

MINUTES
INVESTMENT COMMITTEE MEETING
MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION (MCERA)

One McInnis Parkway, 1st Floor
Retirement Board Chambers
San Rafael, CA

December 16, 2020 – 9:00 a.m.

This meeting was held via teleconference pursuant to Executive Order N-25-20, issued by Governor Newsom on March 12, 2020, Executive Order N-29-20, issued by Governor Newsom on March 17, 2020, and Executive Order N-35-20, issued by Governor Newsom on March 21, 2020. The public was able to listen to and observe the meeting on YouTube.

CALL TO ORDER

Chair Klein called the meeting to order at 9:01 a.m.

ROLL CALL

PRESENT: Block, Cooper, Given, Gladstern, Jones (alternate retired), Klein, Murphy, Silberstein, Thomas, Werby

ABSENT: Poirier (alternate safety), Shaw (ex officio alternate)

A. OPEN TIME FOR PUBLIC EXPRESSION

Note: The public may also address the Committee regarding any agenda item when the Committee considers the item.

Open time for public expression, from three to five minutes per speaker, on items not on the Committee Agenda. While members of the public are welcome to address the Committee during this time on matters within the Committee's jurisdiction, except as otherwise permitted by the Ralph M. Brown Act (Government Code Sections 54950 et seq.), no deliberation or action may be taken by the Committee concerning a non-agenda item. Members of the Committee may (1) briefly respond to statements made or questions posed by persons addressing the Committee, (2) ask a question for clarification, or (3) provide a reference to staff for factual information.

No members of the public provided comment. Retirement Administrator Jeff Wickman announced that public comment will be live going forward.

B. MANAGER REPORTS

1. Manager Overview – Jim Callahan, Callan LLC

Jim Callahan, President of Callan LLC, introduced the review of the AEW Core Property Trust portfolio and the real estate market.

2. AEW – Core Real Estate – Mike Acton, Lily Kao, Candida Hoeberichts – 9:05 a.m.

Candida Hoeberichts, Director of AEW Investor Relations, introduced Mike Acton, Managing Director and Head of AEW Research, and Lily Kao, Senior Portfolio Manager. Ms. Hoeberichts stated core real estate is AEW's largest strategy and the Core Property Trust (CPT) is the flagship fund. Ms. Hoeberichts introduced several new members of the AEW investment team and reported Sara Cassidy and Lily Kao were promoted to Senior Portfolio Manager.

Mr. Acton stated the implication of COVID-19 is slowing economic activity, including in the property market for retail and restaurants. The recovery is expected to continue until early 2023 when he expects the real estate market will have recovered. Expectations are for rising interest rates over the coming decade. Property yields remain attractive relative to U.S. Treasury yields, supporting additional capital flowing into the real estate market. This is expected to support a floor in commercial property real estate valuations. Industrial properties and warehouses have remained strong.

Ms. Kao reported CPT's objective is to assemble a high quality core real estate portfolio with good income yield. The CPT has higher occupancy than the benchmark. Portfolio managers have pivoted the portfolio based on secular trends and diversified holdings by product type and geography. Locations include top tier markets with strong job growth and quality of life; examples are Charlotte, North Carolina, and Texas where investments have been added. Office industrial, retail and multifamily sectors are the focus of CPT. Ms. Kao stated the defensive income profile has outperformed the benchmark over ten years. Ms. Kao said over time core real estate is expected to provide attractive income returns.

Due to COVID-19 disproportionately affecting selected markets, recent returns are negative. In the second quarter of 2020 the negative impact to income was apparent. Since then rent relief has moderated and multifamily and office have had consistent rent collection. Retail centers dipped in the second quarter and are recovering since then. AEW negotiated lower rent and deferred payments and tenants have begun to pay what is due. AEW is expecting the fund's income to remain stable and have been thoughtful in their approach to valuations. There are no enclosed malls in the Core Property Trust – all malls are open air. Many holdings lease to off-price retailers who are continuing to do well. AEW is seeing underperformance in urban markets affected by the working-from-home theme, and similar themes are affecting multi-family as well. Industrial continues to outperform other sectors and Ms. Kao is seeing increasing rents and demand which is driving cap rates down.

Trustee Klein asked about the vacancy rate at 500 Folsom in San Francisco. Ms. Kao replied 500 Folsom is a high rise near the Salesforce transit center. Last year the property

experienced strong velocity and lease rates. With COVID-19 rents have declined 15 to 25% for studio apartments. The property is 85% leased and Ms. Kao expects full stabilization by this time next year. Leases are relatively short term, which will favor higher rent in a few years.

Ms. Kao stated AEW and the CPT fund are committed to the ESG Global ESG Benchmark for real assets (GRESB). CPT ranks 84 in this index, which is high relative to peers. Trustee Gladstern asked how climate change affects the strategy. Ms. Kao replied that AEW uses the company Four Twenty Seven to assist with due diligence on sustainability. Mitigation of ESG risks are incorporated into the annual business plan, and electric vehicle charging stations and solar panels are favored.

Trustee Silberstein asked if we are continuing to reinvest dividends and Mr. Wickman said reinvesting dividends was changed in March 2020 to receiving dividends. Responding to Trustee Silberstein's inquiry about adding leverage to the portfolio, Ms. Kao said CPT will continue to be a low leverage fund. Trustee Werby asked if 500 Folsom was written down and Ms. Kao replied affirmatively due to lower rent growth. All assets are appraised once per year by a third party valuation consultant. In summary Ms. Kao said she is seeing cap rates decline and money flowing into multi-family and industrial sectors.

C. NEW BUSINESS

1. Institutional Shareholder Services (ISS) Governance Risk Report – Jack Ferdon, Nathan Worthington

Presentation of the ISS Quarterly Governance Risk Report

Mr. Wickman introduced Jack Ferdon, Senior Associate, Client Service & Consultants, and Nathan Worthington, Executive Director, Regional Head of Client Service and Consultants with Institutional Shareholder Services (ISS). The Administrator said Mr. Ferdon and Mr. Worthington's presentation is intended as an introduction into the value of the Governance Committee's review of the quarterly ISS Governance Risk Report.

Mr. Ferdon reviewed the third quarter of 2020 ISS Governance Risk Report for MCERA's Fund. He explained that the ISS Quality Score is given to each company based on a relative review of corporate governance factors. Mr. Ferdon reported that thirty percent of companies in the Fund fall into the low rating level, some of which is expected for passive investments such as the S&P 500. Commingled fund values in the report do not represent MCERA's position.

Turning to the Manager Summary, Mr. Ferdon highlighted that Parametric votes most often against management recommendations because they follow the ISS Public Fund policy. The percentage of meetings voted is affected by onerous documentation requirements before a vote can be submitted and therefore is not a concern, he said. Overall MCERA managers voted 80% in favor of management proposals. The report shows voting by proposal types. Mr. Ferdon said it is notable that most of MCERA's votes against executive management recommendations involve executive compensation.

Trustee Gladstern asked about the differences in the ISS Public Fund Policy from the ISS Benchmark Policy. In response Mr. Ferdon said the Public Fund Policy is more aggressive

with respect to recommending voting against management recommendations in several areas, including executive compensation plans. Mr. Worthington added that the general framework is that ISS analyzes shareholder proposals on a case-by-case basis. The Public Fund Policy uses sustainability guides for environmental issues, human rights abuses, workplace safety, and fair lending policies. Trustee Silberstein observed that the ISS Public Fund Policy was developed from conversations with large institutional investors to hold managers more accountable than standard policies. MCERA's policy is similar to the ISS Public Fund Policy, Trustee Silberstein observed.

2. Proxy Voting Education – Jeff Wickman, Retirement Administrator

Review MCERA's current proxy voting process, discuss potential options to the current approach and discuss the current proxy voting policy.

Mr. Wickman thanked the Sacramento County Employees' Retirement System (SCERS) for providing him with information about their proxy voting processes. This educational session on proxy voting is presented as background for the Governance Committee's recommendation that the Investment Committee consider hiring ISS vote proxies for two of MCERA's domestic equity investments: the S&P 500 fund and the DFA small cap core portfolio.

Mr. Wickman explained that proxy voting allows voting without being at companies' annual meetings. There are California Government Code sections requiring proxy voting which MCERA complies with. Proxy voting rights are considered a Plan asset, meaning they need to be managed according to MCERA's fiduciary duties of care and loyalty.

The first option for proxy voting is internal proxy voting which is generally performed by the largest pension plans. The second option is to delegate proxy voting to investment managers as MCERA does. MCERA has the responsibility of monitoring proxy voting by the managers. The third option is to use a third-party service provider. Considerations are ease of execution and meeting fiduciary and regulatory requirements. Third-party firms establish guidelines, research a large volume of issues, and develop model or custom guidelines. The two largest providers of proxy voting services are ISS and Glass Lewis. ISS has been helping MCERA and providing the Governance Risk Report used by the Governance Committee to assess proxy voting.

MCERA's Proxy Voting and Corporate Governance Policy is modeled after Council of Institutional Investors (CII) policies. Model guidelines provided by ISS include its Public Fund Policy and its Benchmark Policy. Mr. Wickman presented a comparison by ISS of MCERA's proxy voting policy with the ISS Benchmark Policy. There were gaps in several areas; for example, MCERA's policy is silent on proxy contests, mergers & acquisitions, or shareholder proposals, whereas the ISS Benchmark Policy provides details.

Staff recommendations to consider at the next Investment Committee meeting are:

- Engage a third party provider if the Investment Committee wants to vote proxies directly.
- Adopt a model policy offered by the third party provider.

- Update the Proxy Voting and Corporate Governance Policy to align with selected provider policy and include Board and staff monitoring and reporting.
- Schedule ISS to present their proxy voting services.

A summary of staff actions when a third party is voting proxies would include:

- Review proxy voting service providers and make a recommendation to the Board for hiring the provider.
- As necessary, review proxy ballots to ensure votes are cast as expected.
- Take action when policy guidelines are insufficient to make a recommendation on voting on a specific issue.
- Report to the Board quarterly a summary of the results of the proxy voting process.
- Ask the third party to prepare a policy review on proxy voting annually.

Based on his discussions with peer systems, Mr. Wickman expects staff can reasonably manage the proxy voting utilizing an external proxy voting provider. Trustee Gladstern expressed appreciation for this presentation because it answers many questions on proxy voting. Chair Klein agreed that needed steps have been clarified and the Committee will move forward with considering proxy voting at its January meeting. Trustee Silberstein commended the Administrator for an excellent presentation. He noted the Governance Committee has been monitoring proxy voting, particularly by DFA and State Street, for a few years.

Trustee Block asked if takeover and merger and acquisition proxy votes could be left to our managers since we hire managers to value the holdings. He also inquired if another party verifies how ISS is voting. Mr. Wickman stated that typically when proxy voting is taken back from the managers all proxy issues are voted by the system or the hired third party provider. Mr. Worthington said that ISS works with Deloitte & Touche on their proxy voting processes and this is included in ISS's SOC report that is available to MCERA. A custom proxy voting policy could be designed to refine how proxy voting is implemented, he said.

Chair Klein recessed the meeting for a break at 10:43 a.m., reconvening at 10:55 a.m.

3. Public Real Assets Structure Review (Action) – Callan LLC – Jim Callahan, Jay Kloepfer
Consider, discuss, and take possible action regarding real asset allocations

Mr. Callahan stated historically MCERA's real assets were invested exclusively in the Woodmont private real estate portfolio. Then the Investment Committee determined to diversify and move ultimately to two core real estate funds managed by AEW and UBS. Part of the prior real estate allocation, 7% of Plan assets, was reallocated to a public diversified real assets portfolio including Treasury Inflation-Protected Securities (TIPS), REITs, commodities, and natural resources. Subsequently, commodities and natural resources were moved from passive to active management. There has been discussion about reconsidering the use of commodities in the portfolio which this topic will address.

Trustee Werby asked why (TIPS) are considered real assets and Mr. Callahan replied because TIPS have a distinct positive correlation to inflation levels.

Jay Kloepfer, Executive Vice President, Director of Capital Research with Callan LLC, stated real assets were built as a complement to the real estate portfolio. Options to consider include eliminating commodity exposure and reallocating funds to the other three real asset managers, keeping a sliver of commodities, or moving to global infrastructure.

Mr. Kloepfer made the point that inflation matters. Relative to history consumer price inflation (CPI) has been benign, averaging 2.2% over 25 years. But Callan believes inflation could be a rising threat two to four years from now based on the extensive economic stimulus. The time to consider an inflation hedge is when the risk is low, he advised. Real assets provide a hedge for inflation and commodities have the highest sensitivity to inflation.

Principles for real asset portfolio design include diversification, short-term inflation sensitivity, and long-term real returns. Mr. Kloepfer said the current real assets portfolio has a balanced, moderate risk posture and has performed as designed. Performance over 5.25 years is in the 35th percentile compared to peers, and active managers have added value. Short-term performance is weaker, especially for commodities. Correlations were reviewed showing REITs, TIPS and commodities have lower correlation to equities than natural resources and positive correlation to the CPI.

Mr. Kloepfer discussed characteristics of alternative structures for real assets. Commodities have underperformed other assets, but their purpose is different. TIPS have low volatility. Real asset correlations and betas with stocks and bonds were presented. Assets are analyzed to look for diversification as well as sensitivity to inflation, Mr. Kloepfer explained. One alternative Callan recommends if commodities are removed from the portfolio is global listed infrastructure, These are liquid stocks generating long-term cash flow that are tied to inflation. The weakness is global infrastructure securities have a higher beta to equities. Three alternative mixes for real assets were presented showing that the best beta exposure to inflation is with the commodities portfolio. Mr. Callahan explained that the tradeoff with the three mixes is greater return but lower correlation to inflation.

The mixes are:

- Mix 1: Reduce commodities by 10% and distribute remaining funds to current real asset managers.
- Mix 2: Remove commodities and replace with global listed public infrastructure.
- Mix 3: Remove commodities and reallocate proceeds to the three remaining real assets.

Trustee Silberstein asked if removing commodities and allocating those funds to the private credit portfolio could be done and Mr. Callahan replied the two are separate discussions. Trustee Gladstern said public infrastructure traditionally has been funded with municipal bonds. She is against privatizing infrastructure because it would fall onto

the residents to make the return we are looking for. Trustee Block said because of potential stagflation commodities should remain in the portfolio as inflation protection. Trustee Silberstein noted that equities provide inflation protection over the long term. Mr. Kloepfer observed that in the event of a supply shock, TIPS and commodities provide inflation protection. Trustee Block agreed there may be a supply shock in commodities in the future due to global demand.

In summary Mr. Callahan said real assets would be useful in certain economic scenarios, noting that the total portfolio is equity and growth oriented. Callan is still comfortable with the current real assets portfolio which would perform better than other assets in certain scenarios.

It was M/S Silberstein/Gladstern to adopt Mix 3 in the Callan presentation for the diversified real assets portfolio to remove commodities and reallocate those funds to remaining public real assets.

Trustee Block observed that removing commodities would not do much to portfolio performance and there would be less diversification. Trustee Silberstein noted commodities have had little return. Trustee Werby views the return as the main consideration. Chair Klein agrees with leaving commodities in the portfolio to provide for diversification and guard against inflation that may result from current economic stimulus.

The motion failed by a vote of 5-4 as follows:

AYES: Cooper, Gladstern, Silberstein, Werby
NOES: Block, Given, Klein, Murphy, Thomas
ABSTAIN: None
ABSENT: None

4. Investment Manager Personnel and Other Updates

a. Morgan Stanley – Jim Callahan, Callan LLC

Anne Heaphy, Senior Vice President with Callan, reported Morgan Stanley announced the retirement of Dirk Hoffmann-Becking at the end of March 2021 for personal reasons. Mr. Hoffmann-Becking is a member of the international equity team covering banking and leisure sectors. Mr. Callahan noted William Lock, as head of the international equity team, is in charge of the Morgan Stanley portfolio and therefore the departure of Mr. Hoffmann-Becking should not be a concern.

b. Morgan Stanley/Eaton Vance – Jim Callahan, Callan LLC

Mr. Callahan reported Morgan Stanley is going to acquire Eaton Vance, the parent company of Parametric. MCERA is invested in Parametric's emerging markets strategy and the overlay program. Because Morgan Stanley tends to be a more hands-on parent company than Eaton Vance has been, with respect to Parametric Callan will be monitoring the situation closely. Trustee Given asked if there is anything in the agreement with Parametric to prevent Morgan Stanley from changing anything and Mr. Callahan said not that he is aware of.

c. Colchester – Jim Callahan, Callan LLC

Mr. Callahan reported Janhavi Kumar, Head of Distribution for North America, will be departing Colchester on December 18, 2020. Jeremy Church, Product Specialist, will replace Ms. Kumar. Callan does not believe this is a meaningful event as the investment team is intact.

5. Watch Period Review – Callan LLC – Jim Callahan, Anne Heaphy

a. Parametric Emerging Markets Equity (Action)

Consider and take possible action regarding Watchlist status

Mr. Callahan said the Parametric Emerging Markets Equity portfolio has been on the Watchlist due to trailing 3-year underperformance since 2015. Underperformance has continued due largely to a different portfolio construction than the MSCI Emerging Markets Index. This benchmark has a significant weight in China which has been one of the strongest emerging markets performers. Mr. Callahan said the recommendation is to retain Parametric on the Watchlist. In addition, it makes sense to replace Parametric with an active manager for the global emerging markets opportunity set. Trustee Gladstern asked if the benchmark is appropriate and Mr. Callahan said yes because it represents the opportunity set.

It was M/S Murphy/Silberstein to retain Parametric on the Watchlist.

Upon Trustee Block's suggestion, the makers of the motions above and below separated into two motions what had been one motion. The motion was approved by a vote of 9-0 as follows:

AYES: Block, Cooper, Given, Gladstern, Klein, Murphy, Silberstein, Thomas, Werby
NOES: None
ABSTAIN: None
ABSENT: None

It was M/S Murphy/Silberstein to direct Callan to conduct a search to evaluate other emerging markets strategies.

Trustee Block said he is against increasing investments in China based on his experience working in the country.

The motion was approved by a vote of 8-1 as follows:

AYES: Cooper, Given, Gladstern, Klein, Murphy, Silberstein, Thomas, Werby
NOES: Block
ABSTAIN: None
ABSENT: None

b. Artisan International Growth Equity (Action)

Consider and take possible action regarding Watchlist status

The Artisan International Growth Equity portfolio went on the Watchlist in November 2017 because of performance relative to peers. Currently five-year performance as of September 30, 2020 remains below the median partly due to the strategy being not as aggressive as the other growth strategies. Mr. Callahan's recommendation is to retain the Artisan portfolio on the Watchlist.

c. Morgan Stanley International Equity (Action)

Consider and take possible action regarding Watchlist status

The Morgan Stanley International Equity portfolio was placed on the Watchlist in November 2017. Although this portfolio no longer qualifies quantitatively for the Watchlist, based on the personnel change and the acquisition discussed above, Mr. Callahan's recommendation is to retain the Morgan Stanley portfolio on the Watchlist.

d. Colchester Global Fixed Income (Action)

Consider and take possible action regarding Watchlist status

The performance of the Colchester Global Fixed Income portfolio is good with respect to the index and peers. Mr. Callahan's recommendation is to remove the Colchester portfolio from the Watchlist.

It was M/S Block/Cooper to retain the Artisan International Growth Equity and Morgan Stanley International Equity portfolios on the Watchlist and to remove the Colchester Global Fixed Income portfolio from the Watchlist. The motion was approved by a vote of 9-0 as follows:

AYES: Cooper, Given, Gladstern, Klein, Murphy, Silberstein, Thomas, Werby
NOES: Block
ABSTAIN: None
ABSENT: None

D. INVESTMENT CONSULTANT QUARTERLY REPORT

1. Quarterly Report as of September 30, 2020

a. Summary Report

Mr. Callahan presented the Summary Quarterly Report for the Fund as of September 30, 2020. The investment consultant stated the equity markets continue to rebound off the March 2020 lows in dramatic fashion. Large cap equities continued outperformance to small caps for the quarter and over longer time frames. Also, growth stocks have been meaningfully outperforming value stocks. Non-U.S. developed equity markets trail the U.S. equity markets, and emerging markets are stronger than Non-U.S. developed markets. Mr. Callahan said this year the U.S. dollar has weakened versus major currencies, which helps international investments. Bonds had modest returns for the quarter and a strong 9.56% return for the prior 12 months. Longer duration bonds have also rebounded. In real estate returns are positive but there is a write-down in the index for the quarter and the trailing year.

Mr. Callahan highlighted the fact that the value of six stocks – Facebook, Apple, Amazon, Netflix, Google, and Microsoft (FAANGM) represent 25% of the S&P 500 Index. As of September 30, 2020, the top five FAANGM stocks were up 42% calendar year-to-date, while remaining stocks in the index had negative returns. Trustee Werby inquired about the markets going forward. Mr. Callahan replied COVID-19 is affecting which companies recover from the weak economy. The expectation is lagging stocks will do better once the economy recovers from the virus.

MCERA ranks favorably against peers, returning 4.5% net of fees in the third quarter of 2020 and 7.3% for the trailing year. There is an overweight to private equity which performed well in the third quarter of 2020. The big headwind over the last year is the overweight in small cap equities in the domestic equity portfolio versus the Russell 3000 Index and value tilt in the DFA domestic small cap core portfolio. The Dimensional Fund Advisors (DFA) small cap core portfolio underperformed and is value oriented by design. International equity portfolios include Morgan Stanley which has a value orientation, Artisan with a growth orientation, and the TimesSquare international small cap portfolio. For the quarter internationals returned 6.3% and 5.2% net of fees for the prior 12 months. Mr. Callahan noted that MCERA is being rewarded for active management over time.

For the quarter ending September 30, 2020, the fixed income portfolio was up 2.1% versus 1.4% for the index and all three managers outperformed. For the trailing year fixed income was up 9.6%, with all three managers ranking favorably compared with the peer group. Trustee Block asked about the performance of the Western Asset fixed income portfolio since the guidelines changes earlier this year. Mr. Callahan replied the guidelines change for Western Asset has been very positive.

Mr. Callahan reported that real estate returns were negative for the third quarter and trailing 12 months. UBS continues to struggle relative to the index and the peer group as it continues to write down properties in retail and office sectors. Public real assets returned 7.28% in the third quarter versus 3.72% for the benchmark. The big standout is the KBI natural resources portfolio with its 14% return for the quarter. In the private equity portfolio MCERA has paid in around \$350 million of the \$400 in commitments and has received \$250 million in distributions. Net asset value is \$301 million, so the total value of the private equity portfolio is almost \$550 million. Returns are in the second quartile of the peer group. In response to Trustee Werby's inquiry, the Administrator said the private debt portfolio consists of \$33 million for Fortress, and \$33.5 million each for CarVal and Varde.

b. Flash Performance Update

Mr. Callahan updated preliminary Fund performance net-of-fees as of November 30, 2020. The fiscal year-to-date return for the domestic equity portfolio was 19.5%, slightly trailing the Russell 3000. Small cap is performing better since the end of September, he said, meaning the overweight to small cap is helping the Fund return in the fourth quarter. The international equity portfolio has a fiscal year-to-date return of 14.4%, underperforming the benchmark. Developed international managers are

underperforming fiscal year returns so far and are ahead of respective benchmarks for the calendar year. The fixed income portfolio was up 4% for the fiscal year-to-date, with all three managers performing well. Public real assets returned 16.7% for the fiscal year to date, with the KBI natural resources portfolio driving returns. The Invesco commodities portfolio performance is far ahead of its benchmark. Mr. Callahan said public real assets have been a good diversifier for the Fund.

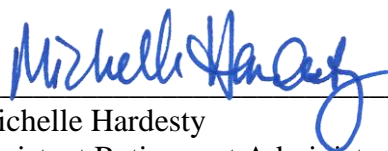
As of November 30, 2020 the Fund is up 6.7% for the calendar year and 11.1% for the fiscal year. In summary, Mr. Callahan said it has been an amazing recovery since March 2020. Trustee Block asking if the divergence in valuations between REITs and private real estate is due to equity beta or underlying asset values. In response, Mr. Callahan said the predominant effect has been equity beta. He noted interest rates are so low that he expects institutional investors to continue searching for yield from REITs.

There being no further business, Chair Klein adjourned the meeting at 1:01 p.m.



Jeff Wickman
Retirement Administrator

On behalf of:
Sara Klein
Investment Committee Chair



Michelle Hardesty
Assistant Retirement Administrator

On behalf of:
Jeff Wickman
Retirement Administrator