

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

**INVESTMENT COMMITTEE MEETING  
February 20, 2018**

**MINUTES**

Attendance was as follows:

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

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

Meketa Investment Group: Stephen McCourt, CFA; and John Humphreys  
Pension Consulting Alliance: Allan Emkin; and Colin Bebee, CFA

The Chair called the meeting to order at 9:00 a.m. Mr. Hilton led the Pledge of Allegiance.

**CONSENT AGENDA**

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

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

Mr. Ball and Ms. Murphy discussed the differences in agenda format between the Regular Board meeting and the Investment Committee meeting.

**C-1 COMMITTEE MEETING:**

**Approval of Meeting and Minutes**

Investment Committee Meeting

January 24, 2018

**Recommendation:** Authorize meeting and approve minutes.

**C-2 QUIET PERIOD - INVESTMENT RELATED SEARCHES**

**Recommendation:** Receive and file.

**C-3 4<sup>th</sup> QUARTER COMPLIANCE REPORT**

**Recommendation:** Receive and file.

**C-4 MEKETA ECONOMIC OUTLOOK**

**Recommendation:** Receive and file.

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

**INDIVIDUAL ITEMS AGENDA**

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

**I-2 CIO COMMENTS**

***Presentation by Molly Murphy, CFA, CIO, OCERS***

Ms. Murphy provided commentary on the global financial markets, including an update on recent price action with the S&P 500, and on volatility, as measured by the VIX. She also discussed recent inflation prints and news surrounding Fed policy on interest rates.

***Mr. Gilbert arrived 9:03 a.m.***

***Mr. Freidenrich arrived 9:08 a.m.***

***Mr. Prevatt arrived 9:09 a.m.***

Mr. Eley, Mr. Ball, and Ms. Murphy continued the discussion on interest rates and quantitative easing, its impact upon the economy and the USD. They also discussed OCERS' core fixed income portfolio, while also providing commentary on bond duration and the yield curve term premium.

**I-3 PORTFOLIO ACTIVITY REPORT**

***Presentation by Molly Murphy, CFA, CIO & Shanta Chary, DIO, OCERS***

Ms. Chary presented the portfolio activity report, including the total fund overview, subscriptions and redemptions, as well as the asset allocation for January 2018.

Ms. Freidenrich, Ms. Chary, Mr. Ball, and Ms. Murphy further discussed the expected role of OCERS' core fixed income portfolio in a rising rate environment.

Ms. Chary discussed the private equity portfolio allocation, noting that the allocation is on target.

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

**I-4 INVESTMENT MANAGER SURVEILLANCE & ACTION PROCEDURE**

***Presentation by Molly Murphy, CFA, CIO, OCERS***

Ms. Murphy continued the investment manager surveillance and action procedure discussion from the January 2018 Investment Committee meeting. She broadly reviewed: 1) the costs and benefits associated with the delegated responsibility including delineated internal (i.e., OCERS' investment staff, legal) and external (i.e., OCERS' consultants) responsibilities and; 2) industry practices, including common rules and unique limitations used by pensions across California and the U.S.

Mr. Prevatt and Ms. Murphy discussed the manager hiring process and the various methods that could initiate this process, including Board directives, specific mandates, and the implementation of asset allocation policy.

Ms. Murphy observed the importance of asset allocation relative to manager selection, as well as the need to create the right checks and balances. She noted the inherent limitations of fixed dollar limits relative to percentage limits.

Mr. Prevatt and Ms. Murphy discussed the recently updated and approved Investment Committee Charter, which also included revisions made to the Investment Manager Monitoring Subcommittee.

Mr. Ball commented upon the importance of checks and balances, opining that Meketa and PCA both need to sign off on the investment manager surveillance and action procedure.

Ms. Murphy and the Committee discussed the role, responsibility, and accountability of OCERS' consultants relative to staff and to the Committee.

Ms. Murphy stated that all of OCERS' consultants work for the Committee.

Mr. McCourt observed that, in light of costs, general consultants broadly do not replicate the due diligence taken by specialty consultants. He remarked that common practice is for the general consultant to confirm or deny the due diligence done by specialty consultants.

Mr. McCourt observed that a number of different models work, noting that the Committee is free to use the consultants as the Committee deems fit. He stated the need for the Committee and staff to clearly specify the consultant's responsibilities, relative to both the Committee and staff.

Ms. Freidenrich and Mr. Hilton expressed their concerns surrounding the changes made to the Investment Committee and CIO Charters at the recent January Investment Committee meeting.

Ms. Murphy and Ms. Freidenrich continued the discussion on the various manager surveillance and action models employed by other pension plans. They also discussed the role and responsibilities of OCERS' legal team, CEO, and consultants.

Mr. Eley observed that the approved investment manager surveillance and action due diligence checklist only included parties that report to the CIO. Since the CEO does not report to the CIO, he recommended that this checklist should also require the CEO's authorization.

Mr. Eley and Ms. Murphy discussed the costs and benefits of frequent/infrequent investment manager presentations to the Committee.

Mr. Dewane opined on the most efficient use of the Committee's time, including empowering staff and consultants through delegated authority.

Mr. Dewane and Mr. McCourt discussed Meketa's manager and operational due diligence process.

Mr. Dewane further opined that much of the Committee's concerns are assuaged by Meketa's fiduciary responsibility towards OCERS.

A **motion** was made by Mr. Packard and **seconded** by Mr. Dewane to receive and file I-4.

Ms. Murphy, Mr. Prevatt, and Mr. Eley discussed OCERS' manager termination process.

Ms. Murphy suggested that OCERS continue through with the approved investment manager surveillance and action procedure for a period of time, noting that the Committee can modify the investment manager surveillance and action procedure as deemed necessary.

Mr. McCourt and Mr. Lindholm expressed agreement.

Mr. Lindholm expressed his preference that the investment manager surveillance and action procedure be discussed at a future Governance Committee meeting.

Mr. McCourt discussed how the issue of delegated authority first arose, noting that foreseeable significant activity in real estate and in the build out of a direct private equity program would benefit from delegated authority. He stated that Meketa would work with staff on dollar limits. He remarked that Meketa would not set a fixed onsite manager meeting cycle, explaining that some investment managers and strategies require more, whereas some less.

Mr. Delaney noted that the Committee discussed the costs and benefits of an operational Board relative to a strategic policy Board at last September's annual off-site meeting.

Mr. Ball gave direction to move this discussion to the Governance Committee, citing the need to focus on macro issues i.e., the role of OCERS' consultants, rather than on micro issues, i.e., the side-letter process.

Mr. Hilton opined that the Committee form an Ad Hoc Committee to take ownership of the investment manager surveillance and action procedure. He noted the need for Mr. McCourt's involvement in this Ad Hoc Committee.

After further discussion, a **motion** was made by Mr. Packard and **seconded** by Mr. Dewane to receive and file I-4. The **motion carried unanimously**.

***The Committee recessed at 10:57 a.m.***

***The Committee reconvened at 11:06 a.m.***

**I-5 ILLIQUID INVESTMENTS ADVISORY SERVICES RFP FINALISTS**

***Presentation by Molly Murphy, CFA, CIO & Shanta Chary, DIO, OCERS***

**TORREYCOVE CAPITAL PARTNERS**

***Presentation by David Fann, Heidi Poon, CFA, & Nic DiLoretta***

Ms. Murphy and Mr. Lindholm discussed the various private equity fee models in the industry, and the risks and opportunities associated with the services those respective models offer.

Ms. Murphy discussed OCERS' initial fee budget for the illiquid investments advisory services RFP, noting some of the fee advantages that the finalists could provide to OCERS.

Ms. Murphy and Mr. Eley discussed OCERS' private equity performance relative to TorreyCove's composite performance.

Ms. Murphy opined that OCERS could outperform the composite due to OCERS' size and consequent access to specific areas of the private equity market.

Ms. Murphy and Ms. Freidenrich continued the fee discussion. They also reviewed OCERS' illiquid investments advisory services RFP due diligence process.

Mr. Hilton noted that he would vote no, primarily due to his desire for more details in the due diligence process.

Ms. Murphy and Ms. Chary referred to staff's handout due diligence process presentation.

Ms. Murphy, Ms. Chary, Mr. Delaney, and the Committee discussed the proper process regarding dais handouts.

Ms. Chary reviewed staff's due diligence process.

A **motion** was made by Mr. Prevatt and **seconded** by Mr. Dewane to approve TorreyCove for private equity and private real assets consulting services. The **motion carried 8-1** with voting as follows:

**AYES**

Mr. Packard  
Mr. Prevatt  
Mr. Dewane  
Mr. Eley  
Mr. Ball  
Mr. Baldwin  
Ms. Freidenrich  
Chair Lindholm

**NAYS**

Mr. Hilton

**ABSTAIN**

**ABSENT**

**TOWNSEND GROUP**

***Presentation by Jennifer Young Stevens, Robert Miranda, & Felix Fels***

Ms. Murphy reviewed staff's due diligence process for real estate consulting services. She discussed the rationale behind staff's recommendation.

Mr. Lindholm and Ms. Murphy discussed fees associated with Townsend and the potential fee advantages that Townsend could offer OCERS' real estate portfolio.

Ms. Freidenrich and Ms. Murphy discussed OCERS' real asset portfolio.

Ms. Freidenrich expressed her concerns, including fees, Townsend's size, their recommendations for non-U.S. investments, and the associated foreign exchange risks.

Mr. Ball expressed his concerns regarding Townsend, including Townsend's large asset base size.

Mr. Hilton, Ms. Freidenrich, and Ms. Murphy discussed the fees associated with the three real estate finalists.

A **motion** was made by Mr. Prevatt and **seconded** by Mr. Dewane to approve Townsend Group for real estate consulting services. The **motion carried 6-3** with voting as follows:

**AYES**

Mr. Prevatt  
Mr. Dewane  
Mr. Gilbert  
Mr. Hilton  
Mr. Baldwin  
Chair Lindholm

**NAYS**

Mr. Ball  
Mr. Packard  
Ms. Freidenrich

**ABSTAIN**

**ABSENT**

Mr. Eley

***The Committee recessed for lunch at 1:17 p.m.***

***Mr. Dewane left at 1:17 p.m.***

***Mr. Gilbert left at 1:17 p.m.***

***The Committee reconvened at 1:52 p.m.***

**CLOSED SESSION ITEM**

**E-1 CONFERENCE REGARDING INITIATION OF LITIGATION (ONE MATTER)  
(GOVERNMENT CODE SECTION 54956.9)**

Adjourn pursuant to Government Code section 54956.9 to consider whether to initiate litigation.

***The Committee entered into Closed Session at 1:52 p.m.***

***The Committee reconvened from Closed Session at 2:16 p.m.***

Chair Lindholm reported that the Investment Committee authorized the General Counsel to retain the law firm of Berman Tabacco to represent OCERS in the case.

**I-6 4<sup>th</sup> QUARTER 2017 PORTFOLIO RISK DISCUSSION**  
***Presentation by Allan Emkin & Colin Bebee, CFA, PCA***

Mr. Emkin and Mr. Bebee presented PCA's 4<sup>th</sup> Quarter 2017 Portfolio Risk Discussion for OCERS' portfolio.

Mr. Bebee observed that the initial 5% allocation to the Risk Mitigation Strategies (RMS) portfolio, would not be impactful, while a larger one, with an inclusion of additional strategies over time, would be impactful.

Mr. Bebee noted that a prolonged period of stagflation is the worst-case scenario for OCERS' portfolio, noting that some periods in February had exhibited characteristics of such stagflation, or where both growth assets and interest rate-sensitive assets decline in value.

Mr. Bebee stated that the RMS portfolio is not designed to protect against short-term drawdowns, such as the price action seen in February; rather, he reported to the Committee that the portfolio is designed to protect against prolonged drawdowns.

Mr. Emkin discussed the potential impact of changing rates on the portfolio, noting the importance is how those rates evolve. He observed that slowly rising rates are generally positive for equities, where losses incurred from bonds as rates rise would be compensated through the income generated from the principal invested. He observed that hyperinflation, or high and unexpected inflation, is sub-optimal for OCERS' portfolio, as equities and bonds would decline simultaneously.

Mr. Ball and Mr. Emkin discussed various risks, including growth, duration, and credit risks.

Mr. Emkin observed that some of OCERS' equity risk is masked by the increased credit allocation.

Mr. Eley and Mr. Emkin discussed liquid credit versus core bonds, and how they would likely perform differently across various interest rate regimes.

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

**I-7 4<sup>th</sup> QUARTER 2017 PORTFOLIO EVALUATION REPORT**  
***Presentation by Stephen McCourt, CFA, Meketa***

Mr. McCourt presented Meketa's 4<sup>th</sup> Quarter 2017 Portfolio Evaluation Report for OCERS' portfolio. Mr. McCourt reported that the 4<sup>th</sup> quarter return was driven by U.S., emerging market, and international developed equities.

Mr. McCourt explained that OCERS' 4<sup>th</sup> quarter performance was lower relative to peers due to OCERS' asset allocation that was relatively underweight public equities and overweight real assets.

Mr. Hilton and Mr. McCourt discussed OCERS' performance in various markets.

Mr. McCourt further explained that OCERS' portfolio would likely have relative outperformance in negative markets.

Mr. McCourt also reported on OCERS' re-categorized hedge fund long-short managers, noting that their long-short portfolio by definition would cause underperformance relative to long-only managers and benchmarks in bull markets.

Mr. Ball, Mr. McCourt, and Ms. Murphy discussed the direct lending portfolio. They remarked upon the Committee's decision to reduce the direct lending allocation, the recent re-categorization of some managers to private credit, and the disparate direct lending opportunity set between the U.S. and Europe.

Mr. McCourt and Mr. Ball discussed time-weighted returns (TWR) and internal rate of returns (IRR) for OCERS' private equity portfolio.

Mr. Ball asked that Meketa highlight performance outliers, while also directing Meketa to work with staff with regarding the issue of TWR and IRR performance reporting for OCERS' illiquid portfolio.

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

#### **I-8 3<sup>rd</sup> QUARTER 2017 REAL ESTATE PERFORMANCE REPORT**

***Presentation by Stephen McCourt, CFA & John Humphreys, Meketa***

Mr. McCourt and Mr. Humphreys presented Meketa's 3<sup>rd</sup> Quarter 2017 Real Estate Performance Report for OCERS' portfolio.

Mr. Humphreys reported that there was no activity in the 3<sup>rd</sup> quarter, but noted that OCERS made a re-up commitment to Waterton Fund XIII in the 4<sup>th</sup> quarter.

Mr. Humphreys and Mr. McCourt provided commentary on recent real estate developments.

Mr. Humphreys remarked upon performance outliers.

Mr. Ball and Ms. Murphy discussed the forward-looking timeline for real estate investments, particularly as it relates to Townsend.

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

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

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

#### **COMMITTEE MEMBER/CEO/CIO/STAFF/CONSULTANT COMMENTS**

Mr. Eley, Mr. Prevatt, Ms. Freidenrich, Ms. Chary, Mr. Delaney, and Ms. Murphy further discussed handouts given at the dais.

**COUNSEL COMMENTS**

**None**

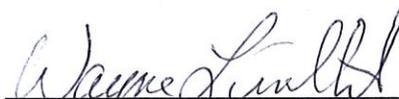
**ADJOURNMENT:** The Chair adjourned the meeting at 3:02 p.m.

Submitted by:



Steve Delaney  
Secretary to the Committee

Approved by:



Wayne Lindholm  
Chair