



ALAMEDA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

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Date: March 11, 2015
To: Members of the Board of Retirement
From: George Wood – Chair
Subject: Summary of the March 11, 2015 Investment Committee Meeting

The Investment Committee met on Wednesday, March 11, 2015 at 9:37 a.m. The Committee members present were Dale Amaral, Keith Carson, Tarrell Gamble, Liz Koppenhaver, Elizabeth Rogers, Donald White, and George Wood. Also present was Alternate Safety member Darryl Walker. Members of the Staff present were, Kathy Foster – Interim Chief Executive Officer, Margo Allen – Fiscal Services Officer, Joseph Fletcher – Chief Counsel, Harsh Jadhav – Chief of Internal Audit, and Betty Tse – Chief Investment Officer.

ACTION ITEM

1. Interview of Three Real Estate Investment Consultants included in the Short List of Candidates for ACERA's Real Estate Investment Consultant Search and Possible Motion by the Investment Committee to Recommend one Finalist to the Board
- In January, the Board of Retirement approved a motion to select Callan Associates (Callan), Courtland Partners, Ltd. (Courtland), and The Townsend Group (Townsend) as the short-listed candidates for ACERA's Real Estate Investment Consultant Search. After the on-site due diligence conducted last month, Staff and SIS still consider Callan, Courtland and Townsend as the top three candidates and have recommended them to the Investment Committee for consideration as finalists in this Real Estate Investment Consultant Search.

The following are highlights from each of the three finalists' presentations and their responses to the Committee's questions:

Callan

The Representatives from Callan were Jim Callahan, Avery Robinson, Lauren Sertich, and Jamie Shen. The following is a summary of their presentations and responses:

- Callan is a 100% employee-owned firm with 75 current owner-employees (Callan has about 180 employees), including all members of the team proposed for ACERA. General Investment Consulting is Callan's primary focus with over 360 clients representing \$2 trillion in assets, including \$34.6 billion in real estate assets.
- Callan's structure allows it to attract and retain skilled professionals, allowing Callan the opportunity to be selective. There have been no disruptions in the real assets consulting team in the last 6 years.
- The Real Assets Group is an important division within Callan to which the firm is committed. Over time, Callan has consistently added resources to the group and will continue to do so, as needed.

- Callan stated that the real estate consulting group does not have any conflicts of interest and that its entire real estate advisory consulting business is non-discretionary. Callan does not have, and is not planning to have, a discretionary real estate consulting business.
- Callan has a collaborative culture and supports “diversity” throughout the company. Callan stated it has the resources, breadth of research capabilities, and dedicated personnel to advise ACERA.
- Callan selected Mr. Robinson because Callan thought he would be a good fit for the ACERA portfolio, since he is the open-end product research lead. Mr. Robinson has 2 full advisory service clients, which are the Marin County Employees’ Retirement Association and the Illinois Municipal Retirement Fund (IMRF). Mr. Robinson worked with IMRF to grow its portfolio from \$400 million to over \$1.4 billion through returns and increases to its real estate allocation.
- Mr. Robinson would represent ACERA at the Investment Committee meetings and would be supported by Ms. Shen and/or Ms. Sertich. As leader of the Real Assets Team, Ms. Shen would provide strategy and structure, and Ms. Sertich would be responsible for reporting and performance measurement. Callan has four additional real estate professionals who would work with ACERA. Accordingly, Callan customizes its recommendations and advises its clients based on their needs.
- Education and research are important components of what is offered to clients, including research from all of Callan’s consulting practices.
- Callan shared its market overview and seeks to advise clients not to make the same mistakes made in 2007 when real estate prices were overvalued.
- Callan shared its observations on ACERA’s portfolio. The representatives stated that the real estate target of 6% is low in comparison to other funds, making manager selection more important. Callan suggested that going forward, the real estate cycle has about 2 more years to run, and that it would consider positioning ACERA’s portfolio to invest in global areas that are lagging the U.S. as it relates to the real estate cycle, like Europe, or look to real assets, such as infrastructure, agriculture and timber.
- Callan discussed its fiduciary role, its Ethics Policies and Procedures, and its philosophy of putting client interests first. Callan would contact ACERA immediately if there was ever a breach of contract.
- Callan stated that clients have full access to all of its research and white papers; they reiterated its (1) independence, (2) experience, (3) resources, and (4) custom solutions and innovation.

Courtland

The Representatives from Courtland were Michael Humphrey, Stanley Kim, Robert Negrelli, and Jack Novatney. The following is a summary of their presentations and responses:

- Courtland is an employee-owned firm –focused exclusively on real estate investment consulting. The company is owned 100% by two individuals; Michael Humphrey owns 90% and Steve Novick owns 10% of the firm.
- Mr. Humphrey was one of three founders of Courtland in 1995 and the firm has 30 institutional clients with a total of \$50 billion of assets under advisement, \$1.5 billion of

which is discretionary assets. Currently 20 - 25% of Courtland's revenue is from discretionary clients.

- Since 2000, Courtland has recommended investment commitments to over \$70 billion in real estate investment opportunities with over 40% invested in international investments.
- Mr. Humphrey described Courtland's experience and evolving business platform. Courtland's Staff members will always be fiduciaries first. Courtland has 30 employees and is headquartered in Cleveland, Ohio. It has additional offices in Los Angeles, San Francisco, Seattle, New York, Philadelphia, and London.
- Mr. Humphrey explained that Courtland needs to build its platform, either through relationships (partnership) with other firms or by building relationships internally through partners. The goal is to build a presence in international locations, with a deeper presence in Europe and office locations in Asia and Latin America. Control of the company will not change. Any new investor will be a minority investor in the firm.
- Regarding succession planning, there are younger people within Courtland that have been with the firm for several years and are taking on more senior responsibilities. The succession plan is for Mr. Humphrey to back out of the "in the trenches" role and for others to step up and take on more responsibilities, but Mr. Humphrey is not planning on stepping down anytime soon.
- In reviewing ACERA's portfolio, Courtland would like to consider international and debt investments, as well as, other real assets. Some of Courtland's top value managers are not in ACERA's portfolio.
- Courtland runs a model portfolio for each client. It would look at the model and ask if any of the assumptions have changed (e.g. has the average asset size changed?). Courtland provides recommendations based on each client's needs.
- Courtland incentivizes its employees through salaries and bonuses, and is looking at ways to increase employee ownership and expand resources in the firm. Courtland has had recent turnover in the team (one analyst is leaving to go to a real estate fund), and it expects turnover to continue sporadically in the future.
- Courtland discussed its fiduciary role, its Code of Ethics policy (which must be read and signed by every employee), which requires putting client interests first. If there were ever a breach of contract, Courtland would notify ACERA immediately.
- Courtland's view of the real estate market is that it is getting frothy, that the cycle is getting long in the tooth and that investors need to be aware of that. Courtland recommended being very selective, understanding the managers that a fund is invested in, and making sure value managers are focused on income.
- Courtland thinks its fee is fair given the work it expects to perform for ACERA.

Townsend

The Representatives from Townsend were Terry Ahern, Prashant Tewari, Jennifer Young, and John Schaeffer. The following is a summary of their presentations and responses:

- Townsend has grown institutionally, offering both non-discretionary and discretionary advice services as the real estate market has become more global. It has \$160 billion in non-discretionary assets under advisement. Townsend is the largest real-estate focused

- consultant as measured by number of clients, number of employees (105), dedicated research capabilities, and global footprint (London-12, Hong Kong-5).
- Across its platform, Townsend works collaboratively and has a team culture, plus it has developed many specialized business operations and investment processes.
 - Ms. Young spoke to Townsend's three main business practices: (1) strategic planning and asset allocation, (2) manager and fund selection, and (3) advocacy and oversight for each of its clients.
 - Because of its size and large clients, Townsend is able to help negotiate significantly reduced investment fees and cited three funds that have been accretive to returns in which ACERA has invested, namely, Jamestown Premier Property Fund, MetLife Property Fund, and CIM Fund IV (Urban REIT).
 - Townsend sits as a member on many Advisory Boards, and can influence terms in the underwriting process. Ms. Young provided specific examples within ACERA's portfolio and referenced how ACERA's portfolio has grown to over 1,600 individual real estate assets and is diversified by property type and geography. Townsend pointed out that ACERA's portfolio has outperformed the ODCE over the past 1, 3, and 5 years during Townsend's tenure.
 - Mr. Tewari provided the Committee with insight to the Global Macro Strategy group, its macro vision, and how the group operates. As an example, coming out of the financial crisis the group suggested clients would do better with equity ownership versus debt.
 - Mr. Ahern spoke to (1) Townsend's people, (2) evolution of the asset class, and (3) insights on how Townsend operates. Townsend looks for intellectually curious people who can work collaboratively, a "We", not an "I" culture, and a flat management structure. Townsend places a high value on creativity, value creation, and is merit based. The real estate asset class has gone from a controlled market with little data available to investors to a global asset class in both the public and private markets. Townsend strategically and purposefully evolved with this rapid change, including expanding its practice of discretionary management. The latter has greatly increased its resources and created synergies across Townsend's platforms. Townsend has a competitive advantage given its size and resources.
 - Mr. Ahern spoke to the "potential conflicts of interest" and to the advantages to clients within both non-discretionary, as well as, discretionary relationships with Townsend. Townsend has a Code of Ethics, and a Policy Regarding Conflicts of Interest. Townsend has a formal Compliance Department and a Compliance Officer with staff to support it. If any conflict should arise, such as a violation of these policies or a breach of its consulting contract, Townsend would advise the Board of Trustees.
 - Townsend, like the others, suggested that as the real estate markets mature in its cycle, ACERA may want to begin (1) increasing its allocation to real estate (6% to 10%), (2) begin to emphasize value-add opportunities while changing the Core/Value-add weightings, and (3) consider international opportunities, e.g., Europe.
- At the conclusion of the three presentations, and after discussion, Mr. Donald White moved, seconded by Mr. Tarrell Gamble, to recommend Callan to the full Board as ACERA's Real Estate Investment Consultant.
 - The motion did not pass with 3 yes (Amaral, Gamble, and White), 3 no (Koppenhaver, Rogers, and Wood), and 0 abstention.

- The matter will be included as an Action Item on the March 19, 2015 Board agenda.

INFORMATION ITEMS

1. Quarterly Performance Review for the Fourth Quarter of 2014 – Equities, Fixed Income, and Real Return Pool

- For the fourth quarter, ACERA's Total Fund returned 1.4% (gross) compared to the policy index of 1.7% and, for the year 2014, returned 4.7% (gross) compared to the policy index of 6.6%. The Total Fund ranked in the 48th and 78th percentile for the quarter and year, respectively.
- For the quarter, ACERA's U.S. equity, international equity, fixed income, and Real Return Pool asset classes returned 5.9%, -2.9%, 1.2%, and -9.7% (gross) compared to their benchmarks 5.2 (Russell 3000 index), -3.8% (MSCI ACWI ex USA IMI), 0.8% (75% Barclays Aggregate 10% Barclays High Yield and 15% Citigroup WGBI ex US), and 0.6% (CPI-U Core+3%), respectively. On a 12-month trailing (gross) basis, U.S. Equities returned 9.5% (80th percentile), International Equity -3.9% (62nd percentile), Fixed Income 7.6% (25th percentile), and Real Return Pool -13.5%.
- As of 12/31/14, the market value of the total Fund was \$6,779,956.556.

2. Quarterly Performance Review for the Fourth Quarter of 2014 – Real Estate

- ACERA's real estate portfolio had gross returns of 2.7% (67th percentile) for Q4 2014 and 12.4% (55th percentile) for the latest one year period compared to the NCREIF-ODCE benchmark of 3.3% and 12.5%, respectively.
- As of 12/31/14, the total market value of ACERA's real estate portfolio was about \$446.8 million; approximately 6.6% of ACERA's Total Fund.

Recommendation

None

TRUSTEE/PUBLIC INPUT

FUTURE DISCUSSION ITEMS

None

ESTABLISHMENT OF NEXT MEETING DATE

April 8, 2015 at 9:30 a.m.

Adjournment into Closed Session pursuant to California Government Code section 54956.81

1. Due Diligence Update on Lighthouse Strategic Alpha Fund, LLC --Conference with Legal Counsel, Investment Staff and SIS.

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**RECONVENE INTO OPEN SESSION TO REPORT ANY ACTION TAKEN IN
CLOSED EXECUTIVE SESSION**

The Committee reconvened into Open Session and announced that no action had been taken during closed session.

ADJOURNMENT

The meeting adjourned at 1:25 p.m.