1 MUNICIPAL EMPLOYEES'
2 ANNUITY AND BENEFIT FUND OF CHICAGO
3 SPECIAL INVESTMENT MEETING
4 NO. 2022-03-01
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10 STENOGRAPHIC REPORT OF PROCEEDINGS had at
11 the video conference meeting of the above-entitled
12 matter, held at 321 North Clark Street, Suite 700,
13 in the City of Chicago, County of Cook, State of
14 Illinois, on March 3, 2022, commencing at the hour
15 of 9:00 a.m.
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1 APPEARANCES

2 BOARD MEMBERS:

3 ROBERT P. DEGNAN, President

4 VERMA R. THOMPSON, Recording Secretary

5 MELISSA CONYEARS-ERVIN, City Treasurer
WILLIAM CANNING, Trustee
6 CRAIG SLACK, Deputy City Treasurer

7 ATTORNEYS FOR THE BOARD:
BURKE, BURNS AND PINELLI, LTD.
8 BY: MS. SARAH A. BOECKMAN

9 ALSO PRESENT:
DENNIS WHITE, Executive Director
10 STACEY RUFFOLO, Deputy Executive Director
DONNA HANSEN, Office Manager
11 SANDRA SHELBY, Comptroller
STEPHEN WOLFF, Investment Officer
12 NIKKI RIALS, Benefits Manager
KRISTEN DEWALD, Manager of Member Services
13 JAMIE WESNER, Marquette Associates
BRETT GRAFFY, Marquette Associates
14 ANDREW SUSSER, MacKay Shields
THERESE HERNANDEZ, MacKay Shields
15 JOSEPH MAIETTA, MacKay Shields
ROY LECKIE, Walter Scott
16 FRANCIS SEMPILL, Walter Scott
DON ANDERSON, Northern Trust
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1 PRESIDENT DEGNAN: I hereby convene this
2 Special Investment Meeting for March 3, 2022.
3 Donna, would you please call the roll?
4 MS. HANSEN: Trustee Canning.
5 TRUSTEE CANNING: Present.
6 MS. HANSEN: Trustee Degnan.
7 PRESIDENT DEGNAN: Present.
8 MS. HANSEN: Trustee Thompson.
9 TRUSTEE THOMPSON: Here.
10 MS. HANSEN: Trustee Conyears-Ervin.
11 TRUSTEE CONYEARS-ERVIN: Present.
12 MS. HANSEN: We have a quorum.
13 PRESIDENT DEGNAN: Thank you. We have a
14 quorum for today's meeting.
15 Public Act 101-0640 allows this meeting
16 to be conducted by audio and video conference
17 because we continue to believe that it is not
18 prudent or practical to have a public meeting. The
19 Act requires a roll call vote be taken on each
20 matter acted upon.
21 Further consistent with Public Act
22 101-0640, I note for the record that both the
23 Executive Director and myself and Mr. Canning are
24 physically present at the Fund's office.

1 We have posted notice of this meeting in
2 accordance with the Open Meetings Act and the
3 meeting is being recorded. A transcript of the
4 proceedings will be prepared and ultimately, after
5 approval, will be made available on the Fund's
6 website.
7 In that notice, we did notify the public
8 that they were welcome to attend in person at the
9 Fund's office.
10 Consistent with Public Act 91-0715 and
11 reasonable constraints determined by the Board of
12 Trustees, at each regular meeting of the Board or
13 its committees that is open to the public, members
14 of the public may request a brief time to address
15 the Board on relevant matters within its
16 jurisdiction.
17 Are there any requests for public comment
18 today?
19 MS. HANSEN: No, sir, there were no
20 requests to address the Board.
21 PRESIDENT DEGNAN: Hearing none, we will
22 move on.
23 Our first item is an informational item
24 before we start the presentations. We have asked

1 the Investment team to update us on what has been
2 happening in the markets due to the recent invasion
3 in Ukraine by Russian forces.
4 Jamie and Stephen, I will turn it over to
5 you.
6 MR. WESNER: Thank you, Mr. President.
7 I am going to share my screen to put up
8 the February Market Tracker. This is the summary
9 of performance through the end of February and
10 really kind of a guide to the conversation.
11 I think we will start the conversation
12 with highlighting that this is an extremely fluid
13 situation, not surprising. We are already in a
14 period of high market volatility given the increase
15 in inflation and the anticipated increase in
16 interest rates that we were expecting throughout
17 2022.
18 I think many market participants
19 identified the risk but I don't think market
20 participants identified the magnitude of the
21 potential risk. I think that goes for other world
22 leaders as well as market participants.
23 I think the thought process was that
24 Russia and Putin may come in and try to annex a few

1 of the Eastern Regions of Ukraine. But this full
2 scale invasion that we have now seen, I think was
3 not priced into the market. And when we saw this
4 invasion take place, the markets are now trying to
5 digest what does this mean not only for Ukraine and
6 Russia, but what does it mean for Europe and the
7 rest of the world.
8 This is really a day-by-day situation.
9 We saw for the first two months of 2022 we saw the
10 global equity markets sell off. It is around 8 to
11 10 percent. We saw in terms of global equity
12 moves. Obviously, the Russian market has been and
13 emerging markets in general has been the most
14 immediately been impacted.
15 And I think of that in regards to the
16 index, whether it be the emerging market index or
17 the broad international index, up until yesterday
18 had Russian stocks as a part of that. The emerging
19 market index stocks were meaningful. 5 percent
20 exposure within that index.
21 Yesterday MSDI, which is the premiere
22 international index provider, did announce that
23 they would be removing Russia from not only their
24 core indices but also their emerging market index.

1 Russia would now be identified as a standalone
2 market. They are basically pulling them out.
3 So what does that mean? Markets are
4 still trying to figure out what it means. It means
5 that index providers, passive index fund providers,
6 now who were benchmarked against that index now
7 have to adjust. Our job is to match the benchmark.
8 This benchmark now does not include Russia
9 equities. In a normal market, that can be done in
10 an orderly fashion.
11 In a market where the Russian exchange is
12 closed and the ability to trade in ADRs and GDRs,
13 which are American Depository Receipts in the U.S.,
14 which is a way for companies to lift their
15 securities in a secondary fashion on a market
16 outside of their own.
17 So some of your managers may own Russian
18 equities through an American Depository Receipt.
19 Even in those cases, those either are not trading
20 or are trading down 70 to 80 percent because of the
21 uncertainty of what this means in regards to how
22 exposure is designed to a Russian entity. What
23 does it mean to own a Russian company right now, if
24 they can't trade with the rest of the world. If

1 they can't either get import products to export the
2 goods to the rest of world. What does that mean to
3 the owner of one of those assets. A lot of
4 uncertainty out there in terms of what does value
5 mean in these securities.
6 For most institutional portfolios like
7 yours, the overall exposure to Russian equities is
8 exceptionally low. 25 basis points exposure area.
9 And while in terms of dollars, we are
10 talking about millions of dollars of exposure.
11 That exposure is dropping considerably because the
12 prices of those securities have gone down.
13 And then many managers, active managers,
14 did try to trim going into this situation. So
15 managers like to trim exposures but as liquidity
16 dried up in the markets, managers in some cases
17 weren't able to liquidate. The positions that are
18 remaining are exceptionally small. Right now
19 typically the approach we see in these
20 situations -- - we haven't seen many of these types
21 of situations, you want to wait to see what happens
22 with the markets. What abilities the managers have
23 to continue to trade out of their positions and
24 then essentially reassess as we get more

1 information.
2 We don't advocate forcing managers to
3 liquidate the positions. Essentially, we would be
4 asking them do something they can't do right now.
5 Most active managers are going to liquidate in an
6 ordinary fashion as liquidity comes back to the
7 marketplace.
8 If we were to get some type of ceasefire
9 in Ukraine, a positive resolution, that may
10 introduce some liquidity back into the market and
11 then managers will do what they are paid to do.
12 Make an assessment and try to add value within the
13 guidelines that you have set forth.
14 Sarah and I were talking about earlier
15 the idea of waiting to see what comes from
16 Springfield.
17 This is a reminder the Iran Sudan
18 restrictions that used to be in place have expired
19 or sunset I think is the right word.
20 But the process that the Municipal Fund
21 has always taken is that while Springfield may take
22 an action, or the State Pension Funds, you are not
23 governed by those actions. But this Fund has
24 historically adopted in spirit a provision for your

1 Investment Policy that is similar to what comes
2 from Springfield. That's always the policy we go
3 through there. If there is a provision that is
4 adopted down in Springfield, we will review that,
5 we will discuss it, and then this Board will take
6 an action to put that into your Investment Policy
7 and target that. Just so you know the processes
8 that are in place. We have a process for this.
9 The policy as we talked about before is
10 kind of a living document. So we will wait to see
11 what information we have and that will be brought
12 to you as a potential amendment to your Investment
13 Policy, if we wanted to divest of Russian holdings.
14 Looking at this in connection with
15 interest rates, yesterday we also started to get
16 testimony from the Federal Reserve Chairman. He
17 testified in front of Congress.
18 We talked about at previous meetings over
19 the last couple of months that the biggest risk to
20 the market was increases in interest rate. Driving
21 by inflation. Coming out of 7 percent plus in
22 terms of year over year increase in their
23 inflation.
24 The Federal Reserve has been transparent

1 and the markets have priced in the increase in the
2 short-term interest rates for 2022. What that
3 would have meant is six or seven interest rate
4 increases.
5 We typically think of Federal Reserve
6 rate increases as coming in in quarter percent
7 increments. They don't have to do that.
8 And so prior to the Russian situation,
9 the thought was the Federal Reserve would do a
10 first interest rate increase in March of a half
11 percent and be a little bit more aggressive. Try
12 to reduce inflation. Look to being more proactive.
13 The Russia situation now it puts Chairman
14 Powell and the rest of the Federal Reserve in more
15 of a predicament that they weren't anticipating.
16 He said yesterday that they will likely
17 still go forward with that quarter percent increase
18 in March, but they will continue to assess the
19 situation. Basically giving flexibility to
20 whatever happens in Ukraine and Russia, that is
21 going to dictate what the Federal Reserve does.
22 If you look at the impact of the Russia
23 crisis, while it's causing the equity markets
24 throughout the world to pull back and correct a

1 bit, what it is also doing is potentially adding to
2 inflation. Because the other factor that we see
3 come out of this crisis in Ukraine and Russia is
4 that oil prices have skyrocketed. You think about
5 one of the largest contributors to inflation is
6 energy prices. Oil now is in excess of $100 a
7 barrel.
8 If we continue to see Russia remain off
9 line in terms of their ability to export energy, we
10 saw the natural gas pipe line that goes to Germany
11 be halted as a reaction to the invasion of Ukraine
12 and the Russians have more supply comes off line,
13 that puts more pressure on our prices to go higher.
14 Then for folks in the U.S. and across the world,
15 that increases commodity prices.
16 Another factor that plays into
17 commodities, that I wasn't as familiar with, was
18 the prices of a lot of grain. The amount of wheat
19 and certain types of seed oils that are produced in
20 Ukraine and Russia.
21 Those are all factors that are input in
22 products in the U.S. but more importantly puts
23 pressure on prices over in Europe and the rest of
24 the world, which ultimately comes back here to the

1 U.S.
2 If Ukraine's supplies are destroyed,
3 Russia is not exporting wheat, for example, now the
4 rest of the world is going to bid out the price of
5 U.S. wheat even more. So back here we're not
6 immune from that. Now we're competing with the
7 rest of the world for our wheat. U.S. producers
8 will now be faced with the idea do I export it
9 more? Do I sell it into the local market?
10 We are likely to see pricing pressures
11 not only at the pumps but at the grocery stores as
12 well. I think we were already seeing it so this is
13 going to add to the inflationary pressure.
14 Unfortunately, it is all connected in
15 terms of the original problem for 2022, which was
16 inflation and now the number one problem for 2022
17 which is the war in Ukraine.
18 A lot of various factors. We're going to
19 talk in a little bit about asset allocation. I
20 will switch over to the asset allocation slide
21 right now to be mindful of our time.
22 As we look at the asset allocation, big
23 question, what do we do in the meantime? How do we
24 protect ourselves from this volatility?

1 You have taken steps over the last few
2 periods or quarters to modify your asset allocation
3 and I will take a minute or two today to talk about
4 that.
5 In terms of your asset allocation, this
6 is the Asset Allocation Study that you approved in
7 May of last year.
8 As you see periods of volatility, whether
9 it be the volatility driven by inflation or
10 volatility driven by a geopolitical event like we
11 are seeing now, we are always concerned about
12 protecting this portfolio to the downside.
13 Madam Treasurer said recently, we can't
14 invest our way out of this problem, our funding
15 ratio problem, but we don't want investments to
16 make our funding problem worse.
17 In an environment like this, where you
18 are still cash flow negative, and as we get into
19 the end of this year we will have to liquidate
20 assets to meet benefit payments. We need to be
21 very conscious about creating a portfolio that can
22 limit the downside when you have a period like
23 January and February.
24 Just as a reminder, and for Trustee

1 Canning who wasn't on the Board when the decision
2 was made, the Board had elected to move towards
3 Portfolio A. That was Portfolio A as your new
4 target.
5 And what we do when we do an Asset
6 Allocation Study is run different portfolios
7 through our model to see what is the expected
8 return in risk characteristics of the portfolio for
9 over ten years.
10 One thing we know for certain is that the
11 next ten years won't produce the returns that are
12 on the page here and they are summarized down here
13 at the bottom, but it gives us a good idea how the
14 portfolios performed relevant to one another.
15 One of the biggest things we look to do
16 over the last couple of years across the plan
17 portfolios is to reduce the fixed income. Fixed
18 income has always been an area of stability. Kind
19 of an anchor for your portfolio in times of
20 volatility like this.
21 We do know that going forward fixed
22 income with interest rates so low likely only give
23 us 1 to 2 percent returns over the next couple of
24 years.

1 In 2020, we have negative returns for
2 fixed income. 2022, we're down about 3 percent in
3 fixed income already.
4 The idea is making sure we have stability
5 in the portfolio without locking ourselves in or
6 increasing the likelihood of lower returns.
7 The Board adopted that in May of last
8 year moving 3 percent out of fixed income so you
9 can see up here at the top. We decreased
10 investment grade fixed income by 3 percent from 11
11 percent to 4 percent. Still have approximately 10
12 percent across various parts of the higher yielding
13 fixed income areas. Bank loans, high yield,
14 private debt. We call it opportunistic credit.
15 Those are all very similar strategies. You have
16 managers that can manage across those areas.
17 But where we added to the portfolio is
18 down at the bottom. We added a slight increase
19 exposure to infrastructure, which as we manage our
20 liquidity over the next several quarters in the
21 year, we may likely increase our allocation to
22 infrastructure slightly. But really where the new
23 allocations are, the increased meaningful changes
24 are, is private debt, private equity. You have now

1 4 percent allocation to each private debt and
2 private equity.
3 As a reminder, this fund hadn't made any
4 new commitments to private debt over the past eight
5 to ten years. Because of the liquidity concerns,
6 there was not an appetite to add to private equity
7 at that time. But now that you have a funding plan
8 in place, and as we move further along the ramp and
9 getting close to next year having actuarial
10 required funding from the City, we are talking much
11 more seriously and are ready to start making
12 commitments to the new private market investments.
13 So that was 4 percent to private debt, 4 percent to
14 private equity.
15 Your existing allocation between 2 and 3
16 percent allocated to private equity. Some of the
17 old investments that you made back in the kind of
18 post-financial crisis era of 2008 to 2012, most of
19 those investments or really all of those
20 investments, they are not making any new
21 investments. If they sell assets, sell companies,
22 they return capital to you.
23 Steve and I get an e-mail probably once a
24 week from one of those managers notifying us of a

1 distribution of capital. Distribution of capital
2 is great, that is money back in the Fund. You can
3 use it to make benefit payments, but that is money
4 that is going out of the private equity and private
5 market asset classes and we need those asset
6 classes because they have the highest expected rate
7 of return and they created the largest rate of
8 return for you over the past several decades.
9 We need to make sure that we have that
10 allocation in there and that is why we are going to
11 talk today and my colleague Brett Graffy is on to
12 talk about private debt. We want to talk about
13 these new asset classes and about making new
14 commitments to these asset classes so you can make
15 sure that we work towards having an 8 percent
16 overall allocation to private markets.
17 Again, it is not going to solve the
18 funding crisis but it will add more stability to
19 the portfolio and it will hopefully create in times
20 like this an environment where we are more likely
21 to hit our assumed rate of return over time.
22 Finally, just at the bottom, as you look
23 at the summary and the comparison of the two
24 portfolios, not only does Portfolio A, which has

1 more higher private market exposure have a higher
2 expected return. You can see 7.16 versus 6.88. It
3 does so without adding any anticipated volatility
4 the portfolio. It actually marginally reduces the
5 volatility.
6 If we look forward, we always want to
7 make sure we have a portfolio that gives us a
8 reasonable expectation of hitting our assumed rate
9 of return but at the same time isn't taking on
10 unnecessary volatility.
11 I just wanted to lay that out as kind of
12 a refresher in terms of asset allocation. I know
13 we are going to have additional conversations in
14 terms of how the Asset Allocation Study plays into
15 the Actuarial Report that you get and the
16 information you will be getting from Segall. Just
17 wanted this again to be a little refresher in terms
18 of asset allocation and then we will have
19 additional conversations on how this plays into
20 going forward.
21 PRESIDENT DEGNAN: Thank you, Jamie.
22 Stephen, do you have anything you want to
23 say?
24 TRUSTEE CONYEARS-ERVIN: I have a

1 question for Jamie. I was thinking about a comment
2 you had made about the divestment in Russia. I
3 know the State of Illinois has been discussing this
4 topic as well. I know the Governor made a point so
5 I know that you mentioned that it's possible at a
6 later time further direction can come from the
7 State as far as legislation. But in us being
8 proactive, and also being respectful of the
9 national situation, there should be discussion from
10 us about divestment as well being proactive.
11 But looking at our current financial
12 situation, I thought it would be worth a
13 conversation for us to have as a fund.
14 MR. WESNER: As we spoke to the managers,
15 the managers are very focused first and foremost on
16 protecting value of the assets that they are
17 charged with managing. But they are certainly also
18 focused on making sure that they are consistent
19 with benchmark and consistent with just the
20 sentiments of the marketplace as well.
21 I think as we move forward, even before
22 things are mandated from funds, and for you whether
23 that is mandated by a mandate put in place by the
24 State that this fund would adopt for its own

1 investment policy, you are seeing a continued
2 decrease in any Russia exposure that you have and
3 we'll update you in two weeks at your regular
4 meeting.
5 I would venture to say that your exposure
6 is going to be even less than it is now. It is
7 definitely a discussion that is being had
8 internally here amongst your staff and consultants.
9 It is a conversation being had with all your
10 investment managers. The discussion is being had
11 and will evolve over the next couple of weeks.
12 TRUSTEE CONYEARS-ERVIN: The next couple
13 of weeks, okay. Let's continue to talk about that.
14 That is definitely at the forefront of my mind
15 because that is something that we have been looking
16 at internally even in the Treasurer's Office. I
17 just want to make certain with the pension funds
18 that we are also being sensitive to what is going
19 on as well.
20 MR. WESNER: Really the challenge is
21 trying to balance dual mandates that most folks
22 have and trying to maximize value. But also doing
23 so in the environment where for most of these
24 Russian securities there is no market right now.

1 So, if you want to take action, you can't take
2 action.
3 I can't recall if I was saying this
4 earlier in the conversation here or if I was saying
5 this before the meeting started. But yesterday
6 when MSDI went as far as to remove Russia from
7 its indices, it really put the most immediate
8 burden on index fund providers because the index
9 fund providers that are out there are charged with
10 mimicking the index. Those index fund providers
11 need to eliminate those Russian holdings.
12 The problem is they can't eliminate the
13 Russian holdings because there is no market for the
14 Russian securities so that is going to create more
15 of an issue.
16 Your active managers, while they are also
17 looking to diverse and reduce those Russian
18 exposures, they at least for their policies they
19 are permitted in most all cases to hold securities
20 outside of the benchmark and so that allows them to
21 stay within their policy guidelines. Where the
22 index fund providers are in a little bit more of a
23 precarious position.
24 We are waiting to see how things evolve

1 because right now the net fund providers I don't
2 think they know what they are doing because they
3 are not able to sell and they are not able to stay
4 in compliance with mimicking the benchmark. That
5 is going to be a day-by-day situation to see how
6 that plays out.
7 Sarah, do you have some thoughts?
8 MS. BOECKMAN: Consistent with what Jamie
9 said from a fiduciary standpoint, the most
10 important thing is that you follow your process.
11 To Jamie's point, I think you have,
12 based on what he said, established what your
13 process has been traditionally when something like
14 this has occurred.
15 I do think you need to be sensitive, like
16 you said Madam Treasurer, to what is going on but
17 you also have to make sure you are not being
18 reactionary and you are following your process,
19 following what your fiduciaries are telling you,
20 your consultant and your Investment Manager.
21 Like Jamie said, I think we are going to
22 know a lot more in two weeks. Your exposure is
23 very limited and it is probably going to be even
24 more limited in two weeks when we have more

1 information.
2 From our perspective as fiduciaries, you
3 want to make sure you are following your process
4 and you are following your process. Like Jamie
5 said, I do think, based on what we have heard, the
6 General Assembly is going to be passing some laws
7 that are binding on the state pension funds.
8 You have used those as a benchmark in the
9 past to consider and implement similar divestment
10 actions, when it comes to Sudan and Iran.
11 We will wait and see what happens there.
12 We will continue to monitor what your managers are
13 saying and what your consultants say.
14 The nice thing is you have a meeting in
15 two weeks. You will know a lot more and to Jamie's
16 point we will know what some of your managers are
17 doing hopefully when some of the restrictions on
18 trading ease up.
19 TRUSTEE CONYEARS-ERVIN: Okay. I just
20 don't necessarily want to wait until a mandate but
21 nevertheless we will talk over the next couple of
22 weeks. I am sure there is going to be a lot of
23 discussion over the next couple of weeks.
24 MS. BOECKMAN: Absolutely.

1 MR. WESNER: To comment on the mandates,
2 the Board always has the flexibility to put
3 anything reasonable in your policy guidelines.
4 While it hasn't been the precedent to act before
5 something takes place in Springfield, you do have
6 the ability to do that.
7 MS. BOECKMAN: Absolutely.
8 MR. WESNER: I wanted to make sure that
9 was clear. You don't have to wait for anything to
10 take place in Springfield first.
11 MS. BOECKMAN: Absolutely. You just used
12 that as a benchmark in the past to be able to say
13 this is what our sister state funds are doing and
14 we reviewed it. It is not binding on us but we
15 have considered that with our fiduciaries, our
16 consultants and our managers, and determine that it
17 is also prudent.
18 To Jamie's point, you don't need that
19 action but I think at this point it is a little bit
20 too early to get to that point until we have more
21 information from your managers on what is going on
22 in the next couple of weeks.
23 As Jamie said, even if you wanted to you
24 wouldn't be able to get out of quite a few of the

1 investments that you are in right now.
2 MR. WESNER: Are there any other
3 questions on the broad market? With your
4 direction, we can move on to the private debt
5 discussions, if you would like.
6 PRESIDENT DEGNAN: Thank you. We will
7 turn to the presentations now.
8 MR. WESNER: The first is going to be my
9 colleague Brett Graffy, who is up on the screen.
10 Brett is our lead Private Debt Analyst. In terms
11 of our views internally on the asset class, our
12 views on the underlying investment managers in the
13 space, Brett leads that process internally.
14 We thought we could have Brett kind of
15 talk through kind of an overview of the asset
16 class. Because while we have it in your asset
17 allocation and we have talked about it a bit in the
18 past, before we launch potentially a RFP in the
19 space, it is good to have further education here to
20 talk through it so you get familiar with the
21 nuances of the asset class and why we think it is
22 good.
23 PRESIDENT DEGNAN: Welcome, Brett. Go
24 ahead with your presentation.

1 MR. GRAFFY: Thanks for having me today.
2 There are about 20 or so slides in this
3 deck. I want to make this as conversational as
4 possible. Please, stop me at any time. I am happy
5 to reiterate any slide or go back on any previous
6 slides that we went through. I want to be timely
7 and efficient with our time.
8 In any of these discussions when starting
9 out, I want to make really a point in communicating
10 why we are investing in private credit and
11 especially why we're looking at it relative to
12 other asset classes in your portfolio so we
13 understand the opportunity set.
14 Really to answer that question, when
15 looking at private credit, we are capturing two
16 premiums in the marketplace today that exist.
17 The first premium is the yield premium.
18 What I mean by that is the yield that private
19 credit is earning over traditional high yield and
20 other fixed income asset classes. In today's
21 market on average, you are probably getting about
22 250 to 300 basis points or 2 and a half to 3
23 percentage points of additional yield compared to
24 those asset classes.

1 The second premium, a structure premium,
2 this is a downside protection and a risk mitigator
3 and the fact that these loans are actually probably
4 at the top of the structure. So they have first
5 claims on assets in instances of bankruptcy
6 liquidation and also defaults and so forth. They
7 are ahead of equity and other pieces of the capital
8 structure so they are senior to everything in that
9 capital structure.
10 Those are really the two premiums that we
11 are capturing in the market by investing this asset
12 class.
13 Going to the first slide, private debt
14 has really received a lot of recognition in the
15 past few years as an emerging and growing asset
16 class. While that is true, private debt has really
17 existed for decades. The biggest difference the
18 past ten or so years is now that private debt
19 lending is done by nonbank institutions.
20 What I mean by nonbank institutions, I
21 will go into a later slide. These are the
22 investment managers that you are probably well
23 aware of in the space or at least seen before.
24 Whereas, prior to the Great Financial

1 Crisis, the banks controlled this market,
2 controlled private debt lending. I will explain
3 further in a few slides.
4 In its simplest form, private debt is
5 typically a middle market company or a small mid
6 size business that is receiving a loan from a
7 nonbank. There is not much that is more
8 complicated beyond that.
9 The most important characteristics in
10 private debt is that it is higher yielding compared
11 to other fixed income asset classes. The interest
12 rate is floating so it changes, it fluctuates, on a
13 quarterly basis in line with LIBOR or interest
14 rates.
15 You compare that to the backdrop right
16 now of potentially rising interest rates, inflation
17 and so forth, that protects your yield.
18 Finally, the duration of the loan itself
19 is shorter in typically about five or six year
20 increments.
21 Going to the next slide, this slide puts
22 into context the private debt market versus other
23 non-investment grade debt.
24 Something important to note here are

1 leveraged loans or high yield bonds, sometimes
2 leveraged loans are called syndicated debt as well.
3 These are pieces of debt typically issued by large
4 cap companies.
5 What I mean by that is companies who have
6 over billion dollars in revenue. They have over
7 500 employees. These are the largest companies in
8 the U.S. By definition, there is about 16,000 of
9 these companies in the U.S. today.
10 What private debt focuses on is middle
11 market businesses and small to mid size businesses.
12 Middle market companies by definition have
13 anywhere from 50 to up million in revenue. In the
14 U.S. alone today there are 200,000 of these
15 companies in the U.S. So the opportunity set is
16 almost ten-fold larger with middle market companies
17 compared to large cap companies.
18 Then you take a step further down, small
19 to mid size businesses, these are companies that
20 have about three, five, ten million dollars of
21 annual revenue. There are about 6 million of these
22 businesses in the U.S. alone today. Combining
23 those two middle market size businesses the
24 opportunity set is about 6.2, 6.3 million

1 businesses in the U.S.
2 When you think about the driver of the
3 U.S. economy, these are the true drivers of the
4 U.S. economy. The opportunity set is exponentially
5 larger. As you can see, there is about a little
6 more than 800 billion AUM in private debt. The
7 majority of that has come in the past seven or
8 eight years as banks have gotten out of this
9 market.
10 You might look at this and think the
11 market is near maturity but we believe and we have
12 the data to show that this market has potential for
13 further growth.
14 Going to the next slide, I won't spend
15 too much time on this because we mentioned some of
16 this a minute ago.
17 Private debt can take a few names. You
18 might see terms like direct lending, distressed,
19 special situations, venture debt.
20 For this conversation, we are focused on
21 direct lending, which are loans to helping middle
22 market businesses. These businesses are either
23 private equity owned or owned by a family a founder
24 or entrepreneur.

1 Going to the next slide, we mentioned a
2 few reasons why the private debt market is
3 attractive. But other reasons why investors are
4 attracted to the asset classes today, especially in
5 today's market, and we will elaborate further here,
6 is yields are higher compared to other fixed
7 income.
8 There is a lower fee structure compared
9 to other alternatives so this isn't a 2 and 20 fee
10 structure that you typically see in venture or
11 private equity. So when combined with other
12 alternatives, you are actually lowering your
13 cumulative fees. The duration is smaller. We
14 talked about that floating interest rate component
15 on a quarterly basis.
16 Additionally, private debt shortens the
17 J-curve. What I mean by that is when you invest in
18 private equity you typically don't see a return for
19 maybe three, four five years. When you invest in
20 private debt, you start receiving distributions or
21 yield on that loan almost the quarter after or very
22 soon after you make that investment. You start
23 seeing a return almost immediately.
24 And then there is strong diversification

1 when complimented with other investments that
2 investors typically have in their portfolio. Like
3 high yield, like investment grade, like private
4 equity.
5 Going to the next slide, this slide
6 highlights diversification and yield benefits
7 particularly relative to other asset classes.
8 Looking at the numbers at the beginning
9 of this week, high yield bonds were yielding around
10 5.6 percent. The Barclay's Aggregate Index was
11 yielding around 2.4 percent. You actually had to
12 go all the way down on the rating scale to Triple C
13 rated bonds to find a comparable yield, which is
14 yielding 8.2 percent, and I will explain later.
15 Triple C rated bonds are not only lower
16 in quality to private credit but they are also
17 subordinate to capital structure. In claims and
18 instances of bankruptcies or default, they do not
19 have first claims on assets and cash.
20 Last, while yields are strong relative to
21 other asset classes, private credit also offers
22 strong diversification benefits. The asset class
23 historically provided strong diversification
24 against cash. The highest rated bonds being

1 investment grade and treasuries.

2 I think maybe the most interesting

3 correlation chart on the bottom right is to

4 syndicated debt, which is those loans to the

5 largest companies in the U.S., those large cap

6 companies and syndicated debt has a correlation of

7 .66. Still relatively low correlation to a similar

8 asset class.

9 As you can see, when you're

10 complimenting, when you are adding private debt to

11 an existing portfolio, you are adding

12 diversification benefits and reducing your

13 volatility.

14 The next slide. Quickly on this one,

15 this is actually data going back to 1992. It is

16 looking at technically the worse rolling five year

17 period for each asset class.

18 As you can see, the only two asset

19 classes that had positive performance as a

20 technical worse drawdown, were private debt and

21 private equity.

22 I will say we're updating this to include

23 Q1 and Q2 2020 data. You would see this theme hold

24 true. They are really the most challenging zero

1 revenue environment that we saw in the Covid
2 environment. This theme continues to ring true.
3 I won't spend too much time on this one.
4 This is comparing private credit defaults and lost
5 rates to syndicate the debt so that is the largest
6 companies in the U.S.
7 As you can see, you have lower default
8 rates, higher recovery rates, and subsequently
9 lower lost rates. It is protecting on the down
10 side in the worst case scenario owes.
11 The next four slides or so highlight the
12 backdrop that is driving the growth of the private
13 debt market.
14 Since 2010, the banking industry has
15 consolidated considerably. Today there is about
16 5000 to 5100 banks in the U.S. There is actually a
17 three year hiatus of new bank starters from 2010 to
18 2013 so no new banks were created at that time.
19 Additional scrutiny on the banks from the
20 fallout of the GFC, which included greater capital
21 requirements needed by the banks.
22 But one of the biggest directives came
23 from the Office of the Comptroller on currency on
24 leverage practices by individual banks. Which

1 stated that the banks should not lend to companies
2 beyond a four to one total debt to net income ratio
3 so it limited the amount of risk that banks could
4 take and wanted to take.
5 Banks have really changed their business
6 model to focus on other parts of the business and
7 gotten out of the middle market lending practice.
8 That void and that vacuum has been filled by
9 nonbank institutions and investment managers that
10 are picking up the slack and lending directly to
11 these companies.
12 As a result, today there is over 800
13 billion in the asset class. There is probably
14 about 200 to 300 nonbank private credit lenders in
15 the market today picking up the slack for the
16 banks.
17 On the next slide, this slide highlights
18 bank participation in the leverage loan and
19 syndicated debt market.
20 This market used to be controlled by
21 names like J.P. Morgan, Morgan Stanley, Goldman
22 Sachs. While they still do participate in it, they
23 don't control the market in a way that they used
24 to. As you can see, it is below double digit

1 participation. That reiterates that the banks
2 continue to pull away from this market.
3 The next slide. This slide quickly
4 compares the markets that banks still participate
5 in versus where the private credit managers focus
6 on.
7 Simply put banks are willing to lend
8 against assets like property plans and equipment.
9 Those are loans that are easy to value. They have
10 an advance rate. If they have a piece of equipment
11 that is worth $100 million, banks are willing to
12 lend 80 percent against that $100 million so they
13 are willing to give a $80 million loan that is
14 backed by the equipment. Worst case scenario, if
15 the lender were to default on that loan, the bank
16 would then own that equipment.
17 Where today, nonbank lenders focus on
18 cash flow lending where they are willing to lend
19 net income typically in the range of four, five,
20 six times net income.
21 On the next slide, I think one of the
22 questions that we often get is that private credit
23 has grown significantly in the past ten or so
24 years. Is it saturated and how much demand is

1 left?

2 This chart shows that private credit we

3 believe has plenty of room to grow. You do see a

4 growth.

5 As a rule of thumb, a private equity

6 backed leverage buyout is typically financed with

7 40 to 50 percent debt and about 60 to 50 percent

8 equity.

9 So with the booming M&A markets, there is

10 a need for this private debt lending capital.

11 Additionally, on the right, you will see

12 that there are about one trillion dollars of

13 leverage loans that are maturing in the next four

14 or five years.

15 The fact that the banks will not be

16 accessible to many of these companies and borrowers

17 will cause them to go the direction of private

18 credit booming that market and continuing to push

19 up that demand.

20 I do want to underscore that demand from

21 private equity managers to finance their deals will

22 continue to drive this market as long as M&A is

23 booming, private credit will still have plenty of

24 room to grow.

1 The next slide is really a continuation
2 of the previous slide. Just looking at the amount
3 of debt and equity in most recent private equity
4 deals.
5 One of the fallouts from post-Covid
6 environment was that private equity managers to
7 finance their deals or to acquire a company were
8 putting in significantly more equity versus debt in
9 their deals. Almost 70 percent equity 30 percent
10 debt.
11 As a borrower or as a lender, that should
12 be very comforting knowing that you have 70 percent
13 equity behind you in a deal to support you in a
14 worst case scenario. So the deal has to fall by 70
15 percent before the loan itself is impaired. The
16 equity would get wiped out if the company were to
17 lose value by 70 percent but the loan will still be
18 intact. That is a very comforting and strong
19 downside protection for individual lenders in this
20 space.
21 On the next slide, I want to talk about
22 the way we have been kind of structuring portfolios
23 and thinking about building portfolios for clients
24 as they are making allocations to private credit.

1 So we have begun to build-out a number of
2 private credit allocations for clients. Last year
3 we made about 60 to 70 dedicated private credit
4 allocations for clients who were approving
5 allocations and making their first allocations in
6 this space.
7 Those ranges were typically going from
8 about 3 to 8 percent of their portfolio has been
9 dedicated to private credit. About 50 to 70
10 percent of that 3 to 8 percent, we have been
11 allocating to senior sponsor back direct lending
12 strategies.
13 What I mean by sponsor back, those are
14 companies that are owned by private equity
15 managers. So that is when you hear the term
16 sponsor back, that is what that refers to.
17 We like these allocations because
18 managers can get money invested quickly and very
19 prudently and earn on average about 6 to 8 percent
20 returns on an annual basis and take advantage of
21 the yield and structure premiums I spoke about,
22 which is why we consider them a core allocation,
23 that green bar at the top.
24 For complimentary allocations, we

1 consider a number of different strategies that have
2 a different risk structure. Typically target
3 higher returns. And those asset classes are things
4 like mezzanine or junior debts but behind senior in
5 the capital structure. Specialty finance, distress
6 and opportunistic debt.
7 We believe that sponsor backs, those
8 loans to private equity backed companies, are an
9 all weather strategy and a core allocation to
10 private credit.
11 We believe that 2020 in this past cycle
12 proved out these strategies and performed very
13 strong in really the most challenging environments.
14 On slide 15 here, this is our market
15 segmentation slide. The managers on here might not
16 agree with the way I panned them out but this is
17 the way that we view them from our perspective and
18 every manager is different.
19 There are different risks and reward
20 expectations, depending on where you focus on in
21 the market. If you're junior, senior, if you are
22 middle market, upper middle market, which is why at
23 Marquette we try to speak to as many managers as
24 possible to understand where they fit in in those

1 risk and return expectations and try to find a fit
2 with managers and our clients with their risk and
3 return expectations.
4 Going to 16, we can skip over this one.
5 TRUSTEE CONYEARS-ERVIN: That is
6 interesting that these names look familiar with our
7 last RFP that we did with the upper middle market.
8 It was just something I just noticed.
9 MR. GRAFFY: This is a small segmentation
10 but just kind of a visual map of where we think
11 that these managers perform best and where their
12 specialty or focus is.
13 When you did that search, a lot of these
14 managers showed up, which is good because we
15 consider some of these to be really the best
16 managers in the space but there is no shortage of
17 managers. A lot of them do very similar things,
18 which is important when you're looking at these
19 managers understand both the qualitative and
20 quantitative metrics so you differentiate between
21 two similar like managers.
22 TRUSTEE CONYEARS-ERVIN: Okay.
23 MR. GRAFFY: We can actually go to the
24 Fund and Capital Structure slide. This highlights

1 individual company's capital structure and how to
2 think about returns depending on where the strategy
3 focuses in the capital structure.
4 I think it's important to mention the
5 components of return for these loans so where the
6 return is coming from.
7 There is really two main parts to think
8 about that and the first one is the original issue
9 discount. That is just a convoluted way of saying
10 it is the discount that the debt issuer, debt
11 originator, received for financing a loan so it is
12 really a finder's fee for finding a company that
13 needs capital.
14 In today's market, managers receive about
15 the 1 to 2 percent discount. For a million dollar
16 or two million dollars to 1 to 2 percent fee for
17 originating that loan.
18 Second is the spread or yield of the
19 loan. So for senior secured loans, so that
20 Carolina blue I would say is the color, yields
21 range from LIBOR plus 4.5 percent to LIBOR plus 6
22 percent, that is a very conservative range.
23 Obviously, for more complex deals, that
24 number can go higher but in today's market there is

1 a lot more floor. A lot more floor starts at about
2 1 percent. 1 percent plus that 450 basis points or
3 600 basis points you are looking at about 5 and
4 half percent to 7 percent yields on a very
5 conservative average.
6 For unlevered senior secured deals, we
7 expect around 5 and a half to 7 percent returns.
8 What these managers end up doing is
9 putting leverage at the fund level to increase the
10 returns. Anytime anyone hears leverage begin to
11 ask questions and this is something that we keep a
12 close eye on.
13 It is common in the marketplace. A
14 majority of these managers have leverage at the
15 fund level. For a conservative in today's market
16 it is about one-to-one leverage. For each dollar
17 of equity that an investor puts in, they will
18 leverage that dollar and get another dollar so
19 purchasing power increases. That typically
20 increases the target returns for these funds to be
21 anywhere from about 8 to 10 percent with leverage.
22 Just important to highlight and note there.
23 Talking about risk, it wouldn't be fair
24 to talk about an asset class without highlighting

1 some of the risks involved. I won't name them off
2 but these are certainly dynamics to consider when
3 reviewing managers and thinking about risks
4 involved with certain strategies.
5 I think the first and last point here, in
6 the market environment that we were recently in,
7 and what I mean by that is Q1 and Q2 2020 and that
8 challenging zero market environment, has pushed
9 back against some of these risks.
10 How managers and strategies perform
11 against the backdrop of Covid will be something
12 that every manager will be compared against for the
13 next several years. It is a very important data
14 point and something very important to focus on.
15 This is where you differentiate the underwriting
16 discipline between each manager and how much risk
17 they are actually taking on.
18 The next slide. I won't reiterate this.
19 This highlights the benefits of adding private
20 credit that we talked about earlier on. Those
21 benefits are returns, correlations, yields, risk
22 mitigates, et cetera.
23 And then, finally, on this slide, this is
24 just, without naming names, highlights some of the

1 names that we are currently allocating to or are
2 proposing or reviewing on behalf of clients.
3 I am pretty proud to say we have done a
4 good job developing relationships in this space and
5 finding attractive managers. This year and last
6 year we covered hundreds of different managers and
7 even more strategies.
8 Lastly, fees are incredibly important and
9 in an asset class where the difference or the delta
10 between the spread between top and bottom quartile
11 managers is relatively low compared to private
12 equity or venture capital, which can be in some
13 cases a 20 or 30 percent difference. Fees are a
14 true differentiator. We try to take advantage of
15 where we can to get things like first closed
16 discounts. We have been able to negotiate fee
17 reductions with managers on behalf of our clients
18 but that is an area of focus for us drawing those
19 fees as low as possible on behalf of our clients.
20 Finally, on the last slide, this hits on
21 those high level points driving the growth and the
22 attractiveness of the asset class.
23 We were very bullish on private debt
24 prior to Covid and even going through Covid we were

1 happy to see that the asset class performed well.
2 Driven by currently a low rate environment in the
3 search for yield, the discussion around private
4 debt has only grown, especially the past six or
5 nine months. The asset class has only become more
6 attractive.
7 We believe against the backdrop of
8 potentially rising rates, having a floating rate
9 nature or potentially rising inflation, that this
10 asset class only remains more attractive.
11 Knock on wood, hopefully, the activity
12 that we have been able to build upon in 2020 and
13 2021 continues.
14 Once, again, hitting on those points
15 complimented to existing allocations in your
16 portfolio, we think private credit makes a strong
17 compliment to what you are currently doing.
18 I know that was a lot of information and
19 a lot of slides. We went over it quickly. I am
20 happy to go back and answer any questions out
21 there. We are happy to go back and hit on any
22 point or slides. Happy to answer questions.
23 PRESIDENT DEGNAN: Anybody have any
24 questions?

1 MR. WESNER: We are available for online
2 discussions, too. A lot of information to digest.
3 Take it in the context of what we were discussing
4 previously in terms of your asset allocation.
5 It actually is going to play nicely into
6 the next conversation we are going to have with one
7 of your existing managers and your existing high
8 yield manager who has expertise in all of the
9 public related areas that Brett was just
10 discussing. It is kind of a very timely
11 conversation.
12 A lot of acronyms, a lot of nuances, to
13 this investment class. If you jotted any of this
14 down, let us know. We are happy to have a followup
15 conversation.
16 PRESIDENT DEGNAN: Thank you, Jamie.
17 Thank you, Brett.
18 MR. GRAFFY: Thank you so much for the
19 time.
20 PRESIDENT DEGNAN: Our next presentation
21 is from representatives from MacKay Shields.
22 MR WOLFF: Today we are joined by Therese
23 Hernandez, who is a Managing Director in
24 Institutional Business Development. Also, Andrew

1 Susser, who is the Executive Managing Director of
2 the High Yield team. Joseph Maietta, who is a
3 Managing Director of the High Yield team.
4 MS. HERNANDEZ: Thanks for having us here
5 today. Nice to see everyone.
6 I am in Client Services and Marketing. I
7 am based in Chicago. I have with us Andrew Susser
8 and Joe Maietta, who are together in our New York
9 office.
10 Andrew Susser is our Lead Portfolio
11 Manager on our high yield product, which we have
12 run for you. Joe Maietta is a Client Portfolio
13 Manager that works closely with Andrew on the team.
14 I will turn it over to Andrew and Joe and
15 they are going to give you an update on the fixed
16 income markets.
17 Please, ask questions at any time and let
18 us know if you want us to cover something that we
19 are on topic with. Thanks.
20 MR. SUSSER: Good morning. I generally
21 will be talking about the fixed income markets but
22 I should preface it by saying I am not an
23 economist.
24 Our strategy focuses on high yield bonds

1 and bank debt but we're very much credit specific
2 bottom up investors so we don't bring in a macro
3 overlay. Even more, I don't have that expertise.
4 I don't know actuarially how you would think about
5 things from a pension but I was asked to give my
6 thoughts, our thoughts, on the fixed income
7 markets.
8 I have an IRA so sometimes I think about
9 long-term investing, too.
10 I think it's important to just step back
11 and think about the world that we live in today
12 even with the higher interest rates.
13 Yields are extraordinarily low. We have
14 had a huge boom market in bonds for over 40 years.
15 Interest rates are near the lowest they have been
16 in thousands of years. And so stepping back that
17 should be something that you really think about as
18 you are investing your portfolio that we're in a
19 very odd time of very low interest rates.
20 I mean, all of a sudden it has become
21 normal to have negative interest rates in Europe
22 and Japan, which I didn't think was very possible.
23 If you are looking at the Barclay's
24 Aggregate, which is what most core managers are up

1 against, you're looking at a yield of 1.8 percent
2 gross of fees which the index is and then showing
3 the S&P 500 yield is 1.4. That's not a lot of
4 yield in this environment and this environment is
5 very extraordinarily strange.
6 To make matters worse, in terms of the
7 yields today and interest rates today, is the real
8 interest rate or the interest rate after you take
9 into account inflation, on the next page, Page 3,
10 so the yield after inflation.
11 Obviously, if you have $100 and all of a
12 sudden everything costs 10 percent more, your $100
13 isn't really worth $100. It's historically been
14 very unusual to have negative real interest rates
15 because it gives an incentive for everyone to
16 borrow money because if you can borrow money at
17 less then the inflation rate you should borrow lots
18 of money. So it is very unusual that we had
19 negative interest rates.
20 One of the things that has changed
21 recently is that inflation has jumped up, which
22 everyone obviously knows, and this was always a
23 risk for a long time and people were comforted by
24 Chairman Powell's words. But I wonder whether

1 there is not a set change with the velocity of the
2 inflation that we are seeing and his shifting
3 comments and then the question is how confident in
4 the markets that it can be controlled.
5 As I said, I am not an economist but it
6 is something that certainly should worry long term
7 investors given how we are starting out at such low
8 interest rates as we start.
9 Moving forward to inflation, on Page 4, I
10 think you all, if you eat or buy almost anything,
11 you realize that there is a lot of inflation in
12 terms of cost push. So commodity prices, labor,
13 inflation, which is good. As well once expectation
14 of inflation have started to rise. Listening to
15 conference calls nearly every company is talking
16 about how they are going to be putting in
17 inflationary increases because there is so much
18 demand facing not enough stuff people are able to
19 get those inflationary increases accepted by the
20 buyers at least for the timebeing right now.
21 Again, that is something that is worrying
22 longer term, if you are a fixed income investor,
23 your upside is limited. So that is something that
24 certainly I think is something to think about.

1 And then if you sort of think about the
2 things that have been helpful for inflation,
3 globalization was helpful for inflation and now we
4 have kind of have deglobalization.
5 The horrible crisis happening in Ukraine
6 is very inflationary in terms of Russia is a big
7 exporter of wheat. People are going to be more
8 focused on their supply changes. Russia is also a
9 big energy producer. All of a sudden freight and
10 everything else is going to cost more money. I
11 think that is something to sort of think about if I
12 were in your shoes on thinking long-term about
13 investing.
14 Now, one of the risks that we do have by
15 the higher inflation, if interest rates go up, your
16 fixed income portfolios can lose a lot of money.
17 Just, on Page 2, you can see what this is
18 a measure of how sensitive to interest rates the
19 different markets are. The black line is the
20 Barclay's Aggregate or your typical core portfolio
21 and you can see that the duration or the interest
22 rate sensitivity has gone up to 7.3 years.
23 If interest rates go up 1 percent, the
24 Barclay's Aggregate would lose 7.3 percent, that is

1 what that 7.3 means. If the interest rates would
2 go up 2 percent, all of a sudden the core portfolio
3 would be down 14 percent all other things being
4 equal.
5 And you can see that, of course, the blue
6 line, that is what we do, the high yield bonds, the
7 duration is four years and it has not actually been
8 trending down because the coupons are bigger and
9 the maturities are shorter in high yield bonds.
10 Generally, high yield bonds have
11 performed very well during periods of inflation
12 because generally it means the economy is doing
13 better.
14 If you think about high yield bonds as
15 sort of a mix between core fixed income bonds and
16 equities, if the economy is doing better and
17 interest rates rise, that means that the overall
18 credits are doing better within the high yield
19 universe and so high yield has typically done
20 fairly well during inflationary times.
21 We have a chart on Page 5 that shows
22 periods when interest rates rose and how high yield
23 performed.
24 MR. MAIETTA: Just to give some

1 historical contents, if you look on Page 5. What
2 we did here is over the last 20 years, we looked at
3 periods where the 10-year U.S. Treasury increased
4 by more than 100 basis points and then we included
5 various fixed income indices and looked at their
6 performance over that timeframe.
7 Right now you're looking at seven
8 distinct periods. The most recent of what occurred
9 after the Covid recovery just until the end of
10 January.
11 When you look at kind of more spread
12 sensitive sectors that have typically more equity
13 beta, which should do well in a rising rate
14 environment, the economy is doing well. That is
15 mostly U.S. high yield, leverage loans and emerging
16 markets. This emerging market includes both
17 developed and sovereign bonds.
18 On the right-hand side, you have more
19 interest rate sensitive types of fixed income
20 securities.
21 What you will notice here in the trend is
22 essentially the higher spread asset classes, such
23 as U.S. high yield and loans, typically do better
24 in a rising rate environment.

1 As Andrew mentioned, they have less
2 duration which means they have less duration
3 sensitivity. They have higher coupons which should
4 insulate you from rising rates. They typically are
5 refinanced at rising rates. That is beneficial
6 over the long-term and if you compare that to more
7 duration sensitive investment grade and global
8 aggregate type investments, which typically have a
9 duration of seven to ten years, those generally do
10 slightly underperform in these types of
11 environment.
12 High yield loans are typically places
13 where investors will look to decrease the duration
14 in their portfolio given those attractive factors.
15 But one thing we do caution is given the overall
16 spreads in both high yield and loans, this type of
17 benefit will probably be less so in the current
18 environment.
19 Looking at spreads for high yield, they
20 are approaching 400 basis points historically below
21 average levels of high yield historically which
22 tends to be a range between 500 to 525 basis
23 points.
24 The good news in terms of high yield is

1 that the quality of high yield has increased pretty
2 significantly over the past couple of years as it's
3 been somewhat of an orphaned asset class.
4 When you look on Page 6, what we did here
5 is we looked at the growth of some pretty popular
6 credit asset classes on Page 6. We looked at
7 private debt leverage loans, investment grade and
8 U.S. high yield.
9 The one big takeaway from this slide is
10 private debt, leveraged loans and environment grade
11 to a degree have seen a very large increase since
12 the Global Financial Crisis as there has been a
13 fair amount of demand for those types of assets,
14 those types of fixed income securities.
15 When you look at high yield, just before
16 2020, where you had a slightly large increase
17 mostly due to some of the investment grade names
18 that were downgraded to high yield, high yield was
19 actually decreasing in an asset base for a number
20 of years.
21 So what that has done is that has led the
22 investor base for high yield to become more
23 strategic investors. Institutional investors such
24 as yourself. More discerning printed underwriting

1 and more higher quality companies coming into the
2 higher market.
3 The biggest takeaway there would be on
4 Page 8, which it is a pretty clear chart. What
5 this is giving you is the percentage of double BBs,
6 which would be the highest quality companies in
7 both the high yield and loan index as a percentage
8 of the market overtime. Over the last 10 to 12
9 years. There has been a pretty big dispersion
10 between high yield and loans or even private debt.
11 While high yield higher quality companies
12 have gone from about 45 percent and now closer to
13 57 percent, the lower market has actually decreased
14 to 50 to 34 percent.
15 Some of those factors are due to high
16 yield being more strategic, more institutional
17 investors and the low market being a little more
18 focused on CLO creation, non-institutional buyers
19 and being more favored by LBO and private equity
20 sponsors.
21 I think the long-term in terms of high
22 yield is the credit quality is good. Overall the
23 fundamentals are strong as well and valuations are
24 fair given the market.

1 MR. SUSSER: We just talked. We were
2 weren't quite sure. What should we have been
3 talking about?
4 MR. WESNER: I think the latter part of
5 that conversation was certainly consistent with
6 what the Trustees have recently been discussing in
7 terms of asset allocation. Kind of your exposure
8 to high yields and to bank loans.
9 Maybe just a question with the chart that
10 is on the screen now given that the mandate you
11 manage for this Board in high yield has been a
12 shorter duration, higher quality mandate, and that
13 you have seen the universe within high yield become
14 more high quality, what impact does that have on
15 the way you manage the portfolio? Does it affect
16 how you view the mandate that you are investing for
17 the Municipal Fund?
18 MR. SUSSER: We manage to a broad based
19 high yield index but your portfolio has a 10
20 percent maximum on Triple C so that has always been
21 in the back of our mind as we are thinking about
22 allocating as well as for your account to try to
23 have more liquid investments in case cash is
24 needed. Your account also doesn't want to hold

1 restructured equities. Those are supposed to be
2 sold and other places hold on to them.
3 So, in terms of the account, it is in
4 very good shape right now generating a good income.
5 It has held up well this year with very rising
6 interest rates because it has had a shorter
7 maturity and I think we haven't had any issues with
8 managing it at all.
9 MR. MAIETTA: In terms of the rising
10 rates that we have seen over the last couple of
11 weeks, the volatility, has that changed any
12 thoughts about where to put money?
13 MR. SUSSER: We're in a situation now
14 where there is a lot of bonds now that are at
15 discounts and so all of a sudden there is a lot of
16 bonds that are on sale and ones where you have
17 upside in case the company gets bought or something
18 good happens. The average Triple C backed eight,
19 nine months ago was par. To give you an example,
20 it is normally in the high 80's and now it's gone
21 back down to 95, which is not great but it is
22 certainly better.
23 We have been looking for bonds that are
24 at a discount that do have that upside for your

1 portfolio and then rolling into this year we were
2 looking for bonds that were very unlikely to go
3 down no matter what because the upside downside
4 didn't make a lot of sense. Just clipping a coupon
5 seems to be the best real value.
6 In terms of the private debt, if you look
7 at high yield, there is a lot of big public
8 companies in high yield. Companies like Charter
9 Communications the second largest cable company in
10 the United States. HCA the largest hospital
11 company. MSCI which gets money from a lot of the
12 indexes that it has. Hilton Hotels.
13 So about 25 percent of the high yield
14 markets are public companies in the S&P 500, that
15 have high yield because they have a little bit too
16 much debt but they are pretty good credits.
17 The riskier companies, the companies that
18 have taken on a lot of debt for LBOs, often private
19 companies, are in the institutional long-term
20 market. That is why that credit quality has really
21 gone down in the institutional market. The direct
22 lending is much greater than it has been. There is
23 a ton of money chasing not enough middle market
24 ideas and so that area is certainly flashing red in

1 terms of what I would worry about going forward.
2 While it is true that private debt worked
3 very well during the pandemic, the composition of
4 that market is much more highly levered small
5 companies that are usually in kind of growth areas.
6 Like tech, healthcare services, things like that.
7 And that economy has done very well over the past
8 decade. So we haven't been through a tougher
9 recession to pressure a lot of the smaller
10 companies that people don't care as much about.
11 But I am the high yield public person so perhaps I
12 am biased.
13 MR. WOLFF: Do you have any other
14 questions from the Trustees?
15 PRESIDENT DEGNAN: Thank you, Andrew.
16 Thank you, Joseph. Thank you, Therese.
17 I believe our next representative will be
18 from Walter Scott.
19 MR. WOLFF: We have Roy Leckie. He is
20 the Executive Director of Investment and Client
21 Services. Also Francis Sempill who is the head of
22 Client Services.
23 MR. SEMPILL: Thank you, very much for
24 the opportunity to meet with you today just to give

1 you an overview of why international and
2 consideration for looking a little bit wider
3 outside of the domestic market.
4 I am going to drive the presentation.
5 Roy is going to do the majority of the talking but
6 we would love to take questions as and when you
7 have them. Obviously, we will leave plenty of time
8 at the end for Q & A as well.
9 I will pause there and hand it over to
10 Roy and we will go through the presentation as we
11 can.
12 MR. LECKIE: Thank you, Francis.
13 Just by way of introduction, my name is
14 Roy Leckie. I am a Director of Walter Scott. I
15 have been with the firm for 26 years and have been
16 very involved in both our investment management but
17 also our client relations. So thank you for this
18 opportunity to just present to you this afternoon.
19 We have a saying in Scotland, I don't
20 know if you have ever heard it. Which goes you
21 can't teach your granny to suck eggs. What it
22 means is don't try and teach people things they
23 already know.
24 I am a little bit worried. Much of what

1 I am going to say this afternoon will be well-known
2 to you. I apologize in advance if that is the
3 case.
4 Obviously, our plan is to state some
5 facts about international investing, investing
6 outside the U.S., give some perspectives on it.
7 And, obviously, I think it is so important that we
8 make some comments about the current issues and
9 current challenges.
10 So with all of that, Francis, Page 3 sets
11 out the agenda and the bios. If we move on from
12 that on to the next page to international
13 investing.
14 So, in our world, in the investment
15 world, international investing is also known as
16 EAFE, EAFE investing. So EAFE is standing for
17 Europe, Australasia, and the Far East. It is
18 really the developed world outside of North
19 America. The developed world invests in the
20 universe outside the U.S. and Canada.
21 You can see in this first table here, how
22 the EAFE index as constructed by Morgan Stanley
23 Capital International, MSCI, which is the main
24 index provider around the world, how it allocates

1 across the EAFE universe. These are all the
2 countries in EAFE. You can see that the biggest
3 exposures, Australia, France, Germany, and U.K.,
4 They obviously are the biggest economies in the
5 EAFE universe. And, therefore, account for the
6 highest weight.
7 To be clear, this is what is called a
8 market capped weighted index as opposed to an
9 economy weighted index. But there is a broad
10 correlation, the size of the economy and the size
11 of the stock markets.
12 That is just the EAFE or the
13 international investments universe list. On the
14 right-hand side, the second table, I have done a
15 comparison here on the sector allocation of the
16 EAFE index as compared to the market, that I am
17 sure you know well the U.S. market. And you can
18 see that the big industry differences, not a huge
19 surprise, much less of a technology exposure in
20 international markets relative to the U.S. The
21 European market has more financials, more
22 industrial exposure.
23 That is just to give you a little
24 snapshot of the exposures as opposed to the

1 international investment universe. The universe
2 that we stock pick from on your behalf and just the
3 state of the line there.
4 Moving on, Francis, on to the next slide.
5 This is a really, really important slide. It is
6 actually kind of particularly important for Walter
7 Scott's investment philosophy, our core investment
8 beliefs. Our investment philosophy is built around
9 this relationship.
10 What it shows is the clear relationship
11 between share prices and profits. What we have
12 here is the EAFE Index, the international equity
13 index, in blue, and then the profits or profit per
14 share of the constituent components. The aggregate
15 companies. The aggregate profits from the
16 companies in the index.
17 What you can see is that over the
18 long-term what drives share prices, what drives the
19 index performance, is the amount of profits that
20 the companies make.
21 There are lots of theories and lots of
22 commentary at all times and noise around what
23 drives prices. Whether it is interest rates or
24 sentiment around wars or disruption. Whether it is

1 earnings expectations and whether earnings come in
2 above or behind consensus. Politics. Geopolitics.
3 Lots of things share prices in the short-term but
4 over the long term the overwhelmingly most
5 important thing that drives share prices in the
6 EAFE universe and indeed any investment universe is
7 the amount of profits that the companies generate.
8 This shows over any reasonable period the
9 thing you must focus on. When I say this relates
10 to Walter Scott's investment philosophy, we're in
11 the business of trying to find companies. Those
12 companies that can grow sustainably their profits
13 at above average rate over the long-term because we
14 know that the share prices while most volatile over
15 short time periods that is what will drive returns
16 over longer term periods.
17 That's why I show this. Just that the
18 EAFE market, the EAFE investment universe, is the
19 same as every other market, every other company,
20 profits over the long-term are what really count,
21 profit growth.
22 So next slide just some characteristics.
23 Again, putting things into perspective. The EAFE
24 universe in an economic sense is actually a very

1 similar size to the U.S. The U.S. economy is a $23
2 trillion economy. The EAFE landscape is a $27
3 trillion economy. Pretty similar. Both account
4 for about one quarter of global GDP of the global
5 economy.
6 The next slide down is quite interesting.
7 The total size of the U.S. stock market is $72
8 trillion, that is a typo there. So the U.S.
9 stockmarket is very considerably larger than the
10 underlying economy. While in the EAFE universe,
11 the economy and the stockmarket are very similar
12 sizes.
13 There is a range of different theories
14 about why that is. Some people just say that this
15 is indicative of the fact that the U.S. markets is
16 very highly valued, indeed possibly overvalued.
17 Others will say, well, it is really down to the
18 fact that the U.S. economy is much more
19 entrepreneurially dynamic. There is much more
20 company formation. We start businesses much more
21 frequently. Many of which go on to be hugely
22 successful. That is why the U.S. stockmarket is so
23 much bigger.
24 There are of course many foreign

1 companies listed in U.S. stockmarket included in
2 that number as well.
3 Further down, just some profitability
4 characteristics. Best return on equity. The U.S.
5 and market is more profitable in aggregate than the
6 EAFE or the international investment landscape.
7 Again, there is a range of theories
8 around that. Some people say we have better
9 management in the U.S. or we have better companies.
10 I actually think its less that, to be honest, and
11 it's more a case of just it goes back to that
12 sector allocation. It is the structural
13 differences between the two markets.
14 So while the U.S. is a lot of technology
15 companies which tend to have very high returns on
16 equities and low capital requirements tend to be
17 quite profitable. Whereas, in Europe and Japan,
18 there is a lot more industrial companies. A lot
19 more financial companies which are structurally
20 lower profitability enterprises. I think that
21 speaks to that.
22 Just the next on the bottom two, just a
23 PE ratio which is very common and easy to calculate
24 metric for valuing stockmarkets relating the price

1 to the profits of companies or markets and then
2 dividend yield. I think this is a really important
3 point at the moment.
4 A lot of people are saying, well, look
5 the U.S. market in PE terms or dividend yield terms
6 is at extremes. It's extremely expensive today
7 relative to international markets. I think that is
8 a very key reason why international investing is
9 becoming I think a lot more interesting to U.S.
10 investors at the moment.
11 On to the next slide, this just shows the
12 historical performance of international investing
13 versus U.S. investing. This is rebased to 1969
14 when these indices started and just to be clear
15 they are both in the same currency. Both in U.S.
16 dollar terms.
17 You can see for long periods the
18 international index was doing better and then if
19 you look right towards the right-hand side of the
20 chart you can see that the last decade or so the
21 U.S. has done considerably better than EAFE.
22 Start to finish, the U.S. market has
23 compounded at about 8.7 percent per annum while the
24 international or EAFE index is compounded at 7.7.

1 Most of that gap as I say has just come
2 in the last decade or so. I think just a general
3 point to make on this is again while markets,
4 stockmarkets, don't go up in a straight line and
5 there is clearly volatility in both of these lines,
6 the general trend is bottom left, top right.
7 I mention that just trying to emphasize
8 the power of equities. Over short time periods
9 equities can be volatile. They can be
10 unpredictable. Over the long-term, they are a
11 very, very reliable asset class for building wealth
12 and building wealth at rates ahead of inflation.
13 They are a great kind of vehicle for
14 capturing the general propensity of economies to
15 grow and living standards to rise and new
16 technologies and new ideas to come to the
17 forefront.
18 That is why Francis and I have got such
19 great jobs. We have a front row seat. As equity
20 investors, we have got a front row seat into this
21 very dynamic and rapidly changing world in the
22 knowledge that over the medium to long-term equity
23 markets go up.
24 I just don't believe, despite all the

1 challenges that we face in the world today, whether
2 it is the immediate challenges of Europe or whether
3 it is the longer term challenges of climate change
4 or inequality or too much debt or whatever it is.
5 We will face these challenges and equity markets
6 will rise through them.
7 On to Slide 8, the next one, this is just
8 the same data actually but what it shows is one
9 relative to the other. It is the U.S. relative to
10 that international markets.
11 You can see for the period from 70's
12 right through to the mid 80's international
13 investing did much, much better than the U.S. Then
14 we had a period through the 90's right until around
15 2000 where the U.S. performed a whole lot better.
16 Then we had quite an extended period between the
17 start of the century and the Global Financial
18 Crisis where international investing did much
19 better.
20 Then since 2008/2009 as the U.S. lead the
21 world both in sort of monetary support, declining
22 interest rates, combined with some just brilliant
23 and very dominant technology companies coming to
24 the forth, the U.S. has just killed it. Absolutely

1 massively outperformed. This is the thing that I
2 think a lot of investors are now considering is
3 coming to an end.
4 Next slide. One other interesting
5 characteristic about the international markets and
6 compared to the U.S. is the concentration. So you
7 can see the blue line the top here. The top ten
8 stocks, the top ten, the largest ten companies in
9 the U.S. now account for well over 25 percent of
10 the total stockmarket capitalization.
11 It is really incredible just how well
12 they have done. The European, Asian, Japanese
13 markets, much more evenly concentrated. Much less
14 concentration risk. I think in and of itself it is
15 not necessarily a bad thing to have a concentrated
16 market. What it does do, and I think this has
17 skewed the behavior of many investors, is that a
18 lot of institutional investors think there is great
19 career risk in being underweight.
20 These top ten companies, not having full
21 exposure to them. They are so dominant in overall
22 stockmarket performance that whether they like the
23 companies from a fundamental perspective, you know,
24 your Facebook, Apple, Amazon, Google, et cetera,

1 they just feel compelled to own them.
2 So thankfully we have never been in that
3 case. We will not own anything whether it is in an
4 index or not. We will only own things if we think
5 there is a fundamental case for owning them.
6 I think this concentration has been a bit
7 self-fulfilling. People feel they have to own them
8 and that just again boosts the share prices which
9 boosts the level of concentration.
10 It is an interest dynamic or
11 characteristic there that international markets
12 don't have that the U.S. does.
13 On this next slide, I won't go into this
14 in detail, again highlights the problem that the
15 U.S. market overall is very dominated by a small
16 number of very, very large powerful companies.
17 That is just a few kind of facts about
18 the EAFE Index, the international investment
19 landscape.
20 Here is a bunch of bullet points. I
21 won't go through all of them. You can read them in
22 your own time but just a kind of perspective. Some
23 of these I suppose are personal perspectives.
24 Others are just probably widely considered points.

1 But I think the first thing to highlight
2 is my belief, our belief, would also be is that
3 U.S. investors should absolutely have domestic
4 exposure and international exposure. It is not an
5 argument of one over the other. You can balance
6 the two. You can work out how much you want to
7 have. I think it makes absolute sense for U.S.
8 individuals and institutions to have exposure to
9 both.
10 The simple benefits of diversification
11 are really clear and well understood. It's just
12 common sense not to have all your eggs in one
13 basket. It is not advisable to only have
14 technology stocks. It will have served you well
15 for the last ten years but doesn't mean it is going
16 to serve you well for the next ten years.
17 In fact, it is very uncommon for market
18 leadership of any country or any sector or indeed
19 any company to last too long.
20 I am sure you have read recently about
21 the nifty fifty and how they are being compared
22 with today's market leaders. It just doesn't last
23 forever.
24 Diversification from a region, country,

1 sector perspective is the most sensible way to
2 invest for the long-term.
3 Then there is this point that is kind of
4 crucial to us at Walter Scott, investing
5 internationally gives you the opportunity to expose
6 portfolios to just many of the world's best
7 companies. The U.S. does not have a monopoly on
8 the best companies in the world.
9 There are comparative advantages in
10 Switzerland in pharmaceuticals or in France and
11 Italy with their luxury goods or in Japan with some
12 of their very high tech manufacturing processes,
13 robotics and things like that. There are some
14 amazing investment vectors like protection and
15 savings in Asia where there is this massive
16 population becoming middle class all of a sudden.
17 We start to think about saving for the future
18 rather than living hand to mouth.
19 There are some incredible companies, some
20 incredible investment dynamics, that you just don't
21 get if you retain a home bias.
22 Some people think that international
23 investing is not worth the hassle because of
24 currency risk.

Now, while we are a long way from being currency experts or currency traders, it is a simple fact, and I think it is on Page 78 of Jeremy Siegal's book "Stocks for the Long Run", that shows you that over the long-term, we would only ever advise investing over a long-term perspective in equities. Otherwise, it's just speculating. Investing is a long-term undertaking.

Currency risk comes out in the wash. Currency movements they impact diminish over time. So it is far more important what you own rather than what currency it is denominated in. Don't worry about currency risk. Don't let that put you off, if you have a long-term investment time horizon.

The point here is about U.S. markets being considerably more highly valued and expensive than European and Japanese and international markets. I think that is a really important point when thinking about allocating capital over the kind of medium term.

An interesting point, and not everyone is concerned about, but I think gradually through time everyone will be concerned about this, and that is

1 the kind of ESG, Ethical Sustainable Investing.
2 It is a fact that Europe or companies in
3 Europe, probably governments in Europe, are ahead
4 of the U.S. when it comes to factoring and thinking
5 and managing their businesses around climate risk
6 and the journey towards net zero.
7 It is being adopted in the U.S., clearly
8 it is, but at different stages and different levels
9 of enthusiasm.
10 If you care about ESG, and I think
11 everybody should to a greater or lesser degree,
12 then I do think at some point that European
13 companies, the international investment landscape,
14 might warrant a little bit of a premium relative to
15 U.S. markets, based on how they are addressing
16 these concerns.
17 MR. WESNER: Sorry to interrupt. We need
18 to be mindful of the Trustees' time. Do you mind
19 wrapping up your thoughts and maybe quickly speak
20 on the current state with Russia and Ukraine? If
21 you have a unique perspective from your side of the
22 ocean versus us and whether there is any risk that
23 you are concerned about in terms of European
24 exposures and the like.

1 MR. LECKIE: The first point is this is a
2 terrible human tragedy and it is very difficult for
3 us to be talking about it from a business and
4 economic and a stockmarket sense without
5 acknowledging that there are people dying right now
6 and it is horrible. It is really horrible.
7 That being said, what are our
8 perspectives? Do not believe anyone who tells you
9 how this is going to play out. We have no idea.
10 There is too much uncertainty and unpredictability
11 about this.
12 What we do know is that Russia is a very,
13 very small component of the global economy. One
14 and a half percent or thereabouts. Russia's
15 economic contribution is pretty limited. It is one
16 of the world's or the world's biggest exporter of
17 oil. Second largest exporter of gas. Third
18 largest exporter of coal.
19 So where there are real risks to the
20 European and the broader economic landscape is
21 around commodities and particularly energy. So
22 that is a risk.
23 So energy prices are rising and will
24 probably continue to rise while this persists. We

1 don't know how long it will last for, we don't know
2 what the end game is. We don't know what Putin is
3 thinking. I think we have to hope and assume he
4 will stop with Ukraine but if he doesn't we're in
5 big trouble.
6 Now I think he's being surprised both at
7 how resilient the Ukraine resistance has been. I
8 think he has been massively surprised at how
9 uniformed the global response has been.
10 I have never seen Europe as coordinated
11 and together as it is today. So we have an
12 incredible response both in terms of aid. There is
13 100 people from Scotland that has gone over to
14 fight against the Russians.
15 The economic sanctions are going to
16 really hurt but in terms of stockmarket contagion,
17 I actually, again, it sounds perverse, I don't
18 think there is going be that much. There is going
19 to be some volatility but I don't think this is
20 going to initiate a bear market. The European
21 economies are still going to grow. Not as much
22 they would have done because of higher energy
23 prices, but European economies will almost
24 certainly still grow at a reasonably healthy clip

1 this year as they recover from the Covid situation.
2 Walter Scott has no direct exposure to
3 Russia, that is a problem with index investing.
4 Russia is part of the emerging markets index. We
5 have no exposure and never would have. It doesn't
6 meet anywhere near our criteria.
7 I can go on at length about this, if you
8 want. Why don't I stop and ask questions, if we
9 have time constraints.
10 PRESIDENT DEGNAN: Do any of the Trustees
11 have any questions for Roy or for Francis?
12 I don't hear any questions from any of
13 the Trustees.
14 Thank you for the presentation, Roy.
15 Thank you, Francis.
16 I will turn it over to Stephen. I
17 believe our next representative is from Northern
18 Trust.
19 MR. WOLFF: Next we are going to do
20 securities lending.
21 I am going to lead off the presentation.
22 I am going to give an overview on what is
23 securities lending in general, some key statistics
24 about our program specifically, and then I also

1 have Don Anderson from Northern Trust. After I
2 finish, he is going to give an overview of the
3 securities lending market and also will be
4 available for any more detailed questions we have
5 as we go through the presentation.
6 I will mention quickly that we are going
7 to have Jamie speak a little bit about the
8 historical context for a couple of minutes as well.
9 If you go to the first slide, so what is
10 securities lending?
11 Just as a reminder, MEABF has a portfolio
12 of about $3.5 billion across a lot of different
13 asset classes. We have fixed income, equities,
14 stocks and bonds, real estate, private equity,
15 cash, all these different asset classes.
16 When it comes to securities lending, we
17 are going to focus on the stocks and bonds portion
18 of that and I have it highlighted in the left box.
19 Essentially, what we do is we lend stocks
20 or bonds to our borrowers. Borrowers are typically
21 large banks, financial institutions, prime brokers,
22 et cetera.
23 In return for leading those securities,
24 we receive two things. One was collateral and then

1 we also receive income. I will go into the details
2 of those two components in further slides.
3 Who are the borrowers? Borrowers, like
4 we said, are large financial institutions. They
5 are generally safe. They generally have high
6 quality credit.
7 The top five borrowers in our program.
8 The number one borrower is Citadel. You may have
9 heard it is based here in Chicago. Also, Morgan
10 Stanley, Citigroup, J.P. Morgan and BNP Paribas,
11 which is a French bank.
12 So why do they borrow? Well, there is a
13 couple of different reasons that they borrow. One
14 is short selling. You may have read about this in
15 the news the last couple of years around Tesla
16 stock. People shorting that stock.
17 Essentially, all this is a borrower will
18 borrow shares, for example, Tesla, sell them on the
19 open market at a certain price. Hoping the price
20 goes down in value and they can repurchase the
21 shares and return them to the persons they borrowed
22 them from and they get to keep the difference
23 between those two prices as their spread or profit.
24 That is one reason for borrowers borrowing.

1 Another is balance sheet management.
2 Sometimes financial institutions as they might
3 approach a quarter end will like to adjust the
4 amount of treasuries or bonds versus the equities
5 on their portfolios and they need to borrow from
6 institutions like public pension funds like
7 ourselves in order to adjust those ratios on their
8 balance sheets for various reasons.
9 Another reason is early settlement.
10 Typically when you trade equities or stocks, you
11 make the trade on one day and then you have two
12 days later, two plus two, where the actual trade
13 settles and you can move the cash.
14 If you want to settle that trade earlier,
15 you may borrow the shares a day or two before for
16 various reasons.
17 So when we think about borrowers we have
18 to manage risk. One of the things that we do to
19 manage risk of our borrowers is we do an extensive
20 credit check. This is run by Northern Trust, who
21 is our securities lending agent. Where they look
22 at all the financial ratios of these borrowers and
23 make sure they have the highest credit quality
24 available.

1 Also, over collateralization. As I
2 mentioned earlier, when we lend a security out we
3 receive collateral. We typically receive the value
4 of that collateral in excess of what we lent out.
5 It is typically anywhere from 102 percent to 105
6 percent of that value. That gives us a little bit
7 of cushion in case anything goes wrong with the
8 collateral and also we have daily marking. Which
9 means if the value of the collateral changes
10 overnight, we ask the borrower to make us whole
11 again. Get us back to the 102 or 105 percent. It
12 happens on a daily basis so it makes the program
13 safe and stable.
14 The final thing I want to point out here
15 is indemnification. With our securities lending
16 agent Northern Trust, if a borrower were to
17 default, or could not return the securities to us,
18 Northern Trust will step in and make up that
19 difference in value. So we have some security and
20 safety net there.
21 If you go to the next slide, I just want
22 to give an overview on the securities on loan. On
23 the pie chart on the left-hand side, you can see
24 the largest component of that pie is the blue

1 piece, which is 39 percent, that is U.S. equities.
2 If you add that to the golden pie piece or kind of
3 yellowish pie piece of 11 percent, which is the
4 global equities, about 50 percent of all of the
5 things we loan are stocks essentially or equities.
6 The other half in the orange slice, 34
7 percent, is U.S. treasuries. And then the gray
8 slice, which is 12 percent, that is U.S. corporate
9 bonds.
10 It is generally a 50/50 split between
11 stocks and bonds that are on loan.
12 To give you an idea of the size of the
13 amount that's on loan, in 2021 the average loan
14 outstanding was about $247 million of our
15 portfolio, which is about 7 percent. At any given
16 time about 7 percent of our portfolio is on loan.
17 That is going to fluctuate based on various
18 factors.
19 On the right-hand side, we have the top
20 ten securities in our portfolio ranked by earnings.
21 You notice in the top five or six names a lot of
22 these companies have recently undergone spinoffs
23 where they took a division of their companies, spun
24 it off as a new publicly traded company.

1 This is good for us because there is
2 typically a lot of demand around these companies
3 that have spinoffs and there is a lack of pricing
4 activity around the newly traded shares and the
5 post-spinoff company.
6 There is also a demand for settlement of
7 trades in the securities and this drives earnings
8 for us so we like this.
9 One specific example here, Number 2,
10 Vivendi, you may have heard of, is a large media
11 conglomerate. They recently spun off their
12 universal music group, which owns the right to Lady
13 Gaga and Taylor Swift music. That type of spinoff
14 activity is good for our securities lending program
15 and drives earnings for us.
16 If we go to the next slide, I want to
17 give a quick summary on our net earnings in the
18 program. If you look at the bar chart on the far
19 right, that is 2021. There are two components of
20 that, the orange and the blue piece. Those are the
21 two components of the net earnings. The lending
22 component is the blue piece. This is essentially
23 think about this as a fee that we receive, which is
24 based on the demand of the securities that are

1 being lent out.
2 The orange component is our investment
3 part of the earnings. That is essentially the
4 interest that we earn on the collateral that we
5 take in.
6 As you can see in 2021, it was roughly a
7 50/50 split. A little bit higher in the investment
8 side.
9 On the left-hand side of this chart,
10 2019, this is actually a partial year. MEABF
11 switched providers in this year between Citigroup
12 to Northern Trust so we don't have a full year of
13 data there.
14 The other thing I want to talk about here
15 is the 2020 to 2021 change. As you can see, the
16 income went down about 32 percent year-over-year
17 between those two periods.
18 Back in early 2020, interest rates were
19 still relatively low but they were at a decent
20 level. The collateral we were receiving were
21 earning good amounts of interest and then the
22 pandemic hit and then the Federal Reserve stepped
23 in, provided liquidity into the market, and also
24 reduced interest rates close to zero. That reduced

1 our earnings in the collateral pool over that time
2 period and that is why we see the fall off going
3 into 2021.
4 If we go to the next slide, I want to
5 talk a little bit about the collateral pool. I
6 have a lot of data on this slide so I apologize. I
7 will hit some of the highlights.
8 The collateral we received really has two
9 components. One is cash and the other is noncash.
10 The top section of the slide is the cash
11 collateral pool. As you can see in the pie chart,
12 the majority is repo agreements, commercial paper,
13 CD's, all very liquid, very short-term cash like
14 products.
15 On the right-hand side of this chart on
16 the top right, you can see that 78 percent of this
17 cash pool is in an A1 plus short-term credit
18 rating, which is the highest credit quality you can
19 receive for these type of short-term securities.
20 It is a very high quality portfolio.
21 I will also point out that if you look at
22 the maturity date, which is the far right column
23 there, 31 percent of these securities mature
24 overnight. If you look at all the securities below

1 97 days or about three months, it is about 79
2 percent of the total portfolio.
3 And then from an interest rate reset
4 perspective, about 75 of this portfolio resets
5 overnight. I think the important thing there is as
6 interest rates increase over time as we are
7 expecting, as the Federal Reserve increases its
8 target, we will be taking advantage of that. As
9 these reset overnight, we will be collecting higher
10 interest rates going forward, which is good for our
11 portfolio.
12 The key takeaways here are the cash
13 collateral pool is a very high quality, very
14 short-term low duration safe investment.
15 The other component of the collateral
16 pool is the noncash. This is typically securities
17 that are longer than a year in maturity. The
18 largest percentage here, the 62 percent in the blue
19 is the Treasury bonds, and then the red piece 32
20 percent is Treasury notes.
21 I have got the top five components of
22 that on the right-hand side. Those are third-party
23 securities that are backed by Ginnie Mae and Fannie
24 Mae which are mortgage backed securities.

1 Government back, very safe investment vehicles.
2 The takeaway here is the cash collateral
3 pool is very conservative, it is very liquid and it
4 is very high quality.
5 PRESIDENT DEGNAN: Very quickly. You
6 probably said it and I missed it. What is the
7 ratio of cash to noncash with the collateral?
8 MR. WOLFF: That is a good question.
9 Don, do you happen to know that?
10 MR. ANDERSON: I don't know yours
11 specifically off the top my head. From a program
12 level, we are at about 30 percent cash, 70 percent
13 noncash currently.
14 MR. WOLFF: Moving to the next slide. I
15 think it's important to monitor this program and
16 make sure the collateral that we receive are marked
17 at what we expect them to be.
18 So I have run the reports in Northern
19 Trust's system to look at all the cash collateral
20 that should be marked at 102 percent, it is. All
21 of the cash that should be marked at 105 percent,
22 it is marked at 105 percent.
23 Noncash items which typically range
24 between 102 and 105 percent is currently marked at

1 106 percent so that checks out.
2 I also went line by line to look at the
3 borrowers to make sure every borrower was in line
4 with our expectations and they all were.
5 I am to happy to report that the
6 collateral pool everything is in order and we are
7 comfortable with it.
8 The next slide I just want to briefly
9 touch on the Northern Trust partnership. As you
10 can see, I have a list of things that Northern
11 Trust does as our securities lending agent here.
12 They do everything from initiating the loan, moving
13 the securities back and forth, marking them daily,
14 returning the security, returning the collateral.
15 They do all of the operational aspects of that.
16 As a form of compensation of that, we
17 split between ourselves and Northern Trust that net
18 earnings or the gross earnings that we receive from
19 this program. That is kind of their fee for
20 running and maintaining and managing this program.
21 Next, I am going to turn it over to Jamie
22 who is going to give a very brief historical
23 perspective with regard to the securities lending
24 market.

1 MR. WESNER: I have also been told I am
2 not allowed to scare you talking about what has
3 happened in the past.
4 Don and I were the two back in 2008 when
5 stuff got bad in the Great Financial Crisis and we
6 saw some of the potential negative effects of
7 improperly managed security lending program came to
8 light.
9 Stephen just outlined the current
10 structure of your plan, which is an exceptionally
11 high quality plan, that is very conservative.
12 Just, again, I don't want to again scare
13 anyone. I want to lend some historical context to
14 if you hear about securities lending. Somebody
15 might say, oh, my gosh, you use securities lending,
16 why do you do that?
17 Securities lending is a way to earn some
18 excess income on the securities you already have in
19 your portfolio.
20 As Stephen was saying, you have this
21 separate account. Separate accounts with all these
22 stocks in there and bonds in there that managers
23 manage on your behalf and there is income to be
24 earned if you lend those out. In the past, the

1 earnings were even more attractive on these lending
2 programs.
3 Your former Executive Director was able
4 to come back and say we are basically paying for
5 all the salaries of our entire staff from the
6 income generated from our securities lending
7 program. It was really attractive. You also had a
8 much higher balance in terms of assets to lend out
9 as well.
10 When we started working with you in 2008,
11 you had $7 billion in assets and you were lending
12 out a higher percentage of those assets as well.
13 Where things ran into trouble back in
14 2008 is the collateral was reinvested into some
15 more aggressive securities, instead of the very
16 conservative investments that it is in now. It was
17 into more aggressive securities that had some
18 exposure to structured projects and all the
19 different things that ran into trouble in 2008.
20 You ended up having some temporary
21 impairments and some permanent impairments in terms
22 of that collateral. That then created a liability
23 essentially, or a loss almost, on the Pension
24 Fund's books that we then had to use several years

1 of income going forward for five to seven years of
2 income to repay that loss back.
3 Again, the securities lending programs of
4 today are not structured the way they were in the
5 past. Fortunately, the markets learned a lot of
6 lessons.
7 Just wanted to give you that little bit
8 of historical context so if someone says why are
9 you in securities lending, all those pros that
10 Stephen just mentioned, you still are able to
11 realize those and you have taken a lot of steps, as
12 has Northern Trust, to make sure that the cons of
13 the securities lending program are minimized.
14 They are never going to be completely
15 eliminated. There are downsize risks but they are
16 severely minimized. And even if we saw a repeat of
17 2008, your securities lending program would be in a
18 position to continue to generate income and not
19 create the liabilities that it did in 2008.
20 PRESIDENT DEGNAN: That is good to know.
21 MR. WESNER: That is probably enough for
22 this venue.
23 MR. WOLFF: Unless there is any
24 additional questions, I will turn it over to Don

1 Anderson at Northern Trust to talk about a more
2 broader securities lending market.
3 PRESIDENT DEGNAN: Sure. Welcome, Don.
4 MR. ANDERSON: Thank you, Stephen and
5 Jamie. Both of you covered things very, very well.
6 Hopefully I can add a little bit to everybody
7 beyond what the two of you discussed. I will do my
8 best to do that.
9 If we can move forward to the next slide,
10 please. What I wanted to do is really quickly go
11 through a couple of things about our program, a
12 couple things about the market and obviously take
13 any questions you have.
14 So just from the program side, we have
15 well over 460 clients participating. About $1.5
16 trillion in securities available. About $193
17 billion on loan. About a 12.4 utilization rate.
18 We run a 24-hour trading operation across five
19 different trading desks around the world. Working
20 with 73 different approved borrowers. All of whom
21 have gone through that extensive credit review that
22 Stephen mentioned that is really done on our side
23 just as though we were making loans to those
24 borrowers.

1 I already mentioned from the collateral
2 structure we are currently at a program level of
3 about 29 percent in cash, 71 percent in noncash.
4 The cash collateral that we take in on
5 your behalf is managed by Northern Trust Asset
6 Management in the fund that Stephen already showed
7 you.
8 From the top ten borrower perspective,
9 again, you will see some of the same names that you
10 saw on your list. What I will add to that is that
11 those top ten borrowers control about 68 percent of
12 the volume within our program. So a small group if
13 you will of very large organizations are still a
14 significant part of our program.
15 When we look at where things were and
16 where they are now, you will see a little bit of a
17 difference.
18 The next slide I wanted to touch on is
19 really from a relationship management standpoint
20 partnership between Northern and Municipal
21 Employees.
22 I am really truly your Client Service
23 Representative from the Securities Lending team. I
24 am backed up by Jason Woo from our Account

1 Management Team.
2 Between Jason and I, our role really is
3 to make sure that Stephen has everything that he
4 needs from his side to monitor the program, to make
5 sure that we are doing what we say we are doing.
6 Other things that we do, obviously, I am
7 before you today to present about our program.
8 Recently we helped out your auditors as they looked
9 at year end. So those are the type of things that
10 from a client service standpoint we are doing.
11 If there are new opportunities, new
12 borrowers, different types of collateral, that is
13 something for Stephen and I to discuss whether you
14 want to do different things with your participation
15 in our program.
16 What I will add is Stephen and I have
17 known each other for a long, long time. We have
18 worked together for a long, long time. I think we
19 have a very good working relationship. As Jamie
20 mentioned, he and I have also known each other for
21 a very, very long time. So we are all well
22 familiar with each other.
23 I wanted to touch a little bit on what is
24 different now relative to the financial crisis as

1 well just as Jamie did.
2 One of the big things, and you will
3 obviously see a consistent theme as I talk to you,
4 is the change from cash to noncash.
5 In 2007, as the Financial Crisis really
6 started to unfold, 80 percent of the securities
7 lending book was in cash collateral, that is down
8 to 29 percent. In June of 2007, 77 percent of the
9 lows were those top ten borrowers, it is down to 68
10 percent. We were working with 47 borrowers. We
11 are now working with 73. A much more
12 diversification within the program.
13 The other big point I wanted to make is
14 if you look at our lending base in 2007 we had
15 about $1.1 trillion. We now have about 1.5. But
16 the big key is in 2007 we were lending $294 billion
17 and now we are only lending 193.
18 So while the lendable base has gone up
19 over $400 billion, the actual volume on loan has
20 gone down $100 billion.
21 What that speaks to is the leverage that
22 has come out of the securities lending market. One
23 of the big reasons for that is how those borrowers
24 are now regulated. This really goes back several

1 years. This isn't new but Morgan Stanley, Golden
2 Sachs, the big borrowers of the world are now
3 regulated as banks. With that regulation that has
4 taken leverage out of the market.
5 One more slide, again, just on the change
6 from cash to noncash. You can see how the balances
7 have changed there over time. I don't mean to beat
8 that story into the ground but that has certainly
9 been a big story over the past few years.
10 Next just to touch on trends from both
11 the borrower side and the lender side. From the
12 borrower's side, obviously, the noncash. But the
13 other big change is that the borrowers are looking
14 for high quality liquid assets. Things like U.S.
15 Government bonds. Their regulatory requirements
16 are different so they need to hold more of these
17 assets.
18 Now as we see so much volatility in the
19 market, again, they want to hold those types of
20 assets.
21 They are also looking for different
22 routes to market. So, for example, where they may
23 be borrowing from you, they may ultimately turn
24 around and lend some of those assets to hedge

1 funds.

2 From your perspective, from our

3 perspective, our legal agreements are with those

4 borrowers. Even if they turn around and lend to a

5 hedge fund, our legal agreement still covers

6 everything. We want your security back, they need

7 to bring your security back. But they may do what

8 we call on lend it to another counter party.

9 From the lender side, from your side of

10 the equation, what clients are really looking for

11 is the opportunity to enhance returns, increase

12 revenues. And what that allows you to do really is

13 what Jamie mentioned offset other costs. Whether

14 those are staff salaries, what you pay to Northern

15 in terms of custody fees, what you pay to Jamie as

16 your consultant. However you determine to use that

17 revenue you can to help offset those costs.

18 I wanted to mention governance and

19 oversight. That is something that Stephen is doing

20 checking to make sure that we are doing what we say

21 we are doing. We are collateralizing your assets.

22 We are investing that cash as we say we are. Those

23 are the important things from the lender's point of

24 view.

1 And then lastly I wanted to touch a
2 little bit on what we have seen in the market over
3 the last year or so and what we see going forward.
4 From the cash side, as has already been
5 mentioned, we have historically low interest rates.
6 That is going to change, that is probably going to
7 change in the next couple of weeks, where everybody
8 expects the Fed to raise interest rates.
9 Currently the market has about six
10 interest rates priced in in 2022. Northern Trust
11 Asset Management believes that is actually going to
12 be a little more aggressive. Northern Trust Asset
13 Management is anticipating four hikes with the
14 expectation and I suppose the hope that inflation
15 will slow down later in the year. But, again, our
16 portfolio managers are well prepared for the rate
17 hikes that we are anticipating and as Stephen
18 pointed out we are doing that through the
19 maturities of the portfolio, the interest rate
20 maturities, that we're looking at and holding well
21 over 70 percent of the portfolio that will reset
22 tomorrow if the Fed raised rates today. We are
23 well prepared for that.
24 From the lending side of the equation,

1 the equity market in 2021 was actually pretty
2 boring until probably the last quarter of the year
3 when we started seeing a lot of volatility hit the
4 market. Obviously, we're still seeing that as we
5 are in the first quarter of 2022.
6 The other things that we kind of saw in
7 2021 we saw a lot of IPL activity. As Stephen
8 mentioned, that is always good for lending. As new
9 securities come to market, there is typically very
10 high demand as people are really trying to get a
11 good handle on where those securities are priced,
12 how they are going to trade, that drives demand in
13 the securities lending market.
14 We also saw pockets of demand in things
15 like electric vehicles, the Teslas, and other
16 companies of the world, space infrastructure.
17 From the fixed income side, what we
18 started to see really again moving towards the end
19 of 2021 and into 2022 is some pretty good demand
20 both on government bonds and corporate bonds really
21 due to the anticipated interest rate hikes that we
22 all expect to see soon. Where borrowers are really
23 positioning themselves from a short position as
24 interest rates are expected to rise.

1 With that, I will be happy to take any
2 questions about securities lending in general,
3 about our relationship with you, or anything that
4 you might like to know about.
5 PRESIDENT DEGNAN: I don't have any
6 questions, Don. I would like to thank you and
7 Jamie and Stephen for this very informative
8 presentation here.
9 Any questions from any other Trustees?
10 Thank you, Don. Thank you again, Jamie
11 and Stephen.
12 MR. WOLFF: Thank you, Don.
13 MR. ANDERSON: Thank you, very much.
14 Have a great day folks.
15 TRUSTEE CANNING: Back to the cash flow
16 for collateral, reset overnight, what exactly is
17 that?
18 MR. WOLFF: Typically in that pool a big
19 chunk of it are repo agreements, which are
20 typically very short-term and overnight securities.
21 The interest rate resets overnight. So,
22 essentially, a lot of those securities are
23 extremely short-term and that is essentially they
24 get priced I think on a nightly basically.

1 MR. WESNER: We are talking about within
2 your investment portfolio the idea if interest
3 rates go up, bond prices going down, you don't want
4 any of that collateral to be at risk to be priced
5 lower. By having those securities rollover and be
6 repriced frequently on an overnight basis or a very
7 short-term basis, when we see interest rates go up
8 and the Federal Reserve is start going to increase
9 rates likely in just the next few weeks, then you
10 nearly immediately start earning the higher rate.
11 It protects you from that interest rate risk and
12 immediately impacts your earnings in a positive
13 fashion.
14 TRUSTEE CANNING: How much earnings are
15 we talking about?
16 MR. WESNER: In the past, back
17 pre-financial crisis, this program was kicking off
18 several million dollars a year in income.
19 In Stephen's chart now, you see that now
20 the earnings are less than a million dollars but it
21 is still real money. If that offsets your fees to
22 Northern for the custodial side or Marquette's
23 management fee, it can offset a lot of different
24 things.

1 It doesn't create as much income as it
2 did in the past but you are not taking on nearly as
3 much risk as you did in the past.
4 I am sure it makes Sarah and Mary Pat
5 comfortable that we went through this educational
6 process. You know what is going on. You at least
7 understand what tech lending is. A lot of people
8 once they are exposed to it didn't know. I didn't
9 know what it was before I started working on your
10 account.
11 MR. WHITE: We had a lot more risk in '07
12 and '08. What does that look like?
13 MR. WESNER: When we came on, I didn't
14 know. I wasn't familiar with this. I remember we
15 did what we call a systems review. We had to put
16 together your assessment of what is the current
17 state of the Municipal portfolio and what are the
18 recommendations.
19 Sitting down with Brian, who was
20 consulting, who we had the relationship with at the
21 time, and talking through securities lending
22 analysis.
23 At that time when the collateral came in
24 and you had to reinvest, they invested

1 three-quarters of it in a vehicle called Step,
2 which was a more variable, more aggressive
3 investment portfolio. 25 percent was in STIFF,
4 which was basically an overnight or much more
5 liquid product.
6 That portion that was invested in that
7 Step portion, when things got bad, and a lot of the
8 securities in there were a lot of the structured
9 products that caused the Great Financial Crisis and
10 they got marked down tremendously.
11 When we did that systems review at that
12 point in time there was a 6 or 7 million dollar
13 liability. This was in the summer of 2008. We got
14 hired in April of 2008. There was a 6 or 7 million
15 dollar liability where some of the securities had
16 already gotten marked down.
17 The Trustees, and the Treasurer at the
18 time, Stephanie Neely, a very, very astute
19 investment professional, and it was, okay,
20 understood that risk but we can't realize these
21 losses.
22 Any rational person in the Trustee's
23 position would have said we don't want to realize
24 these losses. Once this corrects, we'll make the

1 portfolio more conservative.
2 Then September and October of 2008
3 happened and at one point in time you had a 50 plus
4 million dollar liability or loss in tech lending.
5 Some of that ended up being permanent. The
6 securities that were permanently impaired. Things
7 that were AAA related ended up being worth nothing.
8 So it took almost five, seven years of
9 taking the earnings from securities lending and
10 paying down the loan. Northern gave you a loan.
11 They didn't make you pay for it right away that
12 loss. They loaned you that money and then you paid
13 it off with securities lending earnings for the
14 next five, seven years.
15 We didn't get to use any of those
16 earnings. You got to use it to pay down that loss.
17 There was a lost decade where securities lending
18 was just a terrible thing. So many lawsuits that
19 came out of this. Things that were misrepresented
20 to clients. Northern was sued. Everybody in tech
21 lending was sued. But your program then was
22 materially different. At one point it went away
23 from Northern and now back to Northern so it's been
24 quite a ride.

1 I don't want to say there's nothing that
2 would ever create the same situation but because of
3 all of the things that Stephen highlighted the
4 integrity of the assets that the collateral pools
5 are invested in now, I feel pretty confident saying
6 you could have a 2008 like event happen again and
7 that collateral pool would not be impaired. If it
8 would be impaired, it would be just a very minor
9 fashion. A lesson was learned by all parties I
10 think that things were structured in a less than
11 ideal fashion. But that is why it is important to
12 understand because I think people sitting in the
13 Trustees' position back then, securities lending
14 wasn't presented. It was a line item that they saw
15 once a quarter. You didn't need to know about it
16 until the program blew up.
17 It is good to have this, understand what
18 it is, what securities lending is. You have a high
19 level familiarity with it. Oh, yeah, Stephen is on
20 top of that. If I need some data on tech lending,
21 I can ask Stephen what is going on with our
22 program.
23 PRESIDENT DEGNAN: Our next item is an
24 action item. Dennis, I will ask you to present

1 this matter.
2 MR. WHITE: Good morning. Just a couple
3 of things here. As you know at the last meeting in
4 February we highlighted certainly our funding
5 position and then with that in mind counsel shared
6 with us this sort of something we received from
7 Segal in 2019 that took a look at our funding at
8 that time. I think it was the end of 2018. They
9 kind of did some modeling for I'd say about eight
10 different scenarios and kind of took a look at what
11 our funding level could look like during this fixed
12 period of the ramp up prior to the actuarially
13 based funding.
14 In that model, certainly, they projected
15 that under a couple scenarios. It could be lower
16 than we actually are right now. We thought with
17 that in mind now might be a good time to kind of
18 update that model.
19 So the action item we're hoping to take
20 is for you to authorize us to work with Segal to
21 update the 2019 projections and using I think the
22 2021 numbers and the 2020 numbers to provide us
23 some new projected models.
24 This morning they sent over a proposal

1 that is for $38,000. This one is a little bit more
2 robust then what we had in mind in terms of simply
3 updating the modeling. This one includes sort of
4 deterministic modeling and some stochastic
5 modeling.
6 It is a little bit more sophisticated
7 then I am comfortable completely digesting but I
8 can say the deterministic model is closer to what
9 they did in 2019 for us in terms of talking about a
10 few different scenarios that show what our funding
11 levels would look like going forward based on I
12 think eight different scenarios in 2019. We wanted
13 to just do that.
14 We haven't finalized with them exactly
15 what the scenarios are. If we do this sort of
16 reduced, just looking at that, as opposed to 38,000
17 here, they emailed during the meeting it would be
18 $22,000.
19 We are seeking authorization for up to
20 $22,000 to work with counsel to produce an update
21 of the 2019 data based on seven or eight different
22 market scenarios to get an idea of what your
23 funding levels will look like.
24 PRESIDENT DEGNAN: It seems like a

1 reasonable approach to me. Any other Trustees have
2 any comments on it?
3 MR. WHITE: From a timing perspective,
4 they think they can have the report done by April
5 12th in time for our board meeting.
6 PRESIDENT DEGNAN: That would be fine.
7 MS. BOECKMAN: As fiduciaries, it is
8 great to have these conversations about your
9 funding ratio. You are obviously coming off the
10 ramp, which was a concern, to be honest, back in
11 2019, which is why the testing originally happened.
12 It is nice now that you are at the end of
13 the ramp, you are about to start to receive
14 actuarially determined contributions on a go
15 forward basis. But based on what you have heard
16 from your investment fiduciaries and your
17 investment staff and where the funding ratio is
18 right now, it is a good idea to update these
19 numbers so you as Trustees are comfortable that the
20 amount of cash and contributions that you are going
21 to be receiving from the City is sufficient to meet
22 your investment obligations and obviously your
23 obligations to your members.
24 We are pretty comfortable, based on what

1 we understand from the 2019 numbers, that you are
2 in an okay spot.
3 I know when you hear the funding ratio it
4 makes people nervous but I think what we're going
5 to find out from Segal is that, yes, that number is
6 going to stay around 17, 18 percent for the next
7 couple of years but then in a little bit it's going
8 to start to go up.
9 I think you are going to see that sort of
10 be respective of what the investment returns are
11 during that time period. But we won't know until
12 we get that information and then it is a good
13 conversation to have with your investment
14 professionals and your legal team.
15 So as fiduciaries you know what to say if
16 you have a constituent call you and say, hey, is 18
17 percent something we need to be worried about?
18 PRESIDENT DEGNAN: Thank you. Is there
19 anymore discussion?
20 We are looking for a motion to approve
21 the retention of Segal Consulting to prepare an
22 update for the 2019 Stress Test in an amount not to
23 exceed the $22,000 quoted. Do I have a motion for
24 this?

1 TRUSTEE CANNING: Motion.
2 PRESIDENT DEGNAN: Motion by Trustee
3 Canning. Do I have a second?
4 MR. SLACK: Second by Mr. Slack.
5 PRESIDENT DEGNAN: Thank you, sir.
6 Donna, please call the roll.
7 MS. HANSEN: Trustee Canning.
8 TRUSTEE CANNING: Yes.
9 MS. HANSEN: Trustee Degnan.
10 PRESIDENT DEGNAN: Yes.
11 MS. HANSEN: Mr. Slack.
12 MR. SLACK: Yes.
13 MS. HANSEN: Motion carries.
14 PRESIDENT DEGNAN: Motion passes.
15 Moving on to the next item.
16 Consideration of a possible special meeting date to
17 discuss funding related topics, including this
18 report that is forthcoming from Segal.
19 On behalf of the Board, we, as Trustees,
20 believe that after we receive the Stress Test
21 report, it would make sense to schedule another
22 special meeting in April to focus on the current
23 funding situation facing the fund and what the
24 Trustees can and should be doing.

1 I think it would be a good idea if we
2 agree upon that date now. If not, Dennis, would
3 you please work with the Trustees, counsel and
4 consultants to set a date where we can focus on
5 funding? Does anyone have an idea?
6 MR. WHITE: Our regular meeting is the
7 April 21st. The 28th might be a good time, if that
8 works.
9 Mr. Slack, does the 28th work for you for
10 a special meeting dedicated to discussing funding?
11 I think from a previous conversation the Treasurer
12 mentioned that might be a good date.
13 MR. SLACK: That's fine. If not her, I
14 can take it.
15 MR. WHITE: Okay.
16 MS. BOECKMAN: I do know this is an
17 important meeting for Trustee Soni, Trustee
18 Thompson and the Treasurer, for all board members
19 obviously. Maybe what you would do is approve this
20 tentative to Dennis confirming that all five can be
21 present. I do think we want to get every Trustee
22 here, if they can, if they want to be here. So
23 that would be my only advice that you approve it
24 tentative to Dennis reaching out and confirming the

1 availability from the rest of the board.
2 PRESIDENT DEGNAN: Do I have a motion to
3 set a tentative special meeting date to discuss
4 funding to April 28, 20202?
5 TRUSTEE CANNING: Motion.
6 MR. SLACK: Second.
7 PRESIDENT DEGNAN: Seconded by Mr. Slack.
8 Donna, would you please call the roll?
9 MS. HANSEN: Trustee Canning.
10 TRUSTEE CANNING: Yes.
11 MS. HANSEN: Trustee Degnan.
12 PRESIDENT DEGNAN: Yes.
13 MS. HANSEN: Mr. Slack.
14 MR. SLACK: Yes.
15 MS. HANSEN: Motion carries.
16 PRESIDENT DEGNAN: Motion passes.
17 New business/old business. Any new
18 business or old business to be addressed?
19 Hearing none, is there a motion to
20 adjourn today's meeting?
21 TRUSTEE CANNING: Motion.
22 MR. SLACK: Second.
23 CHAIRMAN FORTUNA: Seconded by Mr. Slack.
24 All in favor say "Aye".

1 (Chorus of ayes.)
2 PRESIDENT DEGNAN: Opposed?
3 Hearing none, motion carries.
4 Thank you.
5
6 (WHICH WERE ALL THE PROCEEDINGS
7 IN THE ABOVE-ENTITLED MEETING
8 AT THIS DATE AND TIME.)
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1 STATE OF ILLINOIS)
) SS.
2 COUNTY OF DU PAGE)
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5
6 DEBORAH TYRRELL, being a Certified Shorthand
7 Reporter, on oath says that she is a court reporter
8 doing business in the County of DuPage and State of
9 Illinois, that she reported in shorthand the
10 proceedings given at the taking of said cause and
11 that the foregoing is a true and correct transcript
12 of her shorthand notes so taken as aforesaid; and
13 contains all the proceedings given at said cause.
14
15
16
17 Debbie Tyrrell
____
DEBBIE TYRRELL, CSR
18 License No. 084-001078
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