

**SONOMA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
INVESTMENT COMMITTEE MEETING MINUTES**

Thursday, June 27, 2024

8:35 a.m.

Presiding: Greg Jahn, Chair

Present: Trustees Travis Balzarini, Amos Eaton, Erick Roeser (Vice Chair), Joe Tambe, Mark Walsh, Brian Williams; Chief Investment Officer Jim Failor, Investment Officer Mickey Nguyen, Retirement Analyst Rebecca Gay, and Administrative Aide Julia Smith; Alexis Georgiadis (of Davidson Kempner)

Present via

Zoom: Chief Executive Officer Julie Wyne; Josh Morris and Romain Levin (of Davidson Kempner); Tim Pflugradt and Chris Behrns (of Aon)

Absent: Trustees Neil Baker (Alternate Retiree), Chris Coursey and Bob Williamson

Public comments were solicited prior to the meeting by emailing Rebecca.Gay@sonoma-county.org. Members of the public that joined the Zoom meeting were provided opportunity to submit live public comment for each agenda item after the Committee and staff provided their comments.

I. MINUTES APPROVAL

May 30, 2024, Investment Committee Meeting Minutes

Recommendation: Approve the May 30, 2024, Investment Committee Meeting Minutes.

A motion was made by Trustee Williams, seconded by Trustee Balzarini, to approve the minutes of the May 30, 2024, Investment Committee meeting. The motion carried 7-0-0-2 with voting as follows:

Mr. Balzarini	Aye
Mr. Coursey	Absent
Mr. Eaton	Aye
Mr. Jahn	Aye
Mr. Roeser	Aye
Mr. Tambe	Aye
Mr. Walsh	Aye
Mr. Williams	Aye
Mr. Williamson	Absent

II. PRESENTATIONS

Davidson Kempner (DK) – Principal Alexis Georgiadis, presenting in person, and Josh Morris, Partner, Head of Real Estate, presenting via Zoom provided an update on the firm and reviewed the performance of, and holdings in, Special Opportunities Funds (SOF) III and IV in which SCERA invests. Ms. Georgiadis described the firm's partnership structure which they believe results in a strong alignment of interests with clients and ownership stability. The Distressed Investments Team is the largest group and is comprised globally of 112 investment professionals. DK's investment approach focuses on downside protection and preservation of capital while acting upon global opportunistic dislocations in four core investment types, although most of SCERA's remaining investments are in Real Estate.

Mr. Morris provided details on the remaining portfolio holdings in Special Opportunity Fund (SOF) III and IV. SOF III with a value of approximately \$5MM and a 7.7% net IRR since inception, has two unrealized deals. The first is a shopping center REIT that originally held 32 centers and now has 5 properties. The second is a mezzanine loan maturing in February 2025 that was part of the sale of 88 car parks in the U.K. Both investments are estimated to take 4-6 quarters for most or all of the capital to be returned.

SCERA's balance in SOF IV is \$20MM with a near 14% net IRR since inception. The Fund commenced winding down on January 28, 2024. Almost half of the Fund's market value is invested in an Italian loan servicing company, the sale of which is scheduled to close in the third quarter of 2024 and afterward most of the market value will be realized. Around 5% of the market value will remain as a post-closing position which is typical and will naturally liquidate over time. The New York City hotel holding is expected to monetize within 2-6 quarters, while operating income has improved substantially due to a recovery in post-pandemic travel. Regarding the position in the debt of Puerto Rico, a Trustee inquired about any lobbying efforts related to DK's participation in the Fuel Line lending group. Ms. Georgiadis will follow up with additional information to staff. The U.K. Tavern portfolio is expected to be realized over the next 2-6 quarters as 200 of the 361 pubs have been sold above their purchase price. With the U.S. Office Building portfolio, the Fund sold 13 of the original 21 suburban properties, so most of the principal has been repatriated. Subject to market conditions, the eight remaining properties may require 3-6 quarters to sell, and as markdowns have been taken over time, target return expectations have been reduced from 1.7 to 1.2-1.3 MOIC (Multiple On Invested Capital). Mr. Morris commented the outlook for Office valuations continues to face headwinds from massive oversupply very similar to Retail's cycle, and this cycle may persist for 10-15 years.

During the Board's recap, Trustee Jahn approved of the manager's performance but questioned where this type of investment fits in the Plan's asset allocation. CIO Failor noted that DK no longer offers the reduced-fee rollover funds like SOF III and IV. He went on to say that we have discussed the possibility of a higher fee fund coupled with co-investments to reduce the effective average fee but recognized the complexity and risks associated with that option. Some trustees

questioned the opaque nature of the mandate, uncertain timing of realization, and ethics associated with distressed investing. Expectations and the original rationale for including these investments in the Opportunistic Allocation were reviewed. In addition, Aon continues to maintain a positive view of DK. The majority of the Board supported staff's continued dialogue with DK to structure a new assignment that might fit with SCERA's investment program and philosophy.

III. INVESTMENT STAFF AND CONSULTANT

- A. Stock Market Concentration – Investment Officer Mickey Nguyen gave an educational presentation on the topic of concentration in global equity indexes. The persistent trend toward passive investing, particularly in US Equity markets, provides important context, highlighting how dramatically investors have shifted over the past decade away from active managers into index funds. The growing concern is that passive investors are taking on extreme concentration risk in the US markets as measured by the Russell 1000 and S&P 500 indexes due in large part to the “Magnificent 7” technology stock rally. However, looking at longer pre-1970s historical periods reveals high concentration in the US stock market was more common than recent historical data shows; strong earnings and reasonable valuations also provide support for the outperformance of this group; and the 10 largest non-US equity markets currently maintain even greater levels of concentration. Nonetheless the relative outperformance of US large cap stocks versus US small cap stocks is statistically stretched, and prudence would suggest a balanced portfolio structure. SCERA's Plan allocation reflects this counterbalance between active and passive, utilizing partial short extension strategies for optimal flexibility, private market investments with low correlation to public equities, and a modest overweight to small cap/value/high quality factors.
- B. Non-US and Global Equity Manager Search – Chris Behrns, Associate Partner at Aon, provided an update on the search process. Aon has identified 4 Non-US Equity and 5 Global Equity strategies managed across 6 investment firms that would be complementary to SCERA's current equity structure. These candidates were selected from a broad Buy-rated list of 35 Non-US Equity and 50 Global Equity managers. To balance out the Plan's value bias, these managers have a growth bias, and one manages a quantitative strategy. This list will be narrowed down to 2-3 managers for an initial interview, and if those discussions result in a high conviction manager, then they will be brought forward to the Board for deliberation and vote. CIO Failor commented that the Plan's current manager structure is quite strong and that if there is not a manager that both consultant and staff strongly support, they are comfortable with not engaging a new manager.

IV. COMMUNICATIONS

- A. SCERA Investment Performance Report for May 2024. CIO Failor noted that May was a good month for equities with US stocks up almost 5% and non-US stocks up nearly 4%.

US stocks were led by Info. Technology stocks which returned over 9% for the month. US bonds were up 1.7% as the yield curve flattened and yields on spread sectors widened. In this environment, the Plan returned 2.5%, which was in line with the Policy Index.

- B. Wall Street Journal, "Is Vermentino the New Chardonnay?", May 23, 2024.
- C. Pensions & Investments, "Higher interest rates wreaking havoc on real estate managers", June 4, 2024.
- D. Bloomberg, "Sam Altman Was Bending the World to His Will . . .", June 6, 2024.
- E. The Economist, "Ray Kurzweil on how AI will transform the physical world", June 17, 2024.

V. GENERAL DISCUSSION MATTERS

Opportunity was given to advise the Investment Committee of new matters and for Committee members to ask questions for clarification, provide information to staff, request staff to report back on a matter, or direct staff to place a matter on a subsequent agenda.

There were no general discussion matters.

VI. PUBLIC COMMENT

Opportunity was given for public comment on non-agenda items within the jurisdiction of the Investment Committee.

There were no public comments.

VII. NEXT MEETING

The next Investment Committee meeting is scheduled for Thursday, July 25, 2024, at 8:30 a.m. Planned topics for this meeting include a presentation by Arrowstreet. All meetings are held at SCERA in the Board Room at 433 Aviation Boulevard, Suite 100, Santa Rosa, CA, and broadcast via Zoom unless otherwise noted.

VIII. ADJOURNMENT

With no further business to conduct, the meeting adjourned at 11:22 a.m.

IX. APPROVAL

The above minutes of the Investment Committee meeting on June 27, 2024, were approved at the Investment Committee meeting on July 25, 2024.

GREG JAHN, CHAIR