

Memorandum

DATE: November 18, 2024
TO: Members of the Board of Retirement
FROM: Tracy Bowman, Director of Finance
SUBJECT: **THIRD QUARTER UNAUDITED FINANCIAL STATEMENTS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2024**

Written Report

Background/Discussion

The attached financial statements reflect the unaudited financial activity for the nine months ended September 30, 2024. These statements are unaudited and are not the official financial statements of OCERS. The following statements represent a review of the progress to date for the third quarter of 2024. The official financial statements of OCERS are included in the Annual Comprehensive Financial Report (ACFR) for the year ended December 31, 2023, which is available on our website, www.ocers.org.

Summary

Statement of Fiduciary Net Position (Unaudited)

As of September 30, 2024, the net position restricted for pension, other postemployment benefits and employer is \$24.6 billion, an increase of \$3.5 billion, or 16.6%, from September 30, 2023. The change is a result of an increase in total assets of \$3.7 billion, offset by an increase in total liabilities of \$207.1 million as described below:

The \$3.7 billion increase in total assets can be attributed to increases of \$1.2 billion in total cash and short-term investments, \$131 million in total receivables and \$2.4 billion in total investments at fair value, offset by a decrease of \$1.3 million in capital assets.

The increase of \$1.2 billion in total cash and short-term investments consists of a \$1.2 billion increase in cash and cash equivalents due to the timing of investing employee and employer contributions received during the quarter and an increase of \$1.1 billion in the new futures overlay account. These increases were offset by a slight decrease of \$25.6 million in securities lending collateral, which resulted from reduced demand in the securities lending program for OCERS' U.S. corporate bond and equity positions.

The increase of \$131 million in total receivables consists of increases of \$33.6 million in investment income, \$81 million in pending securities sales and \$15.3 million in contributions 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 \$2.4 billion, or 11.5% from September 30, 2023 to September 30, 2024. The total portfolio reported a net return of 17.7% for the one-year period ending September 30, 2024, compared

to a net return of 9% for the same one-year period ending September 30, 2023. Over the past year, the economy has shown resilience to higher interest rates, despite the introduction of a new geopolitical risk stemming from the Israel-Hamas conflict in the Middle East. In addition, the Federal Reserve (Fed) reduced interest rates by half a percentage point in September 2024, after observing signs that inflation was continuing its trajectory toward the Fed's 2% target and the labor market cooling considerably. This has resulted in strong returns in equities and bonds over the last twelve months. Global public equity increased by \$1.3 billion, private equity increased by \$313.6 million, income strategies increased by \$501.3 million, real assets increased by \$148.4 million, risk mitigation increased by \$57.6 million and unique strategies increased by \$108.3 million.

Global public equity posted a 31.5% return over the one-year period which surpassed the benchmark of 31% largely due to the influence of the "Magnificent Seven" large-cap technology companies (Amazon, Alphabet, Microsoft, Apple, Tesla, Meta Platforms and NVIDIA) whose high market capitalizations significantly impacted the overall market. Private equity yielded a return of 5.9% mainly due to its sensitivity to higher interest rates and fewer transactions in this sector, which generally faces sensitivity to rate environments. Income strategies achieved a return of 11.3% mainly driven by strong public fixed income returns of 12.5% over twelve months, largely attributed to the Fed's interest rate cut in September. Real assets returned 3.9% with real estate underperforming amid a higher interest rate environment and challenges in the commercial real estate sector; however, the energy portfolio delivered a strong a one-year return of 21.4% mainly due to high activity in the sector and favorable exit valuations. Risk mitigation reported a one-year return of 3.2%, aligning with its role of safeguarding the portfolio during market downturns. Unique strategies achieved a 10.9% return driven by strong performance from investments in general partner stakes.

The decrease in capital assets of \$1.3 million from the prior year represents depreciation expense, which is primarily attributed to the Pension Administration System Solution (PASS).

Total liabilities increased \$207.1 million, or 35.6%, from September 30, 2023 to September 30 2024, primarily due to an increase of \$141 million in liabilities for securities purchased, mainly due to the timing of these transactions, as well as an \$88.2 million increase in retiree payroll payable, which was affected by the timing of payroll distribution; in 2023, October 1 fell on a Sunday, leading to an early payout on September 29, resulting in a smaller liability compared to 2024, when October 1 fell on a Tuesday, resulting in a larger liability at the period end. These increases were offset by a decrease of \$25.6 million in obligations under securities lending program, as mentioned earlier.

Statement of Changes in Fiduciary Net Position (Unaudited)

The ending net position restricted for pension, other postemployment benefits and employer as of September 30, 2024, increased by \$3.5 billion or 16.6%, when compared to the same period ending September 30, 2023.

Total additions to fiduciary net position increased 78% or \$1.4 billion from the previous year. Net investment income for the nine months ended September 30, 2024, was \$2.3 billion versus \$1 billion for the nine months ended September 30, 2023, an increase of \$1.3 billion or 131%. The increase can be attributed to an increase in net appreciation in fair value of investments which increased \$1.2 billion and an increase in dividends, interest, and other investment income which increased \$94 million from the prior year. The third quarter in 2024 reported a year-to-date net return of 10.9%, compared to a year-to-date net return of 5% for the third quarter in 2023.

Total investment fees and expenses increased by \$16.6 million in September 2024 primarily due to a \$21.9 million increase in total investment management fees, which was partially offset by a decrease of \$5.9 million in other fund expenses, including indirect flow-through investment expenses in limited partner structures. Overall, the strong growth in net investment income and higher returns were key contributors to the significant increase in fiduciary net position additions.

Total contributions increased \$80.8 million over the prior year due to employer contributions, which increased \$62.9 million, and employee contributions, which increased \$17.6 million. These increases can be attributed to increases in contribution rates.

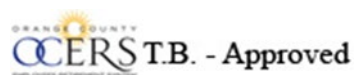
Total deductions from fiduciary net position increased 5.7%, or \$54.5 million, from the previous year. Participant benefits increased by \$48 million, which is expected due to the continued growth in member pension benefit payments, both in the total number of OCERS' retired members receiving a pension benefit and an increase in the average benefit received. In September 2024, there were 21,369 payees with an average benefit payment of \$4,969 compared to 20,917 payees with an average benefit payment of \$4,813 in September 2023.

Other Supporting Schedules

In addition to the basic financial statements for the nine months ended September 30, 2024, 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 Nine Months Ended September 30, 2024

Orange County Employees Retirement System

Unaudited Financial Statements
For the Nine Months Ended September 30, 2024

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Statement of Fiduciary Net Position (Unaudited)

As of September 30, 2024

(with summarized comparative amounts as of September 30, 2023)

(Dollars in Thousands)

	Pension Trust Fund	Health Care Fund- County	Health Care Fund- OCFA	Custodial Fund - OCTA	Total Funds	Comparative Totals 2023
Assets						
Cash and Short-Term Investments						
Cash and Cash Equivalents	\$ 1,369,902	\$ 28,000	\$ 6,378	\$ 155	\$1,404,435	\$ 207,139
Securities Lending Collateral	<u>218,108</u>	<u>4,458</u>	<u>1,016</u>	<u>-</u>	<u>223,582</u>	<u>249,146</u>
Total Cash and Short-Term Investments	1,588,010	32,458	7,394	155	1,628,017	456,285
Receivables						
Investment Income	49,303	1,008	230	-	50,541	16,991
Securities Sales	188,288	3,849	877	-	193,014	112,047
Contributions	70,111	-	-	-	70,111	54,823
Foreign Currency Forward Contracts	636	13	3	-	652	229
Other Receivables	<u>8,757</u>	<u>179</u>	<u>41</u>	<u>-</u>	<u>8,977</u>	<u>8,221</u>
Total Receivables	317,095	5,049	1,151	-	323,295	192,311
Investments at Fair Value						
Global Public Equity	10,508,885	214,795	48,929	15,782	10,788,391	9,512,232
Private Equity	3,751,324	76,675	17,466	-	3,845,465	3,531,894
Income Strategies	3,496,308	71,462	16,279	5,798	3,589,847	3,088,504
Real Assets	3,038,252	62,100	14,146	-	3,114,498	2,966,140
Risk Mitigation	1,802,315	36,838	8,392	-	1,847,545	1,789,983
Unique Strategies	<u>188,992</u>	<u>3,863</u>	<u>880</u>	<u>-</u>	<u>193,735</u>	<u>85,438</u>
Total Investments at Fair Value	22,786,076	465,733	106,092	21,580	23,379,481	20,974,191
Capital Assets, Net	<u>6,015</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,015</u>	<u>7,340</u>
Total Assets	<u>24,697,196</u>	<u>503,240</u>	<u>114,637</u>	<u>21,735</u>	<u>25,336,808</u>	<u>21,630,127</u>
Liabilities						
Obligations Under Securities Lending Program	218,108	4,458	1,016	-	223,582	249,146
Securities Purchased	360,344	7,365	1,678	-	369,387	228,444
Unearned Contributions	60,443	-	-	-	60,443	56,015
Retiree Payroll Payable	103,827	4,600	696	-	109,123	20,912
Other	<u>25,458</u>	<u>520</u>	<u>119</u>	<u>-</u>	<u>26,097</u>	<u>27,041</u>
Total Liabilities	<u>768,180</u>	<u>16,943</u>	<u>3,509</u>	<u>-</u>	<u>788,632</u>	<u>581,558</u>
Net Position Restricted for Pension, Other Postemployment Benefits and Employer	<u>\$23,929,016</u>	<u>\$ 486,297</u>	<u>\$ 111,128</u>	<u>\$ 21,735</u>	<u>\$24,548,176</u>	<u>\$21,048,569</u>

Statement of Changes in Fiduciary Net Position (Unaudited)

For the Nine Months Ended September 30, 2024

(with summarized comparative amounts for the Nine Months Ended September 30, 2023)

(Dollars in Thousands)

	Pension Trust Fund	Health Care Fund- County	Health Care Fund- OCFA	Custodial Fund - OCTA	Total Funds	Comparative Totals 2023
Additions						
Contributions						
Employer	\$ 617,640	\$ -	\$ 29,631	\$ -	\$ 647,271	\$ 584,369
Employee	224,146	-	-	-	224,146	206,531
Employer OPEB Contributions	-	-	-	827	827	575
Total Contributions	841,786	-	29,631	827	872,244	791,475
Investment Income						
Net Appreciation in Fair Value of Investments	2,098,488	44,749	9,071	2,744	2,155,052	907,125
Dividends, Interest, & Other Investment Income	316,851	6,476	1,475	15	324,817	230,787
Securities Lending Income						
Gross Earnings	9,145	187	43	-	9,375	8,927
Less: Borrower Rebates and Bank Charges	(8,567)	(175)	(40)	-	(8,782)	(8,225)
Net Securities Lending Income	578	12	3	-	593	702
Total Investment Income	2,415,917	51,237	10,549	2,759	2,480,462	1,138,614
Investment Fees and Expenses	(140,293)	(2,867)	(653)	(2)	(143,815)	(127,206)
Net Investment Income	2,275,624	48,370	9,896	2,757	2,336,647	1,011,408
Total Additions	3,117,410	48,370	39,527	3,584	3,208,891	1,802,883
Deductions						
Participant Benefits	946,725	26,893	5,762	-	979,380	931,427
Death Benefits	1,456	-	-	-	1,456	636
Member Withdrawals and Refunds	14,236	-	-	-	14,236	10,195
Employer OPEB Payments	-	-	-	1,296	1,296	1,131
Administrative Expenses	23,406	18	16	17	23,457	21,892
Total Deductions	985,823	26,911	5,778	1,313	1,019,825	965,281
Net Increase	2,131,587	21,459	33,749	2,271	2,189,066	837,602
Net Position Restricted For Pension, Other Postemployment Benefits and Employer, Beginning of Year	21,797,429	464,838	77,379	19,464	22,359,110	20,210,967
Ending Net Position Restricted For Pension, Other Postemployment Benefits and Employer	\$ 23,929,016	\$ 486,297	\$ 111,128	\$ 21,735	\$ 24,548,176	\$ 21,048,569

Total Plan Reserves

For the Nine Months Ended September 30, 2024

(with summarized comparative amounts for the Nine Months Ended September 30, 2023)

(Dollars in Thousands)

	2024	2023
Pension Reserve	\$ 13,686,648	\$ 12,902,598
Employee Contribution Reserve	3,993,123	3,797,361
Employer Contribution Reserve	3,098,774	2,890,481
Annuity Reserve	3,049,171	2,832,438
Health Care Reserve	597,425	521,452
Custodial Fund Reserve	21,735	17,920
County Investment Account (POB Proceeds) Reserve	156,488	140,150
OCSD UAAL Deferred Reserve	16,025	14,398
Contra Account and Actuarial Deferred Return	(71,213)	(2,068,229)
Total Net Position Restricted for Pension, Other Postemployment Benefits and Employer	\$ 24,548,176	\$ 21,048,569

Schedule of Contributions

For the Nine Months Ended September 30, 2024

(with summarized comparative amounts for the Nine Months Ended September 30, 2023)

(Dollars in Thousands)

	2024		2023	
	Employee	Employer	Employee	Employer
Pension Trust Fund Contributions				
County of Orange	\$ 166,916	\$ 480,491	\$ 153,609	\$ 440,748
Orange County Fire Authority	24,688	63,057 ¹	23,196	63,187 ¹
Orange County Superior Court of California	12,848	35,249	11,799	33,575
Orange County Transportation Authority	9,714	26,065	8,836	25,268
Orange County Sanitation District	7,006	7,091	6,346	6,591
Orange County Employees Retirement System	1,164	3,836	1,029	3,399
UCI - Medical Center and Campus	-	2,181 ²	-	2,264 ²
City of San Juan Capistrano	507	1,736	465	1,708
Transportation Corridor Agencies	679	754	687	653
Orange County Department of Education	-	249 ²	-	237 ²
Orange County Cemetery District	149	198	147	207
Orange County Local Agency Formation Commission	40	161	41	175
Orange County In-Home Supportive Services Public Authority	137	166	118	151
Children and Families Commission of Orange County	155	201	130	194
Orange County Public Law Library	132	99	128	97
Orange County Mosquito and Vector Control District	11	-	-	-
Contributions Before Prepaid Discount	224,146	621,534	206,531	578,454
Prepaid Employer Contributions Discount	-	(3,894)	-	(19,998)
Total Pension Trust Fund Contributions	224,146	617,640	206,531	558,456
Health Care Fund - OCFA Contributions	-	29,631	-	25,913
Custodial Fund - OCTA OPEB Contributions	-	827	-	575
Total Contributions	\$ 224,146	\$ 648,098	\$ 206,531	\$ 584,944

¹ Unfunded actuarial accrued liability payments were made in 2024 for \$11.2 million and 2023 for \$10.3 million by 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.

Schedule of Investment Expenses

For the Nine Months Ended September 30, 2024

(with summarized comparative amounts for the Nine Months Ended September 30, 2023)

(Dollars in Thousands)

	2024	2023
Investment Management Fees*		
Global Public Equity	\$ 11,086	\$ 9,140
Income Strategies	13,626	10,814
Real Assets	32,897	23,695
Private Equity	36,471	31,795
Risk Mitigation	7,168	7,213
Unique Strategies	4,132	893
Short-Term Investments	121	93
Total Investment Management Fees	105,501	83,643
Other Fund Expenses¹	32,074	37,959
Other Investment Expenses		
Consulting/Research Fees	1,766	1,697
Investment Department Expenses	3,768	3,093
Legal Services	239	361
Custodian Services	435	435
Investment Service Providers	30	16
Total Other Investment Expenses	6,238	5,602
Security Lending Activity		
Security Lending Fees	136	174
Rebate Fees	8,646	8,051
Total Security Lending Activity	8,782	8,225
Custodial Fund - OCTA Investment Fees and Expenses	2	2
Total Investment Expenses	\$ 152,597	\$ 135,431

* 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 Nine Months Ended September 30, 2024

(with summarized comparative amounts for the Nine Months Ended September 30, 2023)

(Dollars in Thousands)

	2024	2023
Pension Trust Fund Administrative Expenses		
Expenses Subject to the Statutory Limit		
Personnel Services		
Employee Salaries and Benefits	\$ 14,932	\$ 13,251
Board Members' Allowance	8	10
Total Personnel Services	14,940	13,261
Office Operating Expenses		
Depreciation/Amortization	1,889	2,016
Professional Services	2,065	2,610
General Office and Administrative Expenses	2,405	2,034
Rent/Leased Real Property	752	567
Total Office Operating Expenses	7,111	7,227
Total Expenses Subject to the Statutory Limit	22,051	20,488
Expenses Not Subject to the Statutory Limit		
Information Technology Professional Services	723	456
Information Security Professional Services	113	90
Finance Software Professional Services	3	6
Actuarial Fees	314	297
Equipment/Software	202	503
Total Expenses Not Subject to the Statutory Limit	1,355	1,352
Total Pension Trust Fund Administrative Expenses	23,406	21,840
Health Care Fund - County Administrative Expenses	18	18
Health Care Fund - OCFA Administrative Expenses	16	17
Custodial Fund - OCTA Administrative Expenses	17	17
Total Administrative Expenses	\$ 23,457	\$ 21,892

Administrative Expense Compared to Projected Actuarial Accrued Liability

For the Nine Months Ended September 30, 2024

(Dollars in Thousands)

Projected Actuarial Accrued Liability (AAL) as of 12/31/24	\$	27,920,705
Maximum Allowed for Administrative Expense (AAL * 0.21%)		58,633
Actual Administrative Expense ¹		<u>22,051</u>
Excess of Allowed Over Actual Expense	\$	<u>36,582</u>
Actual Administrative Expense for the nine months ended 9/30/24 as a Percentage of Projected Actuarial Accrued Liability as of 12/31/24		0.08%
Actual Administrative Expense for the six months ended 9/30/23 as a Percentage of Projected Actuarial Accrued Liability as of 12/31/23		0.08%
¹ Administrative Expense Reconciliation		
Administrative Expense per Statement of Changes in Fiduciary Net Position	\$	23,406
Less: Administrative Expense Not Considered per CERL Section 31596.1		<u>(1,355)</u>
Administrative Expense Allowable Under CERL Section 31580.2	\$	<u>22,051</u>