ANNE ARUNDEL COUNTY
RETIREMENT AND PENSON SYSTEM

Board of Trustees
Minutes of July 18, 2023, Meeting

Members Present: Christine Anderson, Howard Brown, Anne Budowski, Karen Henry, Rhody Holthaus, Mary Lu Hughes, Kevin Nethers, Billie Penley, Ronald Seldon, Chris Trumbauer, and Leroy Wilkison

Members Absent: Alan Hyatt and M. Kathleen Sulick

Staff Present: Lynn Daitch, John Hammond, Kelly Lovett, and Beth Zimmerman

Staff Absent: Lori Blair

Guests: Rhett Humphreys, Keith Stronkowsky, DeAnna Ingram Jones, Cheryl Stober, Rene Lefevre, Remi Omisore, Gar Chung, and Joe Ebisa

Recorder: Stacy Kish, Audio Associates

Ms. Anderson called the meeting of the Board of Trustees of the Anne Arundel County Retirement and Pension System (Board) to order at 12:01 p.m. The minutes for the June 20 meeting were unanimously approved.

Manager Interview

Loomis Sayles
Cheryl Stober and Rene Lefevre

Mr. Lefevre gave an update on the firm. As of May 30, the company is up to $306 billion due to market action and positive client inflows. Loomis Sayles divides the fixed and equity side of portfolio. The equity is just under $76 billion, which is up 18% since 2022 mostly from market action. The firm did conclude a DSP program, a voluntary separation program. Of the 97 eligible employees, 27 participated and gave the firm cost-saving opportunities and elevated employees to new positions.

Elaine Stokes will retire in December 2023 but will remain on the Board until February 2024. Four long-tenure strategists have been named associate portfolio managers (see page 8). Effective June 30, the full discretion and bank loan teams will combine under one umbrella.

This will enhance the efficiency of both teams and allow the teams to leverage their expertise in the marketplace.

Ms. Stober continued with an update on the bank loan merger. As the market has evolved, there is more overlap between the high-yield and bank loan space. As small companies in this space have merged and grown, it has become more attractive for them to issue fixed-rate debt. It has been converging to a more unified market in the last few years and being under the full discretion umbrella will give new opportunities over both sets of products. Bank loans are floating rate products and will reset when the federal reserve changes rates.

The market has been dominated by CLOs, which are stabilizing in the bank loan space and help to preserve a floor to the market. CLO demand is a growth engine and helps keep prices stable in the market. Loomis Sayles pays attention to CLOs.

Defaults are still the main focus in the bank loan space. Loomis Sayles provides deep credit research. Default modeling often overpredicts what will happen in the default space. Loomis Sayles still expects a recession but believes it will be milder than originally anticipated.

There is nothing left to mature in 2023 or 2024 (see page 14). Companies that are better quality can refinance, and this is where the portfolio tends to focus. Lower-rated names may be having a harder time due to how things are trading on the secondary market.

The Board is invested in a high-quality portfolio (see page 16), and the prices tend to hold up better. The default track record shows that Loomis Sayles have not had a default since June 2020.

The company's strategy holds to the DD benchmark (see page 22). Loomis Sayles has seen CLOs continue to form. As of May 31, Loomis Sayles is up 6.77% compared to benchmark of 5.75%. Performance has been strong in 2022 and 2023. Inflation has not been a big issue for companies that the company tracks. The odds of a recession are increasing, which may result in some rate cuts that could hurt the portfolio compared to where it is today. Loomis Sayles expects to carry a good part of the portfolio for the next six months.

There were no questions from the Board.

New England Pension Consultants
Rhett Humphreys, Keith Stronkowsky, DeAnna Ingram Jones

Mr. Humphreys introduced Keith Stronkowsky, who will be participating during the in-person meeting in August. Mr. Humphreys presented the June 30 preliminary flash report. Year-to-date, global equity is at 13.9%. U.S. large companies is at 6.9%, and international developed is at 11.7%. The emerging market equity index is at 4.9%.

Global bonds are at 1.4%. U.S. investment grade fixed income is more than 2.1%. U.S. investment grade credit and high-yield credit is 5.4%. Emerging market debt (e.g., hard currency and local currency) are up and invested through the PIMPCO portfolio. All asset classes are up.

Anne Arundel portfolio is about 75% updated. Year-to-date net of fees is at 7%. The one year and three-year marks are greater than that. This is good news for actuarial. The 7% is motivated by public equities (13%) and U.S. domestic equity (14.4%). International equity is at 13.1%.

The only manager that is giving NEPC pause is Hardman Johnston, and there is nothing going on here but style. This is a growth manager, which has been out of favor recently. Causeway is a dedicated value manager and is doing well. You have both styles in your portfolio. Emerging was paired back, but it is 6% for the year. It is going to be a similar theme of value and growth.

Mr. Trumbauer: Going back to domestic equity. Those numbers are extraordinary. Can you say more about why they are overperforming?

Mr. Humphreys: It is style. While value has outperformed growth recently, if you look at the index this year, growth is making a comeback. NEPC requested the Board rebalance because value was overweighted. In the past six months, growth is up 13% whereas value is up 4%.

The fixed income portfolio is divided into total fixed income (3.8%) that is made up of core/core-plus and non-core (e.g., bank loans, high-yield, and emerging market debt). By diversifying into yield credit asset classes, the Board has added 11 percentage points of 12% of the fund, which is more than 1.2 percentage points of additional rate of return. This has not only protected but added a lot of value.

Mr. Humphreys presented the Board with a recommendation. He recommended that the Board take $80 million and split it between the PIMPCO Fund ($40 million) and Dover Street Fund XI ($40 million) managed by HarbourVest. The Dover Street Fund XI is a secondaries fund, which means the general partner will buy secondary interest in funds that are already up and running for several years. This helps manage the J-curve. HarbourVest also makes investments at a discount. This is a $12 billion 10-year fund with a possible four-year extension. The fees are favorable (e.g., 75 basis points and the carry interest is 12.5%). The fund must earn 8% net of fees before the fund will take their 12% of profit. This means the Board has already cleared your actuarial rate of return before sharing the rate of profits.

HarbourVest will be closing the fund on December 31. It has been open since late last year and has already started investing. As a limited-partner committee, the Board will mitigate blind pool risk and will buy into a positive rate of return from day one. The HarbourVest presentation from the week of July 11 is included in the July 18 NEPC presentation.

Mr. Trumbauer: I was impressed by the HarbourVest presentation and their track record. The investment committee reached consensus to move forward with NEPC recommendation to bring this to the full Board for a vote. I move that we go forward with the investment in the Dover Street Fund XI.

Mr. Wilkison seconded the motion.

The board voted to invest $40 million in the Dover Street Fund XI. All approved. No opposition.

Clifton Larson Allen LLP
Remi Omisore

Clifton Larson Allen LLP issued the report during the week of July 11. Mr. Omisore presented the results of the audit of the financial statements and risk assessment. Managers are responsible for preparing the financial statements. Clifton Larson Allen LLP issued unmodified opinion, the highest level of assurance on financial statements.

The audit follows the generally accepted auditing standards (GAAS). Clifton Larson Allen LLP compares this plan to other similar plans and found no outliers to bring to the Board's attention. The accounting estimates (e.g., investment balance and valuations) include assumptions that are made by management of the investment vehicles or trust. Clifton Larson Allen LLP looks for bias or outliers and found no items of concern. For pension liability, management hires an actuary and compare input and assumptions to other like plans and found nothing to report to the Board. Clifton Larson Allen LLP identified no weaknesses or deficiencies during the audit process.

The financial risk assessment consists of several components (e.g., management of override of controls, improper revenue recognition, valuation of alternative investments, valuation of pension liability and related amounts, new accounting pronouncements, and financial reporting). There were no new items applicable to the plan this year.

The pension liability has not raised any concerns. Historically, the portfolio has been over the 7% return rate, and there are no concerns to bring to the Board. Clifton Larson Allen LLP looks to see if everything is in-line with industry standards (e.g., National Conference on Public Employee Retirement Systems) to look for outliers. There are no risks from an audit perspective.

Governmental Accounting Standards Board updates should not impact the plan. No new line items on the financial statements. Clifton Larson Allen LLP has issued an unmodified or clean opinion (e.g., no finance or material weaknesses or deficiencies). This information will be presented to oversight at the next meeting.

Administrative Report

Ms. Lovett announced two retirements in July. In addition, Bill 5823 went before the council and was passed unanimously. This bill will add a seventh year of drop to police plan only. It was a result of labor negotiations earlier in the year. In addition, the Bill made changes to payment options to employees who dropped out of the drop before the end of the initial three-year period. These employees will now have an opportunity to pay the missed contributions while they were in the drop in a lump sum or over a three-year payroll deduction. If the employee retires, they can pay in a lumpsum or pay the offset until repayment is completed.

Rhody Holthaus has been elected as the employee representative and will take the position previously held by William DeHoff.

John Hammond: We have completed the PIMPCO paperwork for the private debt instrument and will have a capital call later in the week. We will begin paperwork for HarbourVest. What percent of police officers take advantage of the drop when they retire?

Ms. Daitch will look into this and follow up with the Board.

Mr. Wilkison: Has there been any progress in filling the other analyst position?

Ms. Lovett: Amy Lucus from state retirement system has joined the staff. She has 20 years of experience in the state system.

Other Business

The next meeting will be held on August 15th, which will be held in person. The meeting adjourned at 1:00 p.m.

I hereby certify that, to the best of my knowledge, the foregoing minutes are accurate and complete.

Anne Budowski — 9/13/2023

Anne M. Budowski — Date
Secretary to the Board