MINUTES

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

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

September 27, 2023 – 9:00 a.m.

This meeting was held at the address listed above and, absent technological disruption, was accessible via videoconference and conducted in accordance with Government Code section 54953 and 54954.2.

CALL TO ORDER

Chair Klein called the meeting to order at 9:05 a.m.

ROLL CALL

PRESENT: Cooper, Gladstern, Klein, Martinovich, Silberstein, Vasquez, Werby, Jones (alternate retired)

ABSENT: Murphy, Poole, Gullett (alternate safety), Shaw (ex officio alternate)

CONSIDER ANY BOARD MEMBER REQUESTS TO TELECONFERENCE FOR "JUST CAUSE" OR "EMERGENCY," AS SET FORTH ON THIS AGENDA BELOW

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.

B. MANAGER REPORTS

1. Manager Overview – Jim Callahan, Callan LLC

   Jim Callahan, President of Callan LLC, stated Abbott Capital Management and Pathway Capital Management will present private equity portfolio reviews.

2. Abbott Capital Management – Private Equity – Tim Maloney, Sean Long
   TIME CERTAIN: 9:05 a.m.

   Sean Long, Director, Marketing and Client Solutions with Abbott Capital Management, provided a general overview of Abbott and introduced Tim Maloney, Managing Director and member of the Investment Committee. Mr. Maloney reported on the investment team Wolf Witt was promoted to Managing Director earlier this year. Mr. Long stated Abbott employs four distinct strategies in the Annual Program (AP) Funds: Venture Capital and Growth Equity, North America Private Equity, Europe Private Equity, and Small Buyouts. Across these strategies, Secondaries and Co-investments are employed as J-curve mitigants to get capital deployed and return distributions to limited partners.

   Mr. Long reported of the $250 million committed by MCERA since 2008 across six funds, 82% has been paid in. The Total Value to Paid-In Capital (TVPI multiple) is 2x, and the program overall is cash flow positive, with distributions paying for commitments. The net Internal Rate of Return (IRR) since inception is 15% and, overall, the program has worked as planned. Mr. Long stated Abbott Capital Private Equity Fund VI (ACE VI) and ACE VII are in harvesting mode and distributing capital. ACE Investors Annual Program 2016 (AP16) and AP17 are in value creation mode, and AP21, AP22, and AP23 are in the investment phase.

   Chair Klein asked about Abbott's confidence level in the valuation for ACE VI and whether MCERA will receive distributions in the next year and a half. In response, Mr. Maloney said Abbott distributed 6% of ACE VI in the past year, acknowledging there is no doubt distributions have been challenged and ACE VI has been extended through March 31, 2025. The intention is to get capital back to limited partners as soon as possible, he said. Mr. Maloney said valuation discounts depend on the strategy and would be material, from 25 to 40%, to sell in the current market. He explained the plan is to implement Secondary sales once discounts to valuations are lower and the remaining Net Asset Value (NAV) is less material. Chair Klein pointed out that the market is telling investors that private equity valuations are inflated. Chair Klein questioned why the Net Asset Values couldn't be marked down to reflect market prices until successful exits from the investments can be achieved. She noted that this strategy would have the added benefit of alleviating MCERA's fees on investment returns that haven't been realized yet.

   In response, Mr. Maloney observed private equity assets are illiquid and Secondary market valuations do not represent what the ultimate valuation is expected to be. He maintained Abbott's valuation process is rigorous. Chair Klein asked about the basis for Abbott's optimistic view of valuations. In response, Mr. Maloney indicated there are two values, liquid and illiquid, and if liquidity is needed, a discount to true value may apply.

Otherwise, the idea is to manage assets until a valuation is reached that will not impact return.

Mr. Long explained through March 31, 2023 the fee was charged on committed capital. After March 31, 2023 during the extension period, the fee was reduced by 50% and based on the NAV.

Trustee Werby asked if fees collected previously are disgorged when assets are written down from apparently inflated values. Mr. Maloney replied that valuations are based on the general partners' audited valuations. Trustee Werby pointed to a court case determining some valuations of assets were not based on reality. He asserted that when Abbott finds out the value was not what Abbott thought it was, Abbott collected fees it was not entitled to. Mr. Maloney replied when fees were collected, the value was there. Mr. Callahan pointed out that in the public markets managers are not going to return fees collected based on market values going up and down.

Mr. Maloney stated the private equity portfolio has grown in value and distributions currently outpace contributions. He spoke to the consistency of strategy diversification over time, highlighting the 30% allocation to venture capital and growth equity that have performed the best. Performance by strategy across MCERA's funds shows consistent long-term IRR and TVPI performance due to manager selection and consistent investment year in and year out. Mr. Long stated that measured against private equity peers, Abbott's IRR &TVPI across strategies consistently beat the median over time. As measured against public equity markets, MCERA's Net IRR has outperformed over every time frame, he said, beating the S&P 500 PME+ (Public Market Equivalent) by more than 2% since inception. He noted the importance of diversification and investing consistently over time, as different strategies outperform in different years.

Chair Klein asked about the Buyout market given the rise in interest rates. In response, Mr. Maloney said higher interest rates have been a challenge for general partners relying on Buyout debt. In 2023 there has been a big gap between what buyers are willing to pay and sellers will accept. Mr. Maloney noted since the beginning of September the transaction market is picking up in velocity.

In summary, Mr. Maloney stated MCERA's private equity portfolio is over 80% funded and has returned over 1x in distributions to MCERA. He said the remaining value should grow and mature over time. Trustee Silberstein said as MCERA is one of the largest investors, he hopes Abbott will take that into account when considering the dissatisfaction with fees. Chair Klein asked what the strategy is when encountering Zombie funds. Mr. Maloney indicated options include full or partial asset sales, or replacing the general partner, depending on an assessment of the assets.

3. Pathway Capital Management – Private Equity – Valerie Ruddick, Bryan Nelson
TIME CERTAIN: 9:35 a.m.

Valerie Ruddick, Managing Director at Pathway Capital Management, reported the key theme at Pathway is continuity and stability. Ms. Ruddick stated MCERA is invested in six Pathway funds, the oldest being PPEF 2008 which is approaching its 15th anniversary and is in the harvest and liquidation phase. PPEF I-11, the newer fund, is in its investment phase that will continue for the next two years. Of $250 million committed across the portfolio as of March 31, 2023, 83% is contributed. Ms. Ruddick said the portfolio continues to mature and distributions exceed the amount contributed to Pathway. As of March 31, 2023, Net IRRs for each fund show outperformance to private equity and public equity benchmarks. Based on preliminary June 30, 2023 valuations, there are no material changes to March 31, 2023 performance metrics. Ms. Ruddick presented performance by strategy, investment type, and region.

Chair Klein asked about valuation discounts in the Secondary market. In response, Ms. Ruddick said Buyout discounts are about 10% and 30% to 40% for older funds and Venture investments. Trustee Vasquez asked how the Special Situations category is defined and Ms. Ruddick said it is an industry-specific multi-strategy that is debt related. Ms. Ruddick introduced Bryan Nelson, Director in the Pathway California office, who looks at new investment opportunities and works with the Co-Investment team.

Mr. Nelson reported in 2017 MCERA's private equity program became cash-flow positive on an annual basis, due to distributions exceeding contributions. Mr. Nelson highlighted record distributions of $74.5 million in 2021 for the program. He said in 2023 the exit environment slowed industry wide, but Initial Public Offering (IPO) activity is picking up and there are green shoots in the exit environment. Mr. Nelson stated the portfolio is diversified across 73 high-quality managers with exposure to over 3,500 underlying portfolio companies. The portfolio is also diversified across strategy. Geographically, the best opportunities are in the U.S. and Europe.

Chair Klein asked why the portfolio still holds public companies. In response, Mr. Nelson explained the general partner may decide not to sell into an IPO that does not generate liquidity. Chair Klein asked about PPEF 2008 which Ms. Ruddick said will be entering the extension stage in December 2023. Chair Klein asked what the Secondary market is telling Pathway relative to valuations and suggested reducing valuations to reduce MCERA's fees. Ms. Ruddick replied that prices in the Secondary market today would have a 60% to 70% discount to the NAV. Ms. Ruddick explained that Pathway is required to use manager valuations for financial reporting under Generally Accepted Accounting Principles (GAAP). She further stated that in the extension period MCERA's fee will step down by about 70% from the current fee. Chair Klein asked what distributions to expect moving forward. Ms. Ruddick replied she is seeing mergers and acquisitions picking up again but does not expect a material increase in distributions until next year.

Chair Klein directed deliberations to **Agenda Item C.2, Private Equity Annual Review and Pacing Plan**.

C. NEW BUSINESS

1. Investment Manager Personnel Update – Morgan Stanley

   No discussion.

2. Private Equity Annual Review and Pacing Plan (ACTION)
   Consider, discuss and take possible action regarding private equity pacing plan

   Gary Robertson, Private Equity Consultant with Callan, stated MCERA's private equity program began during the Great Financial Crisis in 2008 and as a result got a slow start. Currently, the private equity allocation is near the top of the 12% target range. He presented valuations through March 31, 2023, noting that fund raising and new investments and exits have slowed. In addition, there is a challenging debt environment and uncertainty in the private equity market.

   As of March 31, 2023 for the total private equity program, MCERA has committed $500 million, paid in $411 million, and received $465 million in distributions. Mr. Robertson reported in the past year MCERA received over $33 million in distributions, about 8% of the NAV, so the portfolio is in good shape and working well. The Total Value to Paid In (TVPI) is 2.00. Managers are performing either in the first or second quartile of peer partnerships including fees, and the total IRR is 15.3%.

   Regarding pacing, Mr. Robertson stated based on the current allocation being above the 8% target, remaining uncalled capital, and lower distributions expected going forward, Callan suggests either pausing commitments for one year or committing less than $60 million this year. Chair Klein pointed out performance metrics are based on valuations that she questions. She is also skeptical that MCERA will receive distributions in accordance with current valuations. Chair Klein, Trustee Silberstein and Trustee Vasquez indicated a preference to wait another year before making new commitments to the private equity program. Hearing no motion to make new commitments, the Chair moved to the next agenda topic.

3. Private Equity Annual Fee Disclosure (ACTION)
   Consider, discuss and take possible action regarding private equity fee disclosure

   Mr. Robertson presented the Annual Private Equity Fee Summary in compliance with California law on tracking and reporting private equity fees and investments. The fee template is an industry standard developed by the Institutional Limited Partners Association (ILPA) that sets forth fees and expenses for the past year and since inception. Fund-of-Funds Managers fees and expenses totaled $3 million over the past year and $35.1 million since inception.

Trustee Cooper was excused from the meeting.

It was M/S Werby/Vasquez to adopt the Private Equity Annual Fee Disclosure as presented. Trustee Jones voted for Trustee Murphy who was absent. The motion passed by a vote of 7-0 as follows:

AYES:	Gladstern, Jones, Klein, Martinovich, Silberstein, Vasquez, Werby
NOES:	None
ABSTAIN:	None
ABSENT:	Cooper, Gullett, Murphy, Poole

Chair Klein recessed the meeting for a break at 11:06 a.m., reconvening at 11:18 a.m.

Trustee Cooper rejoined the meeting at 11:18 a.m.

4. International Equity Allocation (ACTION)
   Consider, discuss and take possible action regarding international equity allocation including passive sleeve and manager search

   Mr. Callahan stated MCERA's international equity portfolio is targeted to 22% of the Fund and is actively managed with a slight growth tilt. Due to recent performance challenges the Investment Committee has discussed ways to mute the growth tilt or retain as is. At its June 21, 2023 meeting the Investment Committee directed Callan to conduct a passive manager search.

   Mr. Callahan stated two ways to approach passive vehicles for developed international markets are the MSCI EAFE Index or the MSCI World ex-US that includes Canada. Reasonable alternative structures for the value and growth allocations managed by Morgan Stanley and Artisan, representing 60% of international equity, are:

   1. Add 20% passive and reduce international value and growth portfolios by 10% each.

   2. Add 30% passive and reduce international value and growth portfolios by 15% each.

   3. Add 30% passive and remove international growth portfolio, retaining Morgan Stanley to reduce cost, tracking error, and the growth tilt.

   Mr. Callahan noted all three alternative international equity structures have the benefit of reducing the growth tilt, more so for Alternative 3. He presented comparisons of the alternative international equity structures for style, regional allocations, rolling three-year returns, cumulative returns and risk metrics. Mr. Callahan pointed out that rolling standard deviations show that removing active management and adding passive management would increase volatility moving forward. In addition, tracking error metrics show adding passive management lowers the tracking error. Trustee Vasquez indicated an information ratio would provide clarity with respect to comparing active managers with a passive index.

   Mr. Callahan presented a comparison showing fees are lower as passive management increases with each alternative structure. When Trustee Gladstern suggested considering removing both Artisan and Morgan Stanley, Mr. Callahan observed both managers have added value to the Fund since inception.

It was M/S Vasquez/Gladstern to allocate 50% of the international equity portfolio to the MSCI World ex US index and increase allocations for the TimesSquare Capital Management International Small Cap Fund and Fidelity Institutional Asset Management Select Emerging Markets Equity Fund to 25% each. Trustee Jones voted for Trustee Murphy who was absent. The motion passed by a vote of 8-0 as follows:

AYES:	Cooper, Gladstern, Jones, Klein, Martinovich, Silberstein, Vasquez, Werby
NOES:	None
ABSTAIN:	None
ABSENT:	Gullett, Murphy, Poole

Mr. Callahan stated there are three viable candidates to manage the passive international equity allocation: BlackRock, Northern and State Street. BlackRock has only a securities lending vehicle and Northern and State Street have lending and non-securities lending vehicles. He addressed risks associated with securities lending evidenced during the Great Financial Crisis, adding that fees are cheaper for securities lending funds. There was general agreement that MCERA may gain operational efficiencies and potential fee savings by engaging one of its current managers, BlackRock or State Street, for the passive international equity allocation.

It was M/S Silberstein/Vasquez to direct staff and Callan to discuss with BlackRock and State Street fees associated with a passive, securities lending international equity vehicle. Trustee Jones voted for Trustee Murphy who was absent. The motion passed by a vote of 8-0 as follows:

AYES:	Cooper, Gladstern, Jones, Klein, Martinovich, Silberstein, Vasquez, Werby
NOES:	None
ABSTAIN:	None
ABSENT:	Gullett, Murphy, Poole

5. Future Meetings

Trustee Silberstein suggested that Fidelity Institutional Asset Management (FIAM) discuss China during its next portfolio review.

D. INVESTMENT CONSULTANT QUARTERLY REPORT

1. Summary Report as of June 30, 2023

Mr. Callahan discussed returns for capital market segments as of June 30, 2023. He reported 2022 was a down year for equities and for fixed income, which was a surprise. There was a rotation from value outperforming growth last year to growth outperforming value this year. In addition, equity market performance has been narrowed down to the Magnificent 7, Facebook (now Meta), Amazon, Apple, Google, Microsoft, Nvidia and Tesla. This narrowing is evidenced by the lower performance of the equal-weighted S&P 500 Index versus the size-weighted S&P 500 Index. Currently in September, equity markets are correcting. Interest rates have risen, and the revaluation of private real estate and private equity is catching up with lower public market valuations.

Mr. Callahan reported as of June 30, 2023 the Fund is valued at $3.1 billion. It is slightly underweight to public equities and the overweight to private equity has moderated. For the quarter the Fund is up about 2% net of fees and up 6.4% net of fees over the past 12 months. Final June 30th returns will incorporate updated private equity valuations that lag on a quarter basis.

During the quarter the domestic small cap equity portfolio managed by Dimensional Fund Advisors outperformed, balancing the underperformance of the Russell 2000 relative to large cap equity. The international equity portfolio underperformed during the quarter, but one-year performance is still strong. Both fixed income managers, Wellington Management Company and Western Asset Management Company, outperformed benchmarks over the past 12 months.

Real estate portfolios were down in absolute and relative terms over the past year. UBS continues to underperform while AEW performed closer to the benchmark. Mr. Callahan said there is concern about debt needing refinancing to be addressed in the next year. In the real assets portfolio both the Invesco commodities portfolio and the Kleinwort Benson Investors global natural resources portfolio added value by outperforming their respective benchmarks.

a. Flash Performance Update as of August 31, 2023

   Mr. Callahan presented Fund performance updated through August 31, 2023. The DFA small cap portfolio continues to perform well, as do international equity and fixed income portfolios year to date. Commercial real estate is sharply negative, and public real assets exceeded the blended benchmark return.

There being no further business, Chair Klein adjourned the meeting at 12:54 p.m.

Sara Klein Investment Committee Chair	Attest: Jeff Wickman, Retirement Administrator