



Memorandum

DATE: March 18, 2024
TO: Members of the Board of Retirement
FROM: Tracy Bowman, Director of Finance
SUBJECT: **FOURTH QUARTER UNAUDITED FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2023**

Written Report

Background/Discussion

The attached financial statements reflect the unaudited financial activity for the year ended December 31, 2023. These reports are preliminary and do not reflect the reclassification of certain investments for financial reporting purposes and timing/market differences between investment manager statements and custodian bank statements. These, and other potential year-end adjustments that may result from the upcoming year-end audit, will be recorded if it is determined to have a material impact in the final Annual Comprehensive Financial Report (ACFR). The ACFR, the official financial statements of OCERS, will be available on our website, www.ocers.org, after the anticipated completion of the audit at the end of June 2024.

Summary

Statement of Fiduciary Net Position (Unaudited)

As of December 31, 2023, the net position restricted for pension, other postemployment benefits and employer is \$22.3 billion, an increase of \$2.1 billion, or 10.2%, from December 31, 2022. The change is a result of an increase in total assets of \$2 billion and a decrease in total liabilities of \$111 million as described below:

The \$2 billion increase in total assets can be attributed to increases of \$92.1 million in total cash and short-term investments, \$24.5 million in total receivables and \$1.8 billion in total investments at fair value, offset by a decrease of \$2.2 million in capital assets.

The increase of \$92.1 million in total cash and short-term investments consists of a \$124.2 million increase in securities lending collateral driven by an increase in demand in the securities lending program for OCERS' U.S. corporate bond and equity positions, offset by a decrease of \$32.1 million in cash and cash equivalents due to the timing of investing employee and employer contributions received during the quarter.

The increase of \$24.5 million in total receivables consists primarily of contributions, which increased by \$25.6 million. This is attributed to the County of Orange opting to not participate in the FY 2023-2024 contribution prepayment program resulting in a higher accrual for contributions earned, but not yet received.

Total investments at fair value increased \$1.8 billion, or 9.1% from December 31, 2022 to December 31, 2023. The total portfolio reported a net return of 11.4% for the one-year period ending December 31, 2023, compared to a

net loss of -7.8% for the same one-year period ending December 31, 2022. The fourth quarter for 2023 saw a rally across the public markets as inflation began easing and the Federal Reserve hinted at future interest rate cuts. Global public equity increased by \$1.6 billion, private equity increased by \$206.9 million, real assets increased by \$137.2 million, risk mitigation increased by \$56.7 million and unique strategies increased by \$46.7 million. These increases were offset by a decrease in income strategies of \$185.9 million. Global public equity saw the strongest performance coming from U.S. Large Cap Stocks and reported a one-year return of 22.9%, which exceeded the benchmark of 21.6%. Private equity reported a one-year return of 2.5% as investment managers continue to digest the higher interest rate environment. Income strategies, which is a new investment category that started in July 2023 and combines the core fixed income and credit categories, reported a one-year return of 6.7% with future interest rate cuts acting as a possible factor that may lift this asset class in the short and medium term. Real assets reported a loss of -0.4% for the one-year period. The real estate portfolio has continued to post losses due to the higher interest rate environment posting losses of -10.5% compared to positive returns for its peers in energy and infrastructure of 13.8% and 11.2%, respectively. Risk mitigation, designed to protect the portfolio during down periods, reported a return of 1.5% for the one-year period. Unique strategies reported a one-year return of 2.9% with a strong contribution from a general partner stake investment.

The decrease in capital assets of \$2.2 million from the prior year represents depreciation expense, which is primarily attributed to the Pension Administration System Solution (PASS).

Total liabilities decreased \$111 million, or -13%, from December 31, 2022 to December 31 2023, primarily due to unearned contributions, which decreased \$281.5 million due to the County of Orange opting to not participate in the FY 2023-2024 contribution prepayment program, as mentioned earlier. This decrease was offset by an increase of \$40.1 million related to the timing of securities purchased and an increase in obligations under the securities lending program of \$124.2 million, as previously discussed.

Statement of Changes in Fiduciary Net Position (Unaudited)

The ending net position restricted for pension, other postemployment benefits and employer as of December 31, 2023, increased by \$2.1 billion or 10.2%, when compared to the same period ending December 31, 2022.

Total additions to fiduciary net position increased 413.4% or \$4.4 billion from the previous year. Net investment income for the year ended December 31, 2023, was \$2.3 billion versus a loss of -\$2.1 billion for the year ended December 31, 2022, an increase of \$4.4 billion or 209.2%. The main cause of the increase is due to the net appreciation in fair value of investments, which increased \$4.6 billion from the prior year, slightly offset by a decrease in dividends, interest, and other investment income of \$203.8 million. The fourth quarter in 2023 reported a year-to-date net return of 11.4%, compared to a year-to-date net loss of -7.8% for the fourth quarter in 2022. This can be attributed to stronger year-to-date returns in 2023 compared to year-to-date returns in 2022 across most investment categories, including global public equity and income strategies, which reported positive year-to-date returns in 2023 compared to negative year-to-date returns in 2022. Private equity also reported a slightly higher year-to-date return in comparison to last year. These gains were offset by real assets, which reported a year-to-date loss for the fourth quarter in 2023 in comparison to year-to-date returns in 2022. Risk mitigation also reported a lower year-to-date return in 2023 compared to 2022. Total investment fees and expenses, including securities lending borrower rebates and bank charges, increased by \$25.8 million in December

2023 primarily due to a \$19.9 million increase in other fund expenses, which includes indirect flow-through investment expenses in limited partner structures. Security lending rebate fees increased \$8.0 million due to increases in the “risk free rate,” such as the Federal Funds Target Range or Overnight Bank Funding Rate (OBFR), that are used to negotiate rebates to borrowers. These increases were slightly offset by a net decrease of \$3.3 million in investment management fees, primarily due to a decrease in returns for the risk mitigation and real assets categories.

Total contributions increased \$19.1 million over the prior year due to employer contributions, which increased \$11.5 million, and employee contributions, which increased \$7.5 million. These increases can be attributed to increases in contribution rates.

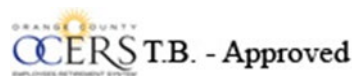
Total deductions from fiduciary net position increased 6.8%, or \$82.4 million, from the previous year. Participant benefits increased by \$84.7 million, which is expected due to the continued growth in member pension benefit payments, both in the total number of OCERS’ retired members receiving a pension benefit and an increase in the average benefit received. In December 2023, there were 20,966 payees with an average benefit payment of \$4,824 compared to 20,391 payees with an average benefit payment of \$4,653 in December 2022. Administrative expenses increased by \$5.5 million, primarily due to an increase in personnel services and professional services.

Other Supporting Schedules

In addition to the basic financial statements for the year ended December 31, 2023, the following supporting schedules are provided for additional information pertaining to OCERS:

- Total Plan Reserves
- Schedule of Contributions
- Schedule of Investment Expenses
- Schedule of Administrative Expenses
- Administrative Expense Compared to Projected Actuarial Accrued Liability

Submitted by:



Tracy Bowman
Director of Finance



Orange County Employees Retirement System

Unaudited Financial Statements

For the Year Ended December 31, 2023

Orange County Employees Retirement System

Unaudited Financial Statements For the Year Ended December 31, 2023

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Statement of Fiduciary Net Position (Unaudited)

As of December 31, 2023

(with summarized comparative amounts as of December 31, 2022)

(Dollars in Thousands)

	Pension Trust Fund	Health Care Fund- County	Health Care Fund- OCFA	Custodial Fund - OCTA	Total Funds	Comparative Totals 2022
Assets						
Cash and Short-Term Investments						
Cash and Cash Equivalents	\$ 370,080	\$ 7,976	\$ 1,326	\$ 628	\$ 380,010	\$ 412,122
Securities Lending Collateral	<u>318,271</u>	<u>6,859</u>	<u>1,140</u>	<u>-</u>	<u>326,270</u>	<u>202,096</u>
Total Cash and Short-Term Investments	688,351	14,835	2,466	628	706,280	614,218
Receivables						
Investment Income	20,747	447	74	-	21,268	15,320
Securities Sales	128,360	2,766	460	-	131,586	141,477
Contributions	41,072	-	-	-	41,072	15,437
Foreign Currency Forward Contracts	1,614	35	6	-	1,655	-
Other Receivables	<u>8,783</u>	<u>189</u>	<u>31</u>	<u>-</u>	<u>9,003</u>	<u>7,880</u>
Total Receivables	200,576	3,437	571	-	204,584	180,114
Investments at Fair Value						
Global Public Equity	10,136,607	218,458	36,307	13,293	10,404,665	8,828,613
Private Equity	3,422,713	73,764	12,260	-	3,508,737	3,301,871
Income Strategies	3,119,961	67,239	11,175	5,543	3,203,918	3,389,808
Real Assets	2,969,682	64,001	10,637	-	3,044,320	2,907,077
Risk Mitigation	1,769,352	38,132	6,337	-	1,813,821	1,757,155
Unique Strategies	<u>118,083</u>	<u>2,545</u>	<u>423</u>	<u>-</u>	<u>121,051</u>	<u>74,365</u>
Total Investments at Fair Value	21,536,398	464,139	77,139	18,836	22,096,512	20,258,889
Capital Assets, Net	<u>6,927</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,927</u>	<u>9,088</u>
Total Assets	<u>22,432,252</u>	<u>482,411</u>	<u>80,176</u>	<u>19,464</u>	<u>23,014,303</u>	<u>21,062,309</u>
Liabilities						
Obligations Under Securities Lending Program	318,272	6,859	1,140	-	326,271	202,096
Securities Purchased	238,481	5,140	854	-	244,475	204,403
Unearned Contributions	38,502	-	-	-	38,502	320,009
Foreign Currency Forward Contracts	16	-	-	-	16	2,367
Retiree Payroll Payable	98,751	5,011	716	-	104,478	98,325
Other	<u>26,019</u>	<u>561</u>	<u>93</u>	<u>-</u>	<u>26,673</u>	<u>24,142</u>
Total Liabilities	<u>720,041</u>	<u>17,571</u>	<u>2,803</u>	<u>-</u>	<u>740,415</u>	<u>851,342</u>
Net Position Restricted for Pension, Other Postemployment Benefits and Employer	<u>\$21,712,211</u>	<u>\$ 464,840</u>	<u>\$ 77,373</u>	<u>\$ 19,464</u>	<u>\$22,273,888</u>	<u>\$20,210,967</u>

Statement of Changes in Fiduciary Net Position (Unaudited)

For the Year Ended December 31, 2023

(with summarized comparative amounts for the Year Ended December 31, 2022)

(Dollars in Thousands)

	Pension Trust Fund	Health Care Fund- County	Health Care Fund- OCFA	Custodial Fund - OCTA	Total Funds	Comparative Totals 2022
Additions						
Contributions						
Employer	\$ 749,776	\$ -	\$ 26,245	\$ -	\$ 776,021	\$ 764,512
Employee	277,455	-	-	-	277,455	269,999
Employer OPEB Contributions	-	-	-	794	794	655
Total Contributions	1,027,231	-	26,245	794	1,054,270	1,035,166
Investment Income						
Net Appreciation/(Depreciation) in Fair Value of Investments	2,106,526	46,098	6,823	2,982	2,162,429	(2,463,745)
Dividends, Interest, & Other Investment Income	296,403	6,388	1,062	24	303,877	507,687
Securities Lending Income						
Gross Earnings	12,219	263	44	-	12,526	4,406
Less: Borrower Rebates and Bank Charges	(11,294)	(243)	(40)	-	(11,577)	(3,612)
Net Securities Lending Income	925	20	4	-	949	794
Total Investment Income/(Loss)	2,403,854	52,506	7,889	3,006	2,467,255	(1,955,264)
Investment Fees and Expenses	(163,590)	(3,525)	(586)	(3)	(167,704)	(149,896)
Net Investment Income/(Loss)	2,240,264	48,981	7,303	3,003	2,299,551	(2,105,160)
Total Additions	3,267,495	48,981	33,548	3,797	3,353,821	(1,069,994)
Deductions						
Participant Benefits	1,200,308	36,837	7,157	-	1,244,302	1,159,589
Death Benefits	1,189	-	-	-	1,189	1,558
Member Withdrawals and Refunds	14,752	-	-	-	14,752	22,239
Employer OPEB Payments	-	-	-	1,531	1,531	1,466
Administrative Expenses	29,056	24	23	23	29,126	23,614
Total Deductions	1,245,305	36,861	7,180	1,554	1,290,900	1,208,466
Net Increase/(Decrease)	2,022,190	12,120	26,368	2,243	2,062,921	(2,278,460)
Net Position Restricted For Pension, Other Postemployment Benefits and Employer, Beginning of Year	19,690,021	452,720	51,005	17,221	20,210,967	22,489,427
Ending Net Position Restricted For Pension, Other Postemployment Benefits and Employer	\$ 21,712,211	\$ 464,840	\$ 77,373	\$ 19,464	\$ 22,273,888	\$ 20,210,967

Total Plan Reserves

For the Year Ended December 31, 2023

(with summarized comparative amounts for the Year Ended December 31, 2022)

(Dollars in Thousands)

	2023	2022
Pension Reserve	\$ 13,115,567	\$ 11,947,372
Employee Contribution Reserve	3,915,650	3,794,047
Employer Contribution Reserve	3,214,949	3,443,588
Annuity Reserve	2,900,053	2,625,821
Health Care Reserve	542,213	503,725
Custodial Fund Reserve	19,464	17,221
County Investment Account (POB Proceeds) Reserve	146,109	140,991
OCSD UAAL Deferred Reserve	16,025	14,399
Contra Account and Actuarial Deferred Return	(1,596,142)	(2,276,197)
Total Net Position Restricted for Pension, Other Postemployment Benefits and Employer	\$ 22,273,888	\$ 20,210,967

Schedule of Contributions

For the Year Ended December 31, 2023

(with summarized comparative amounts for the Year Ended December 31, 2022)

(Dollars in Thousands)

	2023		2022	
	Employee	Employer	Employee	Employer
Pension Trust Fund Contributions				
County of Orange	\$ 205,958	\$ 587,980	\$ 202,014	\$ 572,012
Orange County Fire Authority	31,508	84,071 ¹	30,119	89,729 ¹
Orange County Superior Court of California	15,971	44,704	14,961	41,375
Orange County Transportation Authority	11,860	33,340	11,226	33,081
Orange County Sanitation District	8,539	8,887	8,371	8,686
Orange County Employees Retirement System	1,363	4,477	1,141	3,614
UCI - Medical Center and Campus	-	2,980 ²	-	3,223 ²
City of San Juan Capistrano	624	2,261	718	2,139
Transportation Corridor Agencies	871	867	769	895
Cypress Recreation and Parks District	-	-	-	596 ³
Orange County Department of Education	-	317 ²	-	367 ²
Orange County Cemetery District	198	274	191	285
Orange County Local Agency Formation Commission	57	237	46	195
Orange County In-Home Supportive Services Public Authority	160	202	147	197
Children and Families Commission of Orange County	174	254	131	208
Orange County Public Law Library	172	130	165	128
Contributions Before Prepaid Discount	277,455	770,981	269,999	756,730
Prepaid Employer Contributions Discount	-	(21,205)	-	(37,039)
Total Pension Trust Fund Contributions	277,455	749,776	269,999	719,691
Health Care Fund - County Contributions	-	-	-	41,889
Health Care Fund - OCFA Contributions	-	26,245	-	2,932
Custodial Fund - OCTA OPEB Contributions	-	794	-	655
Total Contributions	\$ 277,455	\$ 776,815	\$ 269,999	\$ 765,167

¹ Unfunded actuarial accrued liability payments were made in 2023 for \$13.8 million and 2022 for \$11.8 million for the Orange County Fire Authority.

² Unfunded actuarial accrued liability payments have been made in accordance with a separate 20-year level dollar payment schedule to include liabilities for employee benefits related to past service credit.

³ This balance reflects the unfunded actuarial accrued liability obligation payment made in July 2022 to fund the obligations for the ongoing benefits owed to Cypress Recreation & Parks District's retired and disabled employees and their survivors and beneficiaries.

Schedule of Investment Expenses

For the Year Ended December 31, 2023

(with summarized comparative amounts for the Year Ended December 31, 2022)

(Dollars in Thousands)

	2023	2022
Investment Management Fees*		
Global Public Equity	\$ 12,336	\$ 15,287
Income Strategies	15,045	12,190
Real Assets	29,497	32,314
Private Equity	39,269	31,508
Risk Mitigation	10,034	19,186
Unique Strategies	2,163	1,049
Short-Term Investments	123	201
Total Investment Management Fees	108,467	111,735
Other Fund Expenses¹	51,695	31,823
Other Investment Expenses		
Consulting/Research Fees	2,272	2,310
Investment Department Expenses	4,226	2,865
Legal Services	435	539
Custodian Services	580	580
Investment Service Providers	26	41
Total Other Investment Expenses	7,539	6,335
Security Lending Activity		
Security Lending Fees	245	204
Rebate Fees	11,332	3,408
Total Security Lending Activity	11,577	3,612
Custodial Fund - OCTA Investment Fees and Expenses	3	3
Total Investment Expenses	\$ 179,281	\$ 153,508

* Does not include undisclosed fees deducted at source.

¹ These costs include, but are not limited to, foreign income tax and other indirect flow-through investment expenses such as organizational expenses in limited partnership structures.

Schedule of Administrative Expenses

For the Year Ended December 31, 2023

(with summarized comparative amounts for the Year Ended December 31, 2022)

(Dollars in Thousands)

	2023	2022
Pension Trust Fund Administrative Expenses		
Expenses Subject to the Statutory Limit		
Personnel Services		
Employee Salaries and Benefits	\$ 17,829	\$ 14,578
Board Members' Allowance	13	13
Total Personnel Services	<u>17,842</u>	<u>14,591</u>
Office Operating Expenses		
Depreciation/Amortization	2,695	2,626
Professional Services	3,266	2,179
General Office and Administrative Expenses	2,750	1,841
Rent/Leased Real Property	813	740
Total Office Operating Expenses	<u>9,524</u>	<u>7,386</u>
Total Expenses Subject to the Statutory Limit	<u>27,366</u>	<u>21,977</u>
Expenses Not Subject to the Statutory Limit		
Information Technology Professional Services	617	558
Information Security Professional Services	144	123
Finance Software Professional Services	9	52
Actuarial Fees	377	339
Equipment/Software	543	497
Total Expenses Not Subject to the Statutory Limit	<u>1,690</u>	<u>1,569</u>
Total Pension Trust Fund Administrative Expenses	29,056	23,546
Health Care Fund - County Administrative Expenses	24	23
Health Care Fund - OCFA Administrative Expenses	23	22
Custodial Fund - OCTA Administrative Expenses	<u>23</u>	<u>23</u>
Total Administrative Expenses	\$ <u>29,126</u>	\$ <u>23,614</u>

Administrative Expense Compared to Projected Actuarial Accrued Liability

For the Year Ended December 31, 2023

(Dollars in Thousands)

Actuarial Accrued Liability (AAL) as of 12/31/23	\$	26,477,040
Maximum Allowed for Administrative Expense (AAL * 0.21%)		55,602
Actual Administrative Expense ¹		<u>27,366</u>
Excess of Allowed Over Actual Expense	\$	<u>28,236</u>
Actual Administrative Expense for the year ended 12/31/23 as a Percentage of Actuarial Accrued Liability as of 12/31/23		0.10%
Actual Administrative Expense for the year ended 12/31/22 as a Percentage of Actuarial Accrued Liability as of 12/31/22		0.09%
¹ Administrative Expense Reconciliation		
Administrative Expense per Statement of Changes in Fiduciary Net Position	\$	29,056
Less: Administrative Expense Not Considered per CERL Section 31596.1		<u>(1,690)</u>
Administrative Expense Allowable Under CERL Section 31580.2	\$	<u>27,366</u>