RETIREMENT COMMISSION MINUTES

The Retirement Commission met on Wednesday, December 13, 2023. The following members were present: Chris Cullinan, Jason Vandever, Scott Hendrix, Al Elias, Ben Cullop, Brian Pinkston, David Hughes, Mary Ann Hardie, Tony Newberry, Lindsay Ideson. Absent: Sam Sanders. Others present: Sara Butler, Lisa Burch, Jamie Valencia, Barry Schmitt.

This meeting was held in the CitySpace Large Conference Room.

Call to Order
Jason Vandever called the meeting to order at 8:30 AM.

Approval of Minutes
The minutes from the October 2023 meeting were approved unanimously with Tony Newberry abstaining because he did not attend the October meeting.

Annual CapTrust Review
Barry Schmitt from CapTrust updated the Commission on Secure 2.0 changes and the state of the economy. In addition, he reviewed the investment options for the Defined Contribution plans, and he presented an expense analysis that compared our fees paid to MissionSquare against other employers with similar plan size. According to this analysis, our fees are below the average.

New Business
There was no new business discussed.

Adjournment
The meeting adjourned at 9:14 AM.

Introduction to Private Equity

Greg McNeillie
Kevin Condy, CFA, CAIA
January 24, 2024

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Introduction

- Private equity (PE) funds typically make long-term investments in companies that need managerial or financial help to realize inherent value

- Investors in PE get an entrepreneurial return for an entrepreneurial level of risk

- Advantages include high return and diversification relative to a portfolio dominated by common stocks and bonds

- Disadvantages include high fees, initial decline in value, structural complexity, long lock-ups, and lack of transparency

- Unlike most alternative investments, private equity can require operating skill which varies considerably between managers

What is Private Equity

- PE is defined as the use of private investment capital to make investments in either private or public companies

- Typically, these companies need managerial or financial help to realize inherent value

- Investment can take part at any point in a company's life-cycle, and for a multitude of reasons
    - Capital to start company
    - Operational improvements
    - Financial engineering
    - Perceived mis-valuation

Why Private Equity

Private Equity offers potential return enhancement relative to common equities

Pros	**Cons**
• Greater Appreciation Potential	• Vintage Year Risk
• Lower Short-term Volatility	• Illiquidity
• Portfolio Diversification	• Fees
	• Administrative Burden

Portfolio Role

- May provide higher return than public equity
- Reduces portfolio volatility
- Diversify return stream

Life of Private Equity Fund

The fund begins to make investments. The investment period is defined in the Private Placement Memorandum

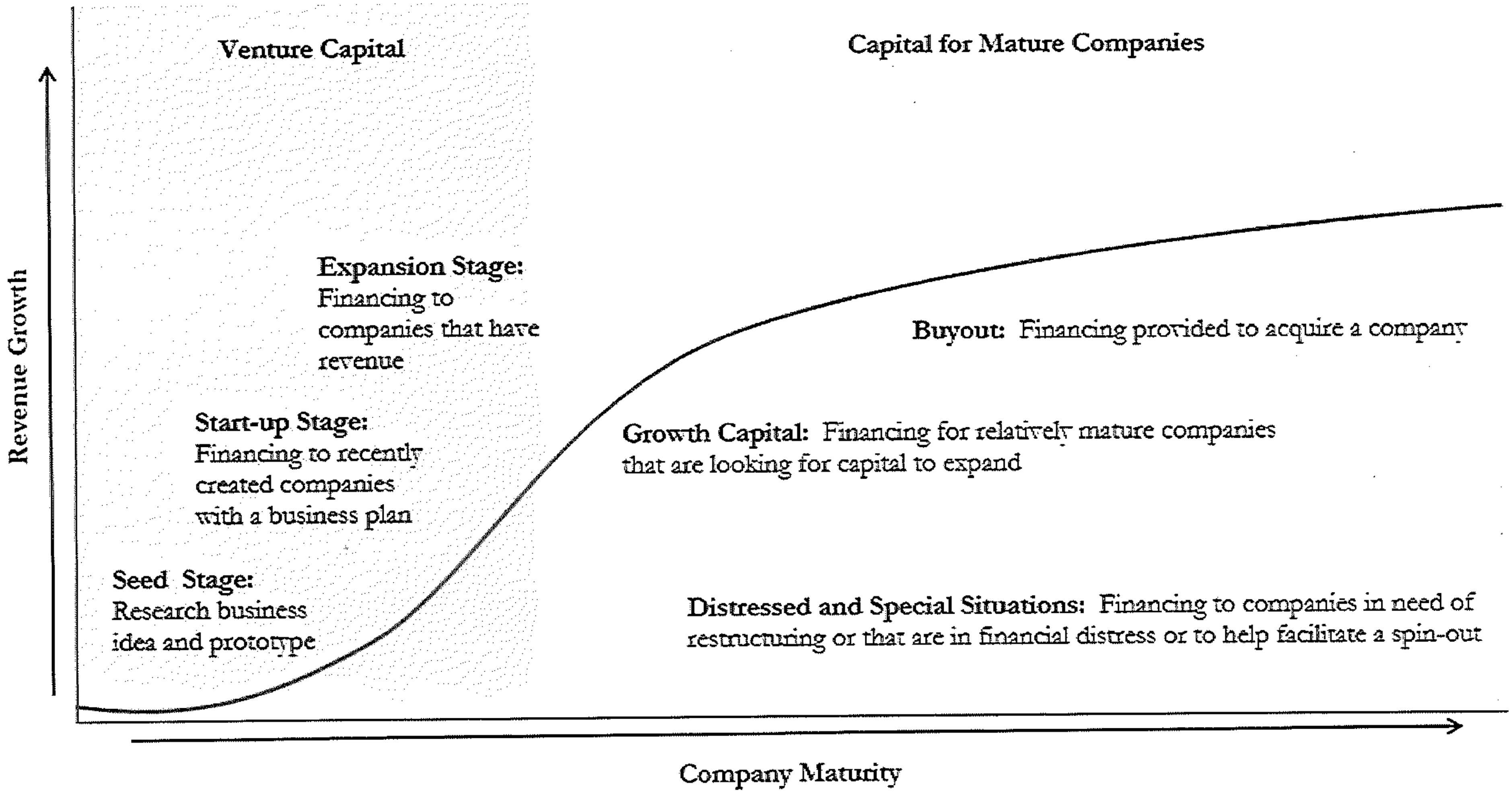
Fund managers implement their strategy. Some additional capital calls can be expected. Liquidations and distributions accelerate as the fund matures.

Year 1		Year 3		Year 5		Year 7		Year 9		Year 11	Year 12
Investment Period			**Realization and Exit Period**							**Extension Period**	

Capital calls are issued to the Limited Partners. Capital calls can last beyond the investment period

Limited extensions to the fund term. Usually 2-years at the discretion of the fund

Investment Styles



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Investment Styles

Venture Capital (Seed /Startup)

- Invests in young companies in the early stages of development
- Injects money and managerial expertise
- High risk, high return strategy
- Example: early investment in Facebook

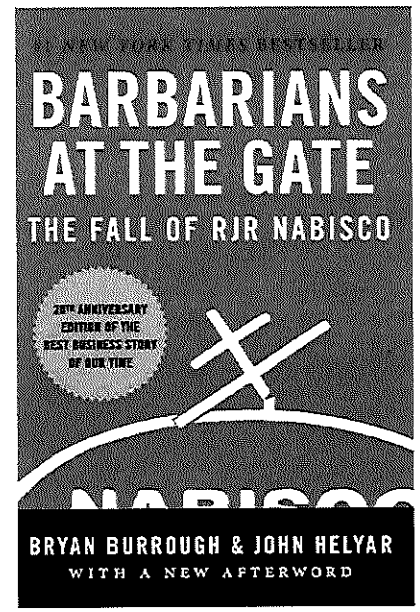
Growth Equity

- Invests in more established companies
- Companies generally have an established business and are looking to expand
- Offers a lower risk/return than Venture Capital
- Example: additional funding for later stage investment in Facebook

Investment Styles

<u>Buyout (Leveraged Buyout)</u>

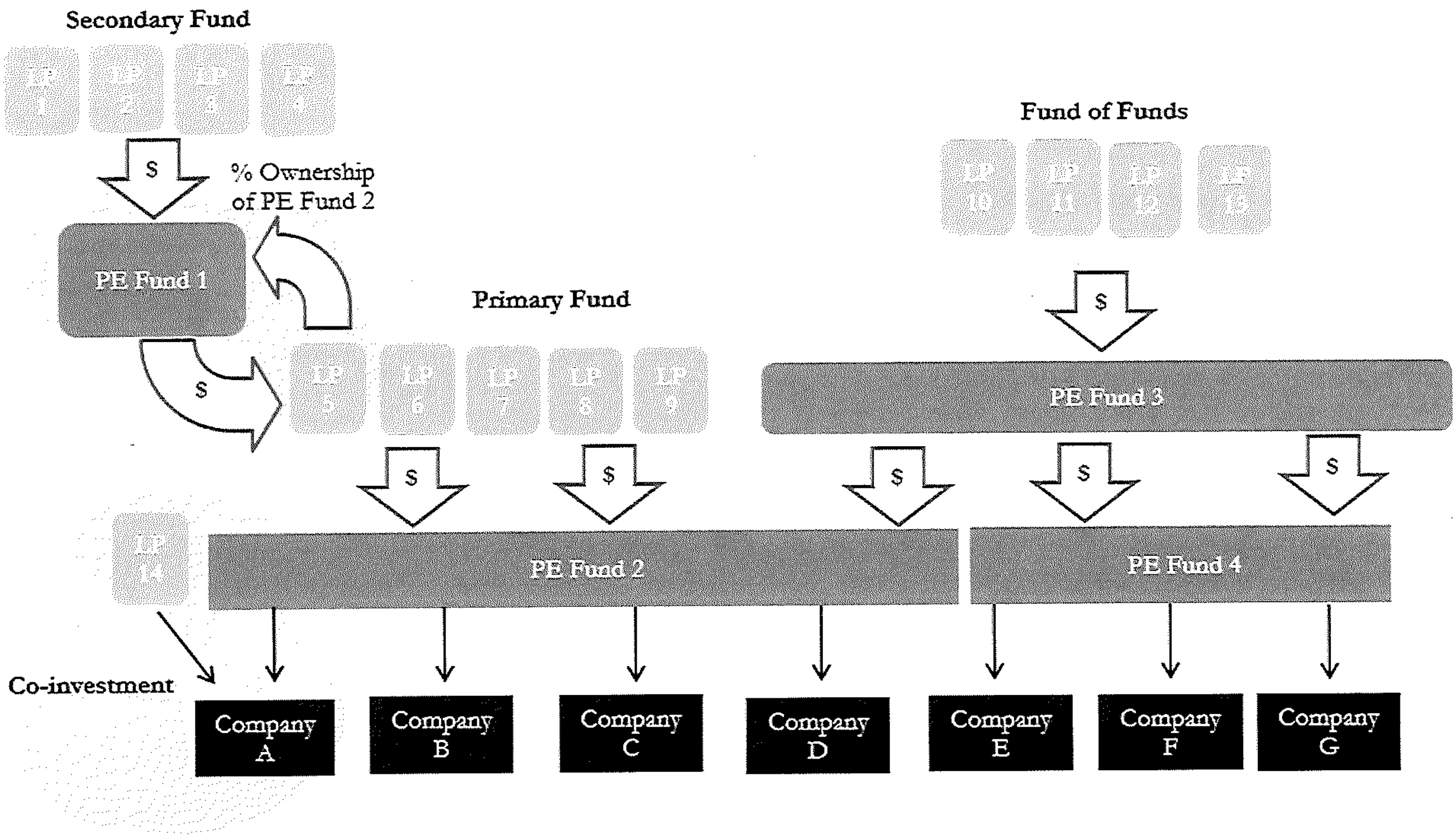
- Invests in mature companies looking to restructure, expand, or be taken private
- Leverage is often used to increase returns
- Offers a lower risk/return than venture capital
- Examples:
  - In 2007, the Blackstone Group acquired all publicly traded shares of Hilton Hotels and took the company private.
  - In 2016, BC Partners took PetSmart private and returned 40% in cash dividends within a year



<u>Distressed and Special Situations</u>

- A broad category referring to investments in equity or debt
- Invests in financially stressed companies
- High risk, high return strategy
- Example: Investing in a company that has filed for bankruptcy

Investment Vehicles Flow Chart



LP = Limited Partner (Investor)

Investment Vehicles

Primary

- Commit capital to a fund manager, or General Partner (GP) who directly invests in the underlying companies
- Funds focused on investment style, business sector, and/or region

Secondary

- The purchase of a Private Equity fund interest from another investor
- Produce earlier cash flows and shorter pay-back period

Fund-of-Funds

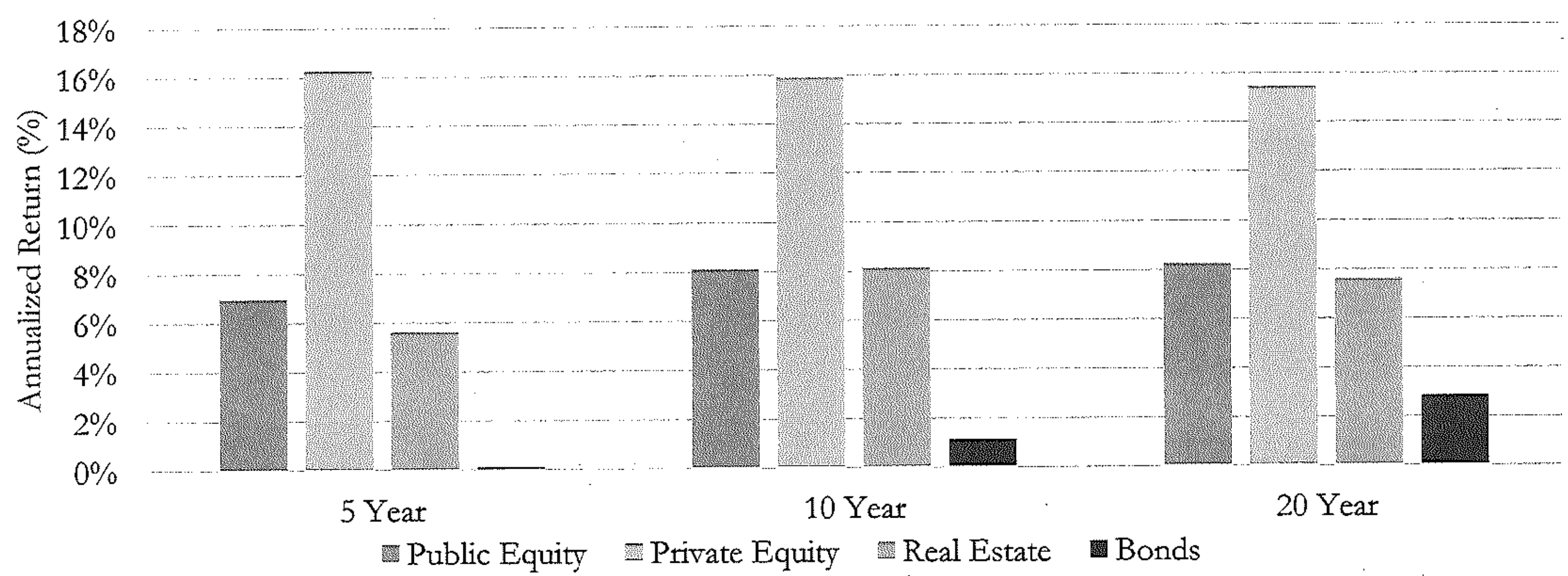
- A fund consisting of investments in Private Equity funds, with multiple strategies
- High level of diversification
- Additional layer of fees

Co-investment

- Investment in company alongside a private equity fund manager
- Investors can potentially get into a profitable investment without paying the usual fees changed by a private equity fund
- Lower level of diversification

Historical Returns

- PE does not meet the academic definition of an asset class. We use this terminology for convenience
- PE returned 15% over the last 20 years, with a correlation to domestic large cap equity of 0.8
- Return has been the highest among major asset classes



Returns as of 9/30/23
Public Equity = MSCI All Country, Private Equity = Cambridge Private Equity, Real Estate = NCREIF ODCE, Bonds = Bloomberg Barclays Aggregate

Return Statistics – 20 Years

Asset Class	Index	Return	Standard Deviation
Large Cap Core	S&P 500	9.7	15.8
Fixed Income	Bloomberg Aggregate	2.8	4.1
Small Cap Core	Russell 2000	8.1	20.8
International Equity	MSCI EAFE	6.4	18.3
Emerging Markets	MSCI Emerging Markets	7.7	21.9
Timber	NCREIF Timber	7.0	4.5
Farmland	NCREIF Farmland	12.6	6.9
Real Estate	NCREIF ODCE	7.6	7.2
Hedge Funds	Dow Jones Tremont	5.3	6.5
Private Equity	Cambridge PE	15.0	9.6

As of 9/30/23

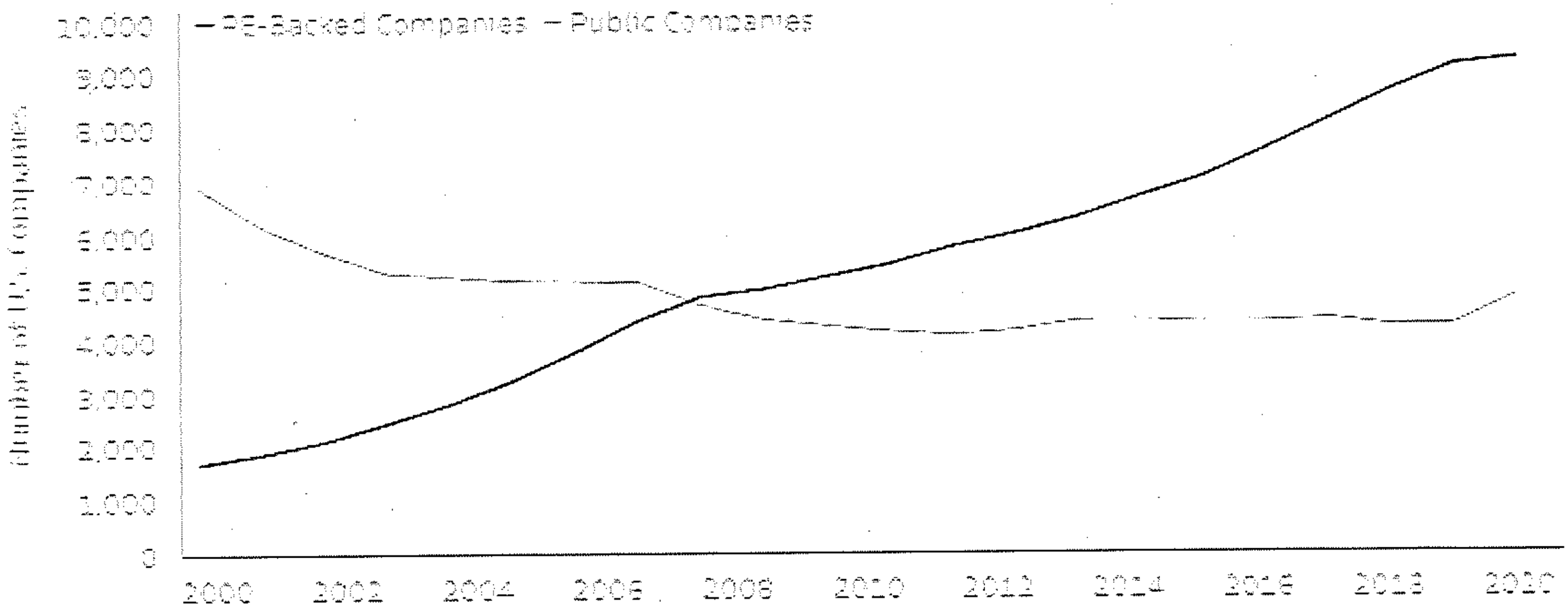
Correlation – 20 Years

Index Name	Asset Class	LC	FI	SC	Int'l	EM	TIM	FARM	RE	HF	PE
S&P 500	Large Cap	1.0	0.0	0.9	0.9	0.8	-0.1	0.1	0.1	0.8	0.8
Bloomberg Aggregate	Fixed Income	0.0	1.0	-0.1	0.1	0.1	0.0	0.0	-0.2	-0.1	-0.1
Russell 2000	Small Cap	0.9	-0.1	1.0	0.9	0.7	-0.1	0.1	0.0	0.8	0.8
MSCI EAFE	International	0.9	0.1	0.9	1.0	0.9	0.0	0.1	0.0	0.8	0.7
MSCI Emerging Markets	Emerging Markets	0.8	0.1	0.7	0.9	1.0	0.0	0.1	0.0	0.9	0.7
NCREIF Timber	Timberland	-0.1	0.0	-0.1	0.0	0.0	1.0	0.7	0.2	0.0	0.1
NCREIF Farmland	Farmland	0.1	0.0	0.1	0.1	0.1	0.7	1.0	0.1	0.1	0.2
NCREIF ODCE	Real Estate	0.1	-0.2	0.0	0.0	0.0	0.2	0.1	1.0	0.1	0.3
Dow Jones Tremont	Hedge Funds	0.8	-0.1	0.8	0.8	0.9	0.0	0.1	0.1	1.0	0.8
Cambridge PE	Private Equity	0.8	-0.1	0.8	0.7	0.7	0.1	0.2	0.3	0.8	1.0

As of 9/30/23

The Increasing Prevalence of Private Equity

The universe of PE-backed companies has grown while the universe of public companies has shrunk



Source: PitchBook as of 6/30/2021. Public companies over time: World Bank, McKinsey.

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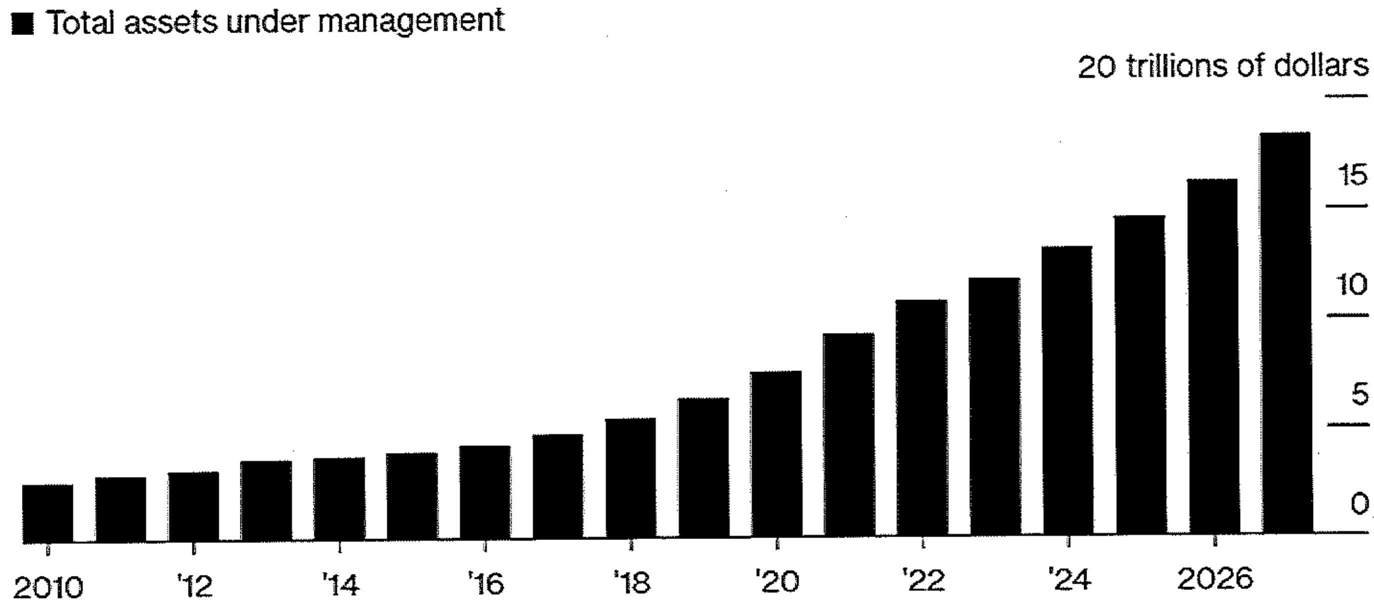
Private Equity Allocations Projected to Grow

- Growth across alternative assets has been strong over the past 10 years, driven by the success of private equity funds in generating returns and raising capital
- Assets under management has grown by 20% annually (CAGR) from 2017-2022[1]
- Assets under management reached $11.7T as of June 30, 2022[1]



Source: Preqin
2022-2027 are projected figures

[1]McKinsey Global Private Market Review 2023: Private markets turn down the volume

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Disadvantages

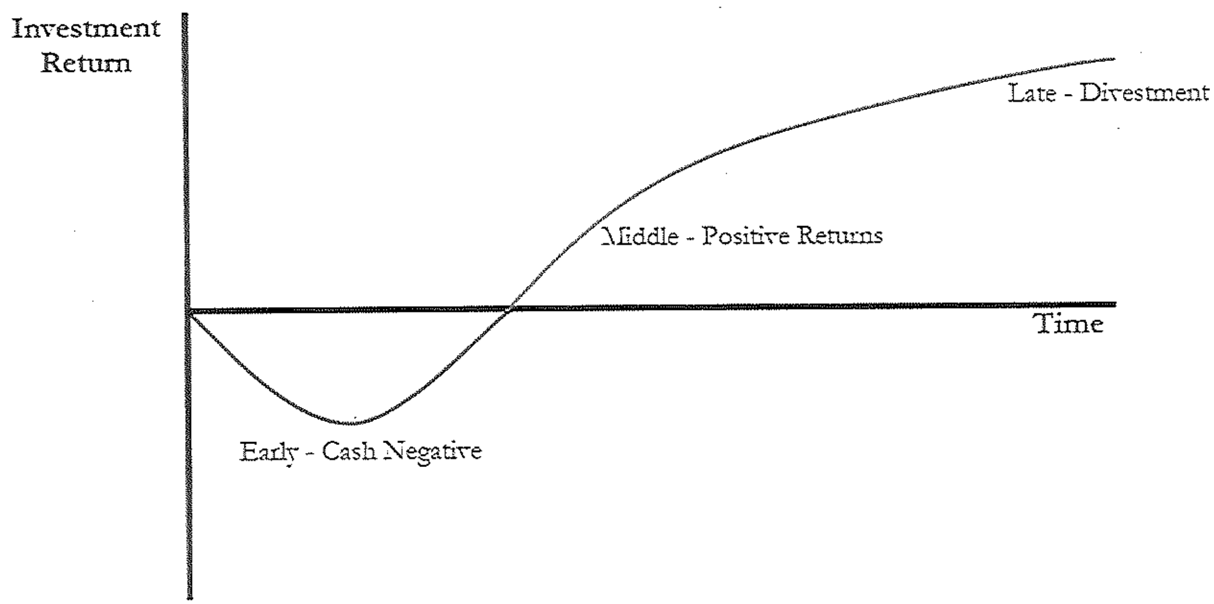
- The return and diversity benefits of private equity are not free
- Disadvantages are many and varied
- We discuss the pitfalls of private equity by grouping them into six common problems
  1. The Structure Problem (complex legal agreement and fees)
  2. The J Curve Problem (tendency for value to decline in early years)
  3. The Vintage Year Problem (return disparity due to timing)
  4. The Access Problem (difficulty of investing with best managers)
  5. The Diversity Problem (need for diversity due to hit or miss nature)
  6. The Measurement Problem (the comparison to public markets)

1) The Structure Problem

- Investing in PE involves the use of a complex limited partnership agreement
- The PE firm is the general partner sometimes called the management company; investors are limited partners, referred to in aggregate as the Fund
- Long lock-up periods of 5-12 years are mandatory, sometimes with extensions at the discretion of the general partner
- The prospectus usually places the limited partners at a legal disadvantage, particularly in indemnifying the general partner

2) The J-Curve Problem

- The early-year decline in value of a PE investment is commonly referred to as the "J Curve"
- Investment managers typically charge fees on committed capital prior to making investments, rather than called capital
- Investments are typically held at cost in the early years of the fund as the manager needs time to implement their plan

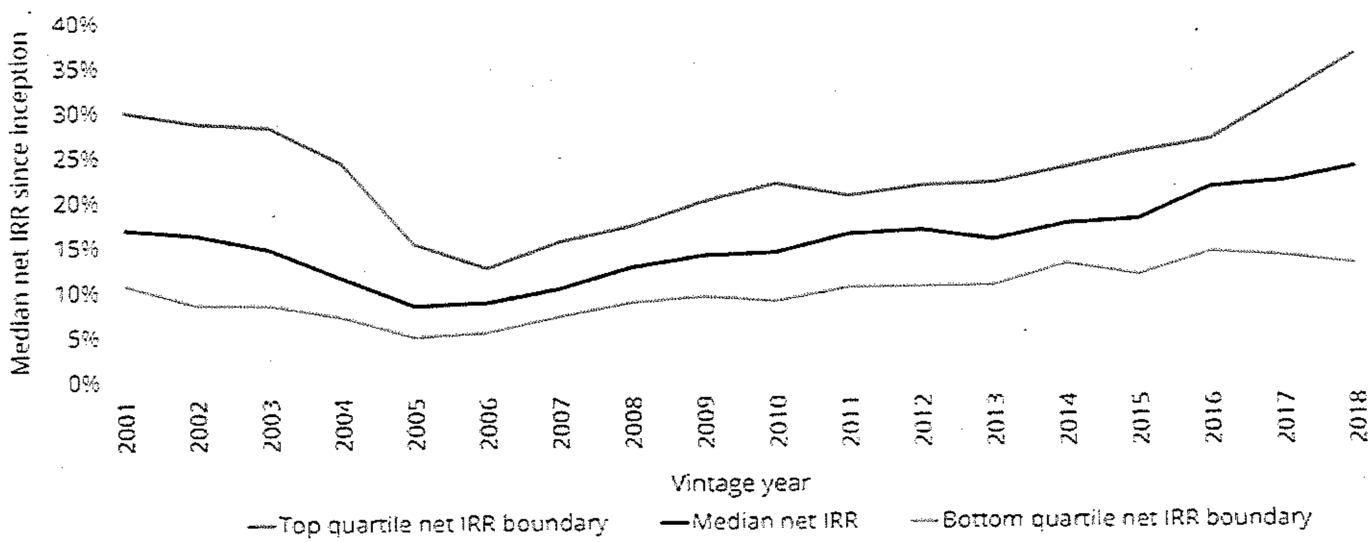


3) The Vintage Year Problem

- Like wine, investing has good years and bad years
- PE capital is committed to new ventures during a 1-3 year period at the start of the fund
- Fund performance is thereafter influenced by the investment environment that characterizes those years
- A fund with bad vintage years can underperform a fund with good vintage years, even if it is otherwise better managed

4) The Access Problem

- Private Equity depends on operating knowledge, relationships, skill and ability, which all financial professionals do not possess in equal amounts
- Managers with good track records are oversubscribed and usually closed to new investors, as the extent to put capital to work is limited
- There is perhaps more return variance between Private Equity managers than in any other asset class. Manager selection is therefore critical



Source: Preqin Pro

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5) The Diversity Problem

- A PE manager seeks the same benefits from diversification as a stock portfolio manager
- A PE portfolio may be diversified by time (vintage years), investment style, investment stage, industry and geography
- Because of timing and limits on personnel skill/experience, most funds are limited in the degree of diversity that they can achieve
- The fund of funds approach significantly increases diversity, and has two key advantages that no individual fund can offer:
  - Diversification across managers
  - Access to managers otherwise closed to new/smaller investors
  - However, a fund-of-funds manager adds another layer of fees

6) The Measurement Problem

- Measurement of Performance, Standard Deviation, Correlation:
  - Significantly impacted by timing of cash flows
  - Difficult to benchmark effectively
  - Multiple performance metrics (IRR, TVPI, DPI, MOIC, etc.)
  - Valuation dates

- Comparing Apples to Oranges to Onions

- Who is doing the valuations? When are they doing it?

Summary

- Private equity has offered, on average, the highest long-term return among the major asset classes
- Complexity of the investment structure, illiquidity, variability of returns among managers and high fees have limited the use of private equities in smaller and midsized funds
- Problems in comparison with traditional asset classes causes problems in assessment and benchmarking
- Private Equity can be complementary to many portfolios, but issues need to be recognized and considered before allocating