

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

INVESTMENT COMMITTEE MEETING
January 24, 2018

MINUTES

Attendance was as follows:

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

Absent: Russell Baldwin; and Charles Packard

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

Meketa Investment Group: Laura Wirick, CFA
Pension Consulting Alliance: Allan Emkin

The Chair called the meeting to order at 9:00 a.m. Mr. Dewane 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. Eley and seconded by Mr. Ball to approve the Consent Agenda. The motion carried unanimously.

C-1 COMMITTEE MEETING:

Approval of Meeting and Minutes

Investment Committee Meeting

December 13, 2017

Recommendation: Authorize meeting and approve minutes.

C-2 QUIET PERIOD - INVESTMENT RELATED SEARCHES

Recommendation: Receive and file.

C-3 SECURITIES LITIGATION UPDATE

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 U.S. equity markets and recent USD price action. She also commented on OCERS' private equity program, the cryptocurrency markets, and blockchain technology.

Mr. Lindholm and Ms. Murphy briefly discussed cryptocurrency within the hedge fund industry.

Mr. Prevatt arrived at 9:08 a.m.

I-3 ILLIQUID INVESTMENTS ADVISORY SERVICES RFP UPDATE

Presentation by Molly Murphy, CFA, CIO, OCERS

Ms. Murphy provided an update on OCERS' Illiquid Investments Advisory Services RFP.

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

I-4 PIMCO: 2018 ECONOMIC OUTLOOK

Presentation by Mihir P. Worah & Michael Chandra, CFA, PIMCO

Ms. Murphy introduced PIMCO's Mr. Worah and Mr. Chandra.

Mr. Worah presented PIMCO's 2018 economic outlook, including a discussion on synchronized global growth and risk assets, as well as risks to their outlook.

Mr. Emkin and Ms. Wirick discussed their respective firms' outlook, particularly where their firms have consensus and divergent views relative to PIMCO as well as to the market.

Ms. Murphy provided an update on OCERS' asset allocation. She described that while OCERS has reduced risk at the margin as a modest acknowledgement that the market cycle is likely in its late stages, she also noted that OCERS is a strategic long-term asset allocator that does not aim to time the markets.

Ms. Freidenrich arrived at 9:58 a.m.

A **motion** was made by Mr. Dewane and **seconded** by Mr. Eley to receive and file I-4. The **motion carried unanimously.**

The Committee recessed at 10:18 a.m.

The Committee reconvened at 10:33 a.m.

Mr. Gilbert arrived at 10:33 a.m.

I-5 PORTFOLIO ACTIVITY REPORT

Presentation by Molly Murphy, CFA, CIO & David Beeson, IO, OCERS

Ms. Murphy and Mr. Beeson presented the portfolio activity report, including the total fund overview, subscriptions and redemptions, as well as the asset allocation for December 2017. Mr. Beeson also provided an update on the employer prepayment program.

Mr. Ball, Mr. Eley, and Ms. Murphy discussed OCERS' cash overlay program, including a discussion on Parametric's portfolio replication capabilities and on its role relative to passive and active investment management.

Ms. Murphy further noted that Parametric's portfolio replication capabilities are more suited for liquid assets and less so for illiquid assets.

Mr. Ball and Ms. Murphy discussed the late-cycle direct lending environment, OCERS' direct lending portfolio, and its expected risk-reward characteristics.

Mr. Beeson discussed 4th quarter and 2017 year-to-date performance figures for the OCERS portfolio and the global markets. He also presented performance figures for select global markets through the end of January 19, 2018.

Mr. Ball and Mr. Beeson discussed OCERS' recent outperformance, specifically a brief review on its attribution from active investment managers versus passive investment managers.

Ms. Freidenrich and Ms. Murphy briefly discussed recent currency performance and its impact upon various benchmarks priced in local currencies and in USD.

A **motion** was made by Mr. Dewane and **seconded** by Mr. Gilbert to receive and file I-5. The **motion carried unanimously.**

I-6 CURRENCY HEDGING

Presentation by Molly Murphy, CFA, CIO, OCERS & Laura Wirick, CFA, Meketa

Ms. Wirick provided Meketa's Currency Hedging presentation. She particularly described the associated costs and benefits of currency hedging. She reported that there is no academic consensus on target or ideal levels of hedging, i.e., fully hedged or a half-hedged portfolio.

Ms. Murphy agreed and further commented that despite various levels of currency hedging, there is effectively negligible long-term performance dispersion that results from the various hedge levels.

Mr. Lindholm, Mr. Ball, and Ms. Wirick discussed the direct relationship between emerging market currency performance and OCERS' emerging market portfolios.

Mr. Ball and Ms. Murphy discussed hedging costs due to interest rate differentials, particularly in emerging markets relative to developed markets.

Ms. Wirick recommended that OCERS' portfolio be neither strategically nor tactically hedged at this time; she further explained that Meketa and staff would communicate and recommend to the Committee should there be a beneficial tactical hedge opportunity (e.g., risk management purposes, market dislocation).

Mr. Ball and Mr. Emkin expressed agreement with Meketa's and staff's recommendation.

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

I-7 INVESTMENT CHARTERS & POLICIES REVIEW

Presentation by Molly Murphy, CFA, CIO, OCERS

Ms. Murphy presented staff's review of the OCERS Investment Charters and Policies. She provided an overview of changes, including the rationalization of sections that overlapped, and sections that were either out of synch or in contradiction with each other. She discussed material changes, particularly those recommended for the Investment Committee and CIO Charters.

The Committee, staff, and consultants deliberated about changes made to the Investment Committee and CIO Charters, particularly the delegation of authority from the Committee to the CIO over manager surveillance and action procedure.

Ms. Murphy stated that such delegation would require the alignment of staff and OCERS' investment consultants, Meketa, or the appropriate specialist consultant for a particular asset class, pursuant to the approved asset allocation targets, ranges and risk profile. She described that a successful implementation of this change would include ongoing communication throughout the manager surveillance and action procedure between staff, consultants, and the Committee, as well as Committee education sessions on investment strategies should the need arise.

Mr. Eley and Ms. Murphy further discussed the costs and benefits associated with the change in delegated authority for manager surveillance and action.

Mr. Ball expressed support for staff's recommended changes, opining that the Committee's involvement in manager decisions may lead to biased Committee decisions based on the managers' marketing ability, rather than the managers' investment acumen.

Ms. Murphy indicated that staff tested this recommended change with the active core bond manager process that commenced months before the actual hiring at the December 2017 Investment Committee meeting. She also caveated that the only difference being that in the future, staff, and consultants would not have a formal recommendation.

Ms. Freidenrich expressed broad support for the change in delegation, but also shared her concerns, noting that such a material change would require her more time to weigh the potential

costs and benefits. She suggested that the change include more details, particularly as it relates to allocation limits.

Mr. Hilton expressed concerns regarding the change in delegation, including a concern that this change could result in over-delegation or other unintentional outcomes.

Mr. Dewane expressed support for the recommended change, explaining that this change is in line with the industry's best practices. He noted that, regardless of the amount of time the Committee spends on manager decisions, it would inherently pale in comparison relative to the amount of time spent by staff and consultants. He stated that manager surveillance and action forms the basis of OCERS' hiring of the CIO and consultants, opining that their experience would translate into a more objective evaluation. He explained that the Committee can make modifications to the recommended changes should the need arise.

A **motion** was made by Mr. Dewane and **seconded** by Mr. Prevatt to approve the following amended charters and policies:

1. Investment Committee Charter
2. Chief Investment Officer Charter
3. Investment Policy Statement
4. Proxy Voting Policy
5. Placement Agent Disclosure Policy
6. Code of Ethics and Standard of Conduct Policy

Rescind the following:

1. Absolute Return Investment Policy Statement
2. Due Diligence Policy
3. Real Estate Strategic Plan Investment Policy Statement
4. Investment Fee Policy
5. OCERS Investment Beliefs as a standalone document (now incorporated verbatim into the Investment Policy Statement)

Ms. Wirick observed that many of Meketa's clients as well as OCERS' larger peers already have this delegation of authority in place; she reported that pensions without such delegation are moving in the direction of delegated authority. She also observed that where this delegation goes wrong is in communication regarding procedures, and not policies.

Mr. Emkin expressed support for the recommended change, observing that corporate pension plans and most endowments and large state pensions delegate manager decisions to the CIO. He considered that today's pension environment is different from the past, observing that more experienced and informed investment staff negates the need for Committees to have manager authority.

Ms. Wirick provided examples of clients where the CIO had delegated authority, including examples where different parts of the portfolio had unique allocation authority limits.

Ms. Wirick, Ms. Murphy, and Ms. Freidenrich discussed the review frequency of the Investment Committee and CIO Charters.

Ms. Murphy stated that the best practice is to revisit the Investment Committee Charter and CIO Charter annually, versus OCERS' current practice of revisiting every three years.

Mr. Eley explained the need for appropriate checks and balances and stated that he would vote no based on OCERS' prior history.

Mr. Prevatt suggested that the Committee needs to evolve from an operational Board to a policy Board, noting the responsibility of staff to implement the Committee's set parameters. He opined that for the Committee to have manager authority is a disservice to OCERS, recognizing that the Committee does not have that level of background and knowledge.

Mr. Dewane and Mr. Prevatt both expressed agreement that, in an effort to initiate the Committee's progression towards a strategic Board, the Committee should approve staff's recommended changes, while also retaining the ability to make further changes should the need arise.

Mr. Gilbert asked about potential scenarios where OCERS' consultants and staff may not agree.

Ms. Murphy and Mr. Ball explained the impossibility, stating that any manager action first requires unanimous consensus amongst the consultants and the CIO.

Mr. Emkin stated that OCERS should formalize a process that supports the independence of the consultants, thus preventing potential scenarios where the consultants may be forced to agree with the CIO.

Ms. Wirick and Ms. Murphy discussed situations where the manager surveillance and action procedure may require timeliness, i.e., key-man risk, opportunistic investment themes.

Mr. Lindholm confirmed his support for the change in delegation of authority. He also shared his support of Mr. Dewane's and Mr. Prevatt's notion that the Committee should move forward with the recommended changes, while also retaining the ability to make further changes should the need arise.

Mr. Prevatt and Mr. Dewane gave direction to staff to come back at a future Investment Committee meeting with suggestions regarding allocation limits and control procedures for consideration.

Mr. Dewane agreed with Mr. Prevatt's suggested modification to his original motion.

Ms. Freidenrich, Mr. Delaney, and Ms. Murphy discussed the costs and benefits of moving forward with the recommended changes now, versus at a later Investment Committee meeting.

Mr. Delaney and Ms. Murphy also stated that there were not any imminent recommended manager transactions, confirming that there would likely be more modifications to the manager decision procedure before any transaction would be undertaken.

Ms. Murphy and Ms. Wirick also confirmed that at the next Investment Committee meeting, staff and Meketa would not only present more detailed and auditable manager surveillance and action procedures, but also provide more information regarding best industry practice at other U.S. pension systems.

Mr. Eley and Ms. Murphy agreed that Trustees should email the CEO and CIO suggestions and modifications for further discussion at the next Investment Committee meeting.

Mr. Gilbert asked Mr. Dewane to clarify the motion.

Mr. Dewane responded and confirmed that the motion was staff's recommendation.

After further discussion, the Committee voted on the **motion** made by Mr. Dewane, **seconded** by Mr. Prevatt to approve the following amended charters and policies:

1. Investment Committee Charter
2. Chief Investment Officer Charter
3. Investment Policy Statement
4. Proxy Voting Policy
5. Placement Agent Disclosure Policy
6. Code of Ethics and Standard of Conduct Policy

Rescind the following:

1. Absolute Return Investment Policy Statement
2. Due Diligence Policy
3. Real Estate Strategic Plan Investment Policy Statement
4. Investment Fee Policy
5. OCERS Investment Beliefs as a standalone document (now incorporated verbatim into the Investment Policy Statement)

The **motion carried 5-3** with voting as follows:

AYES

Mr. Ball
Mr. Dewane
Mr. Gilbert
Mr. Prevatt
Chair Lindholm

NAYS

Ms. Freidenrich
Mr. Hilton
Mr. Eley

ABSTAIN

ABSENT

Mr. Baldwin
Mr. Packard

* * * * ***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

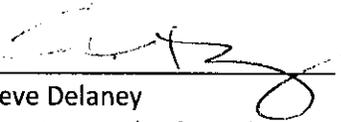
None

COUNSEL COMMENTS

None

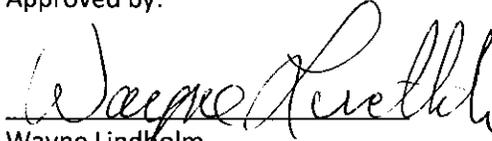
ADJOURNMENT: The Chair adjourned the meeting at 12:22 p.m.

Submitted by:



Steve Delaney
Secretary to the Committee

Approved by:



Wayne Lindholm
Chair