

May 20, 2024

Board of Retirement
Ventura County Employees' Retirement Association
1190 South Victoria Avenue, Suite 200
Ventura, CA 93003

SUBJECT: Asset Allocation Recommendations

Recommendation

Staff and NEPC recommend that the Board adopt the proposed asset allocation targets, ranges and benchmarks as recommended in Exhibit A.

Discussion

Asset allocation is both the biggest and the most consequential decision a prudent investor makes, as it is the main driver of investment portfolio risk and return. At the February meeting the Board took its initial step in a three-step asset allocation process with its review and consideration of NEPC's Capital Market Assumptions.

The second step taken by the Board in the asset allocation process was consideration of an asset-liability study conducted by NEPC at its April meeting. The study integrated actuarial data provided by VCERA's actuary Segal with the NEPC Capital Markets Assumptions discussed by the Board at its February meeting. The study incorporated objectives over both 10- and 30- year horizons, and the study's outcome serves as the framework for the third and final step in the process- your ultimate asset allocation decision.

Attached for your consideration as Exhibit A is a recommended Asset Allocation matrix containing targets, ranges, and benchmarks. The recommended changes from the current policy:

1. reduce the non-U.S. publicly traded equities target from 15% to 13%.
2. increase the private credit (debt) target from 8% to 10%.
3. maintain the current 8% real estate target, but within real estate, reduces the core real estate target from 6% to 4%, while increasing the non-core real estate target from 2% to 4%.
4. Revise ranges to be symmetrical around the asset class targets at +/- 4% around U.S. Equity, Non-U.S. equity, Global Equity; and Private Equity; +/- 3% around Real Assets.
5. Revise the benchmark for private credit to the more applicable CS Leveraged Loan + 2%.
6. Use one quarter lagged returns for the Private Equity and Private Credit benchmarks as portfolio valuation financial reports lag by at least a quarter.

Displayed in this memo as Exhibit B, and as slide 23 of 36 in the NEPC Asset Liability Study presentation deck dated April 29, 2024, is a granular breakdown of comparisons of the Current Policy **target** allocations; the **actual** allocations as of 3/31/2024, and the **recommended** target allocations, together with relevant metrics.

Staff and NEPC are recommending only modest asset allocation changes as they maintain the same expected 10-year rate of return while marginally increasing the 30-year expected return by 10 basis points relative to the current asset allocation targets. The level of volatility is expected to remain the same with this new mix as well, however the Fund's expected risk-adjusted performance as measured by the Sharpe Ratio is expected to marginally improve.

The modestly higher allocation to Private Credit (Debt), funded from non-U.S. equity, increases the likelihood of manager outperformance (alpha) through the selection of outperforming managers. VCERA has added value through approving opportunistic strategies that have provided strong net-of-fee returns while mitigating the effect of the J-curve.

We expect the proposed target asset allocation changes to be actualized over three to five years to account for the illiquid nature of private markets assets and to ensure vintage year diversification.

Exhibit C is the current asset allocation mix, adopted by the Board at its meeting on April 18, 2022.

Exhibit D contains definitions of metrics used to benchmark the respective asset classes. Under separate cover is NEPC's 2024 Asset Allocation presentation deck.

As discussed above and noted further in the NEPC Asset Allocation presentation deck, NEPC and I believe that the current asset allocation targets as modified with only minor recommended changes will better position VCERA to meet its long-term obligations.

RECOMMENDED: THAT THE BOARD APPROVE THE ASSET ALLOCATION RECOMMENDATIONS MIX, RANGES, AND BENCHMARKS AS PRESENTED IN THE ATTACHED EXHIBIT A.

Respectfully submitted,



Dan Gallagher
Chief Investment Officer

Attachments

Exhibit A: **Asset Allocation Recommendation- May 20, 2024 Board Meeting**

Exhibit B: from Asset-Liability Study: **ASSET ALLOCATION PROFILES**
Current Policy Targets vs Actual vs Recommended

Exhibit C: **Prior Aset Allocation Mix as of April 18, 2022**

Exhibit D: **Index / Benchmarks Definitions**

Exhibit A
Asset Allocation Recommendation- May 20, 2024 Board Meeting

<u>Asset Classs</u>	<u>Targets</u>	<u>Ranges</u>	<u>Benchmarks</u>
<i>Equity</i>			
U.S. Equity	26%	22% -- 30%	Russell 3000
Non-U.S. Equity	13%	9% -- 17%	MSCI ACWI ex U.S. Index Net
Global Equity	9%	5% -- 13%	MSCI ACWI Index Net
Private Equity	18%	14% -- 22%	Russell 3000 + 2% (lagged by 1 quarter)
<i>Debt</i>			
Publicly Traded Fixed Income	10%	7% -- 13%	Bloomberg Barclays Aggregate Bonds Index
Private Credit	10%	6% -- 14%	CS Leveraged Loan + 2% (lagged by 1 quarter)
<i>Real Assets</i>			
Real Assets	6%	3% -- 9%	CPI + 2%
Real Estate	8%	5% -- 11%	NCREIF ODCE Index
<i>Cash</i>	0%	0% -- 3%	90 Day T-Bills

Exhibit B

ASSET ALLOCATION PROFILES

Current Policy Targets vs Actual vs Recommended

	Current Policy	Actual Allocation as of 3/31/2024	Recommended
Cash	0.0%	0.7%	0.0%
Total Cash	0.0%	0.7%	0.0%
US Large-Cap Equity	22.4%	27.1%	24.0%
US Small/Mid-Cap Equity	3.6%	1.3%	2.0%
Non-US Developed Equity	10.8%	11.8%	10.0%
Emerging Market Equity	4.3%	3.0%	3.0%
Global Equity	9.0%	10.1%	9.0%
Private Equity	18.0%	17.7%	18.0%
Total Equity	68.0%	71.0%	66.0%
US Aggregate Bond	4.0%	4.4%	4.0%
Absolute Return Fixed Income	4.0%	4.4%	4.0%
Private Debt	8.0%	7.5%	10.0%
10 Year US Treasury Bond	2.0%	0.9%	2.0%
Total Fixed Income	18.0%	17.2%	20.0%
Real Estate - Core	6.0%	4.8%	4.0%
Real Estate - Non-Core	2.0%	1.3%	4.0%
Private Real Assets - Natural Resources	2.0%	2.5%	2.0%
Private Real Assets - Infrastructure	4.0%	2.5%	4.0%
Total Real Assets	14.0%	11.1%	14.0%
Expected Return - 10 Year	6.7%	6.5%	6.7%
Expected Return - 30 Year	8.0%	7.9%	8.1%
Asset Volatility	15.9%	16.0%	15.9%
Sharpe Ratio - 10 Year	0.17	0.16	0.18
Sharpe Ratio - 30 Year	0.29	0.28	0.30

Notes: Shaded regions reflect changes relative to Current Policy allocation



ASSET-LIABILITY STUDY- slide page 23; VCERA Board meeting April 29, 2024
Rob Goldthorpe, ASA, Investment Director
Rose Dean, CFA, Partner

Exhibit C
Prior Aset Allocation Mix as of April 18, 2022

<u>Asset Classs</u>	<u>Targets</u>	<u>Ranges</u>	<u>Benchmarks</u>
<i>Equity</i>			
U.S. Equity	26%	20% -- 32%	Russell 3000
Non-U.S. Equity	15%	12% -- 20%	MSCI ACWI ex U.S. Index Net
Global Equity	9%	7% -- 13%	MSCI ACWI Index Net
Private Equity	18%	14% -- 22%	Russell 3000 + 2%
<i>Debt</i>			
Publicly Traded Fixed Income	10%	7% -- 13%	Bloomberg Barclays Aggregate Bonds Index
Private Credit	8%	4% -- 12%	50% CS Leveraged Loan / 50% ICE BofA US HY BBB Rated Constrained Index
<i>Real Assets</i>			
Real Assets	6%	4% -- 8%	CPI + 2%
Real Estate	8%	5% -- 11%	NCREIF ODCE Index
<i>Cash</i>	0%	0% -- 3%	90 Day T-Bills

Exhibit D

Index / Benchmarks Definitions

Russell 3000 Index: The Russell 3000 comprises the 3000 largest U.S. companies by market cap. The Russell 3000 Index represents approximately 99% of the U.S. equity market. This index is rebalanced once annually in June.

MSCI ACWI Ex US Index: The MSCI ACWI ex. U.S. Index is a free float-adjusted market capitalization-weighted index that is designed to measure the combined equity market performance of developed and emerging markets (excluding the U.S.). The MSCI ACWI captures large and mid-cap representation across 22 Developed Markets and 24 Emerging Markets countries.

MSCI ACWI Index Net: The MSCI All Country World Index is a free float-adjusted market capitalization-weighted index that is designed to measure the combined equity market performance of developed and emerging markets (including the U.S.). The MSCI ACWI captures large and mid-cap representation across 23 Developed Markets and 24 Emerging Markets countries.

Bloomberg Barclays Capital U.S. Aggregate: The Bloomberg Barclays U.S. Aggregate Index provides a measure of the performance of the U.S. dollar denominated investment grade bond market, which includes investment grade (must be Baa3/BBB- or higher using the middle rating of Moody's Investor Service, Inc., Standard & Poor's, and Fitch Inc.) government bonds, investment grade corporate bonds, mortgage pass through securities, commercial mortgage backed securities and asset backed securities that are publicly for sale in the United States. The securities in the U.S. Aggregate Index must have at least 1 year remaining to maturity and must have \$250 million or more of outstanding face value.

Credit Suisse Leveraged Loan Index: The Credit Suisse Leveraged Loan is an index designed to mirror the investable universe of the U.S. dollar denominated leveraged loan market. New loans are added to the index on their effective date if they qualify according to the following criteria: Loans must be rated "5B" or lower; only fully-funded term loans are included; the tenor must be at least one year; and the issuers must be domiciled in developed countries. Loans are removed from the index when they are upgraded to investment grade, or when they exit the market (for example, at maturity, refinancing or bankruptcy workout). Total return of the index is the sum of three components: principal, interest, and reinvestment return. The cumulative return assumes that coupon payments are reinvested into the index at the beginning of each period.

Consumer Price Index: The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

NCREIF ODCE Index: The NCREIF ODCE is a capitalization weighted, time-weighted return index that measures the performance of open-end core real estate funds. The funds included in the creation of this index are generally considered diversified across U.S. property types and regions.

90-day T-Bills: The 90-day T-bill index is designed to measure the performance of U.S. Treasury Bills maturing in 3 months.

H:\Asset Allocation\2024\20240520 Dan cover- Asset Alloc target change- 2% increases in pvt credit, from non-US eqty and 2% core to non-core - Board- v2.docx