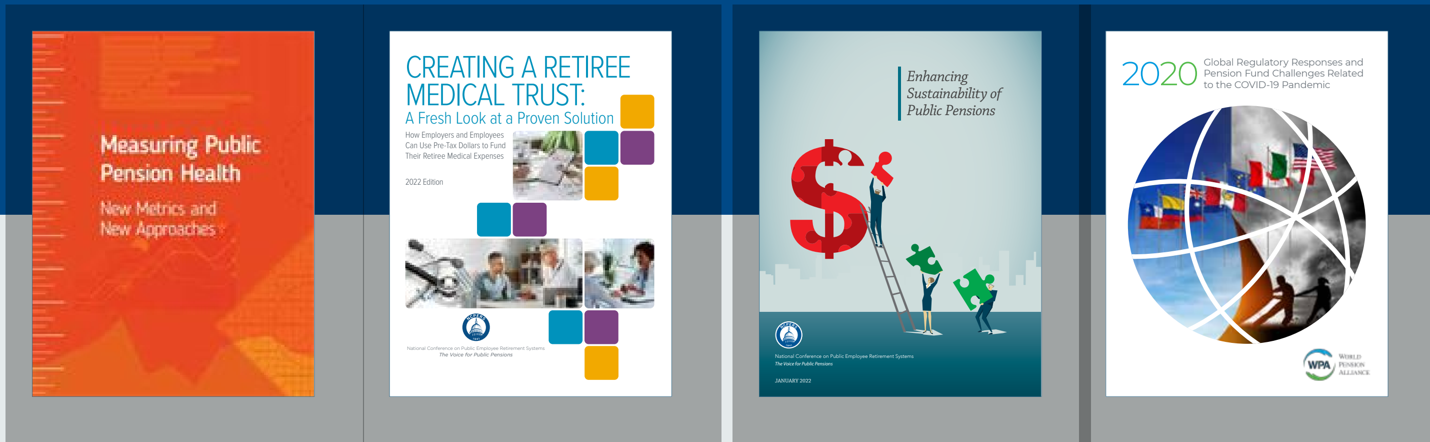
Footnotes:

[1] Choi, James R and Zhao, Kevin. "Did Mutual Fund Return Persistence Persist?" The National Bureau of Economic Research Issued January 2020.

__Bob Parise__ is managing director, head of sales and relationship management, and practice lead for public funds and Taft-Hartley plans for the institutional client group at Northern Trust Asset Management. He is a member of the Business Leadership Council. Bob collaborates across sales and client relationship management to establish business strategy and lead the delivery of investment solutions in the equity, fixed income and alternative asset classes.

Bob has more than 25 years of industry experience. He holds a bachelor's degree in business with an emphasis in finance from Western Illinois University and an MBA from DePaul University. He holds Series 3, 7, 24 and 63 licenses.

Don't miss the latest research from NCPERS.



Find new metrics and approaches for measuring public pension health, research on how employers and employees can use pre-tax dollars to fund retiree medical expenses, and more.

LEARN MORE

NCPERS Legal

Securities Class Action Settlements and SEC Fair Funds: What's the Difference?

By: Mike Lange, Esq., Financial Recovery Technologies

Photo illustration © 2023 shutterstock.com

Securities class action settlements and Securities and Exchange Commission (SEC) Fair Funds look similar. Both involve compensation to harmed investors, sometimes from the same defendants. Both use third party administrators for claim submissions with similar forms and procedures. However, the actors involved – and their motivations – differ in fundamental ways resulting in challenges for participating institutional investors.

Securities class action settlements and SEC Fair Funds differ with respect to who is in charge and their relationship to harmed investors.

In securities class action settlements, the lead plaintiff and counsel prosecute claims on their behalf. When cases settle, lead counsel engage and manage third-party administrators for claim submission under supervision by the courts.

Fair Funds are created in connection with resolutions of either litigation in federal courts by the SEC against defendants, or internal SEC enforcement proceedings against them. If resolutions include disgorgements, Fair Funds are created, and the SEC engages and manages third party administrators for claim submission.

The actors involved in the recovery efforts for securities class action and SEC Fair Funds have different goals.

In a securities class action, the lead plaintiff and counsel are fiduciaries to the class solely focused on maximizing their compensation. Both they and the courts overseeing distributions strive for maximum notice, inclusion, and participation. Courts preliminarily approve settlements, then notify class members and hold hearings on final approval so class members can weigh in on matters including proposed distribution plans. Claimants can challenge the disposition of their claims and if necessary, escalate issues to class counsel and the court.

By contrast, the SEC is a government enforcement agency and not a fiduciary for harmed investors. Compensation is only one aspect of its resolutions. The SEC can impose other sanctions including fines and penalties, cease and desist orders, and/or serving as executives at publicly traded companies. The defendants' behavior before or during prosecutions – including remedial efforts to prevent recurrence – can reduce monetary punishments. The SEC allocates recovered funds between fines and penalties, which it keeps, and disgorgements, which return money to investors.

Securities class action settlements and Securities and Exchange Commission (SEC) Fair Funds look similar. Both involve compensation to harmed investors, sometimes from the same defendants.

Administrative requirements are different and pose operational challenges

Fair Funds have additional administrative requirements that are not seen in securities class action settlements that can increase filing burdens and make investor participation more challenging. These include:

- **Greater documentation burdens:** In securities class actions, administrators use an audit approach for trade substantiation, targeting document requests at high-risk claims – those from unverified sources and/or involving large payouts. By contrast, some Fair Funds require full documentation from all claimants for all trades.

- **Faster and tighter administrations:** The SEC runs faster administrations with stricter compliance requirements. By contrast, in securities class action settlements, it's not uncommon for courts to permit exceptions that expand participation. For example, courts may accept late filed claims if distributions have not yet occurred and/or there is no significant prejudice to other class members.

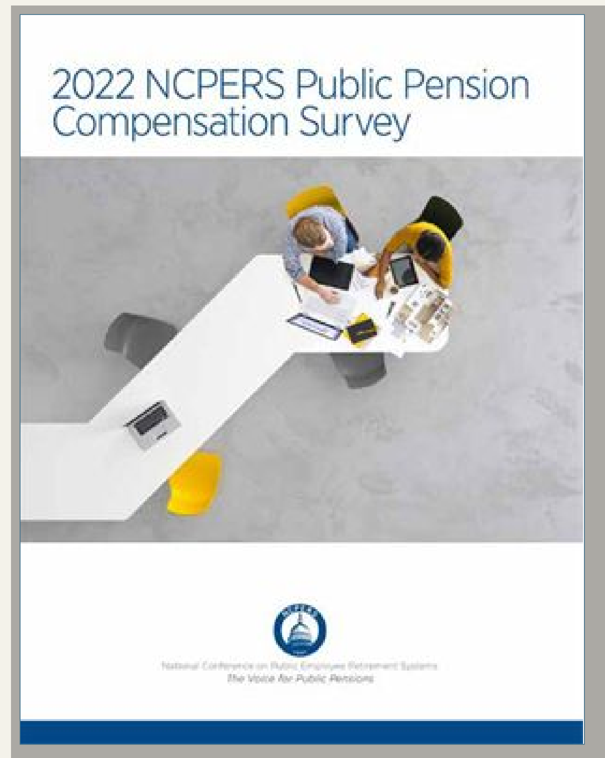
In sum, securities class actions are prosecuted for the benefit of harmed investors. Lead plaintiffs, class counsel, and courts supervising administrations do so as fiduciaries to class members, with a bias towards inclusion and maximum participation. By contrast, the SEC prosecutes claims to achieve a range of goals, only one of which is victim compensation. The SEC is not a fiduciary for harmed investors, and Fair Funds can focus on goals that reduce inclusion and participation. ◆

***Mike Lange** is Financial Recovery Technologies' Senior Vice President of Worldwide Litigation and is responsible for helping clients navigate the challenges involved in evaluating litigation opportunities, analyzing the risks and opportunities, and helping them build a comprehensive shareholder litigation program and policy. He also serves as a subject matter expert and regularly shares insights into the class action landscape to clients, prospects and the broader investment community.*

Order your copy of NCPERS 2022 Public Pension Compensation Survey today.

Access in-depth compensation and benefits data from more than 150 public pension funds representing more than 9 million active and retired individuals.

LEARN MORE



The Rule of Three: Inflation, Recession, Growth

By: Ken McAtamney, Partner, Portfolio Manager, William Blair Investment Management

Photo illustration © 2023 sistock.com

Editor's Note: This article is excerpted from William Blair's October 25, 2022 blog, which you can read in full here.

The number three is pervasive through some of society's greatest stories—there were three little pigs, three musketeers, and three stooges, for example. In fact, the use of the number three in storytelling is so common that it's come to be known as the rule of three. In keeping with that concept, here are my big three for investors to consider in the fourth quarter of 2022: recessionary fears, high inflation, and slowing growth.

Recession

As we analyze the risk of recession in the United States, we must consider whether the country can shift into a more normal expansion, growing at its pre-COVID average, or whether the consumer is more likely to hit the spending breaks, sending the economy into a recession.

The answer, we believe, will depend on how quickly inflationary pressures abate and the Fed can reach its approximate target policy rate. With key indicators such as the labor market (essentially, wages and payroll) yet to see a significant slowdown, it is likely that chances of a pivot to a less hawkish stance will remain low for the remainder of the year.

In Europe, recession appears unavoidable. Simply put, Europe has been hit with a sudden and large energy shock. This is not so much about whether Europe will have enough gas to heat its homes this coming winter, but rather about its energy prices being multiples higher moving forward. This has become an increasing concern as both Nord Stream pipelines were discovered to have multiple leaks.

In addition, while China appears particularly challenged due to ongoing COVID-related disruptions of its domestic economy, demand recovery is expected as its zero-COVID policy eases. This could begin as early as spring 2023. Early signs of gradual easing of monetary policy and increased fiscal stimulus are also supportive to recovery of growth.

In Europe, recession appears unavoidable. Simply put, Europe has been hit with a sudden and large energy shock.

Inflation

Global inflation rates have continued to soar in 2022. As we discussed last quarter, inflation has been significantly influenced by Russia's invasion of Ukraine.

As a result, Europe is only now reaching its pre-COVID output trajectory, which is considerably slower than that of the United States. Inflation is also high in Europe, with high energy prices (the result of substituting liquified natural gas, or LNG, for Russian gas) driving inflation. We expect European inflation to peak when energy prices roll over.

In the United States, slowing consumer demand and normalizing supply chains are beginning to exert downward pressure on inflation. Specifically, goods price inflation has already rolled over, although it will be many more months before the year-over-year print will be at 2%. Monthly consumer price index (CPI) data will remain a key indicator to monitor as we look to determine when annual inflation will decelerate closer to its target range.

Growth

Corporate earnings growth, especially outside the United States, is widely expected to decelerate throughout the remainder of 2022, given the soaring inflation and macroeconomic uncertainty. While some of that expected deceleration has been reflected in multiple contraction, we expect negative earnings revisions to continue to put further downward pressure on multiples.

Investment Implications

As we continue to analyze various market outcomes while uncertainty remains quite high, we increasingly believe that the underlying corporate performance of our portfolio holdings is quite resilient, and their long-term earnings power is likely to remain unchanged. Looking forward, we believe equity returns will likely be driven by earnings growth, and multiple compression will largely stop when earnings growth ceases to decelerate. ◆

Ken McAtamney, *is the head of the global equity team and a portfolio manager for William Blair's International Growth, Global Leaders, International Leaders, and Emerging Markets Leaders strategies. Ken is also a member of the Investment Management leadership team. He was previously co-director of research and a mid-large-cap industrials and healthcare analyst. Before joining William Blair in 2005, Ken was a vice president at Goldman Sachs and Co., where he was responsible for institutional equity research coverage for both international and U.S. equity. Before that, he was a corporate banking officer with NBD Bank. Ken received a B.A. from Michigan State University, and an M.B.A. from Indiana University.*

NCPERS Accredited Fiduciary (NAF) Program

A trustee accreditation program specifically designed and tailored for public pension governance.

SPRING CLASS
MAY 20-21 | NEW ORLEANS

FALL CLASS
OCTOBER 21 - 22 | LAS VEGAS

Why Mortality Improvement Scales Matter

By: Elizabeth Wiley and Graham Schmidt, Cheiron

Photo illustration © 2023 shutterstock.com

For the first time since the Society of Actuaries (SOA) began publishing annual mortality improvement scales for pension plans in 2014, it did not release an updated scale in 2022.

Citing the uncertainty caused by higher levels of deaths during the COVID-19 pandemic, the SOA's Retirement Plan Experience Committee (RPEC), which develops these scales, chose not to issue new tables in 2022. The 2021 mortality improvement scale MP-2021 remains the most recently published scale.

Public pension plans typically rely on actuaries to provide advice and recommendations on demographic assumptions, including assumptions about the mortality of plan participants.

For most pension valuations, the mortality assumption consists of base tables as of a certain date and improvement scales to adjust these base tables for use in different years. This adjustment reflects actual historical and anticipated future improvement in life expectancies.

Mortality improvement scales are tables of mortality improvement rates by age, sex, and year. In developing improvement scales, the RPEC combines historical rates of change with long-term assumptions about the rate of future mortality improvement in a mathematical model. The RPEC has incorporated additional historical data with each new MP scale, and MP-2021 included historical data through 2019.

The pandemic resulted in a higher incidence of deaths from almost all causes in 2020. However, these excess death rates varied significantly throughout the year as well as by region, race, and other variables. Moreover, the way the model is constructed means that these excess rates would result in this increased mortality being reflected in the expected mortality improvement rates for future years, at least in the short to medium term, resulting in additional expected declines in lifespans. So, the RPEC concluded that incorporating this 2020 data into the model would not be appropriate.

Public pension plans typically rely on actuaries to provide advice and recommendations on demographic assumptions, including assumptions about the mortality of plan participants.

Why does it matter that the SOA did not publish an improvement table in 2022?

In order to appropriately fund and manage public pension plans, actuaries project the future costs of the plans in annual valuations to determine the liability for future promised benefits. Assumptions about future mortality have a significant impact on these future costs, so it is important to use an appropriate mortality improvement scale to predict future costs and make informed decisions about the funding and management of these plans.

As a result, public pension plans periodically update their mortality improvement scale either annually or when they complete an experience study, typically every three to five years, to the most recent scale.

Without a MP-2022 scale, updating the mortality improvement assumption presents a challenge. However, the SOA developed and published tools that allow actuaries to create improvement scales, including reflecting the more recent historical data affected by the pandemic. The RPEC also noted that the MP-2021 scale still represents a reasonable scale to use to predict future improvements in mortality.

While there is no MP-2022, actuaries still have the tools and information necessary, in consultation with boards and staff, to continue to recommend appropriate mortality improvement assumptions. ◆

Elizabeth Wiley, FSA, FCA, MAAA, EA, *Consulting Actuary at Cheiron Inc. has 18 years of experience working with public pension plans. Her experience includes preparing GASB disclosures, analyzing ERISA and IRS regulations, state legislation, valuation sensitivity analysis and asset/liability projections, and conducting actuarial audits of large public retirement plans.*

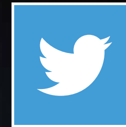
She speaks regularly at annual industry conferences. She volunteers with the American Academy of Actuaries, the Society of Actuaries, and the Conference of Consulting Actuaries. She joined Cheiron in March 2013. She is a Fellow of the Society of Actuaries, a Fellow of the Conference of Consulting Actuaries, an Enrolled Actuary under ERISA, and a Member of the American Academy of Actuaries.

Graham Schmidt, ASA, FCA, MAAA, EA, *Consulting Actuary at Cheiron Inc. has more than two decades of experience as a public pension actuarial consultant. He is a member of the California Actuarial Advisory Panel.*

His experience includes working on audits, accounting and disclosure issues, and risk analyses. He also oversees Cheiron's retiree medical benefit trusts practice. He is a member of the Society of Actuaries' Retirement Plans Experience Committee and has volunteered on public plan committees of the Academy of Actuaries and the Conference of Consulting Actuaries.

He joined Cheiron in January 2013 and opened the firm's Bay Area office that year. He is an Associate of the Society of Actuaries, a Member of the American Academy of Actuaries, a Fellow of the Conference of Consulting Actuaries, and an Enrolled Actuary under ERISA.

Don't Miss NCPERS' Social Media



The Voice for Public Pensions

Calendar of Events 2023

January

Legislative Conference

January 22–24
Renaissance Washington, DC
Washington, DC

Pension Communications Summit

January 23–24
Renaissance Washington, DC
Washington, DC

May

NCPERS Accredited Fiduciary (NAF) Program

May 20–21
Marriott New Orleans
New Orleans, LA

Trustee Educational Seminar (TEDS)

May 20–21
Marriott New Orleans
New Orleans, LA

Annual Conference & Exhibition (ACE)

May 21–24
New Orleans, LA

June

Chief Officers Summit

June 19-21
Denver, CO

View all upcoming NCPERS conferences at www.ncpers.org/future-conferences.

2023-2024 Officers

Kathy Harrell
President

Dale Chase
First Vice President

James Lemonda
Second Vice President

Carol G. Stukes-Baylor
Secretary

Will Pryor
Treasurer

Daniel Fortuna
Immediate Past President

Executive Board Members

Dan Givens
Florida

David Harer
Alabama

Michael Linynsky
Maryland

David Kazansky
New York

Sherry Mose
Texas

John Neal
Arkansas

Frank Ramagnano
Canada

Tom Ross
Massachusetts

Ralph Sicuro
Pennsylvania

Ginger Sigler
Oklahoma

The Voice for Public Pensions

PERSist is published by the National Conference on Public Employee Retirement Systems.
Website: www.NCPERS.org • E-mail: lizzy@ncpers.org