County Employees Retirement System
Board of Trustees – Special Meeting
October 10, 2024, at 2:00 pm ET (9:00 am CT)
Live Video Conference/Facebook Live

AGENDA

1.	Call to Order	Lisle Cheatham
2.	Opening Statement	Eric Branco
3.	Roll Call	Sherry Rankin
4.	Public Comment	Sherry Rankin
5.	Chairman's Corner	Lisle Cheatham
6.	Investment Committee Recommendation*	Dr. Merl Hackbart KPPA Investment Staff
7.	CERS Board Election Ballot a. Candidate 5-minute Presentations	Kristen Coffey
8.	CEO Report	Ed Owens, III
9.	KPPA Executive Director Report	Ryan Barrow
10.	Closed Session*	Eric Branco
11.	Adjourn	Lisle Cheatham

*Board May Take Action

MEMORANDUM

TO: County Employees Retirement System Board of Trustees

From: Dr. Merl Hackbart, Chair
Investment Committee

Date: September 27, 2024

Subject: Summary of Investment Committee Third Quarter Special Meeting

The County Employees Retirement System Investment Committee held a special meeting on September 17, 2024, to discuss the CERS Investment Policy Statement (IPS) and consider a Real Return asset class recommendation from the Investment Office.

1. **The following item was approved by the Investment Committee and is being forwarded to the County Employees Retirement System Board of Trustees for ratification.***

    a. **Real Asset Allocation Recommendation -- The Investment Committee approved by unanimous vote an allocation of $60 million to the Investment Manager, Strategic Value Partners, for a continuation vehicle in Project Spurs. The committee is submitting the approval for ratification by the Board of Trustees.**

RECOMMENDATION: The Investment Committee requests the County Employees Retirement System Board of Trustees ratify the action taken by the Investment Committee.

2. **During the special meeting the Committee also heard the following reports.**

    a. Wilshire team members walked through the proposed changes to the IPS for the committee. A redlined version of the current IPS, a clean version of the new IPS, and a memo highlighting the proposed changes were provided for the committee to consider. The committee held a robust discussion with the Wilshire team and the KPPA Investment Office concerning several of the proposed changes. After completing discussion on the entire document, the committee asked that a version of the old IPS be created with the proposed changes side-by-side so the committee could better see the impact of the changes.

The committee then determined it would be better to see the changes side-by-side before voting on the most significant policy statement entrusted to them by the Board of Trustees. As a result no vote was taken on approval of the IPS and it will come before the committee again at the next regularly scheduled committee meeting.

b. The Investment Office presented the Real Return allocation mandate to the committee. The recommendation called for a $60 million allocation across the four CERS plans. Several committee members commented they appreciated the presentation format used by the Investment Office as it highlighted other Real Return options that were considered but for various reasons not considered for investment at this time. The committee voted unanimously to approve the recommendation.

KPPA
Kentucky Public Pensions Authority

CERS Investment Committee

Real Assets Recommendation

September 17, 2024

Asset Allocations

Over the last several years, the CERS portfolios have maintained a structural underweight to the Real Return asset class based on lack of compelling risk/return opportunities

CERS Pension - Target vs Actual Weights
September 6, 2024

Category	Market Value	Actual	Target	IPS Min	IPS Max	Tgt Diff
Equity	$5,264,657,136	54.0%				
Public Equity	$4,645,047,655	47.6%	45.0%	30.0%	55.0%	2.6%
Private Equity	$619,609,480	6.4%	8.0%	4.0%	12.0%	-1.6%
Fixed Income	$3,585,934,035	36.8%				
Specialty Credit	$1,950,950,857	20.0%	20.0%	16.0%	24.0%	0.0%
Core Fixed Income	$1,293,330,432	13.3%	13.0%	10.0%	20.0%	0.3%
Cash	$341,652,745	3.5%	2.0%	0.0%	5.0%	1.5%
Inflation Protected	$905,076,062	9.3%				
Real Return	$392,151,931	4.0%	7.0%	4.0%	10.0%	-3.0%
Real Estate	$512,924,132	5.3%	5.0%	3.0%	7.0%	0.3%
TOTAL PORTFOLIO	$9,755,667,233					

CERS Real Return - Target vs Actual Weights
2017 - Present

Year	Actual	Target	+ / -
2017	9%	15%	-6%
2018	9%	15%	-6%
2019	9%	15%	-6%
2020	7%	10%	-3%
2021	6%	13%	-7%
2022	3%	13%	-10%
2023	4%	13%	-9%
Sep-24	4%	7%	-3%

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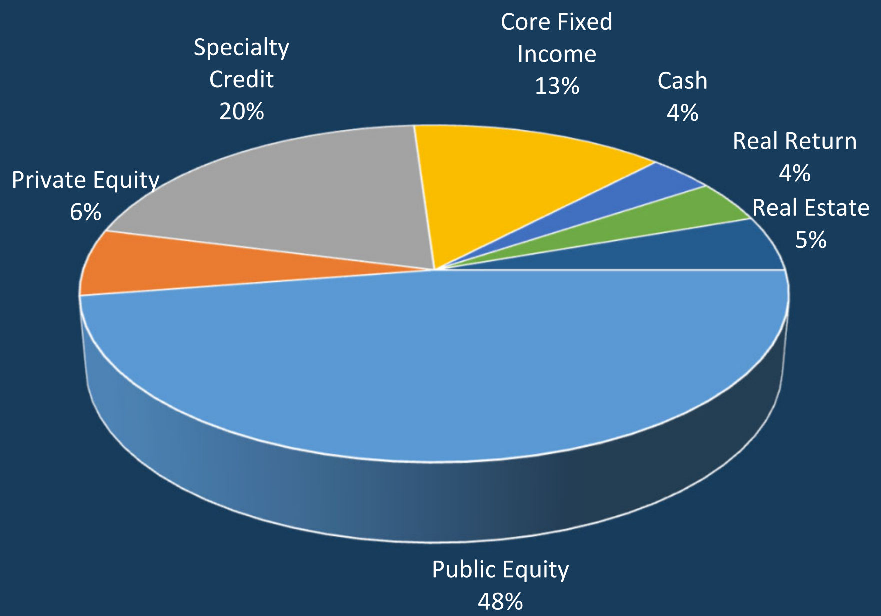
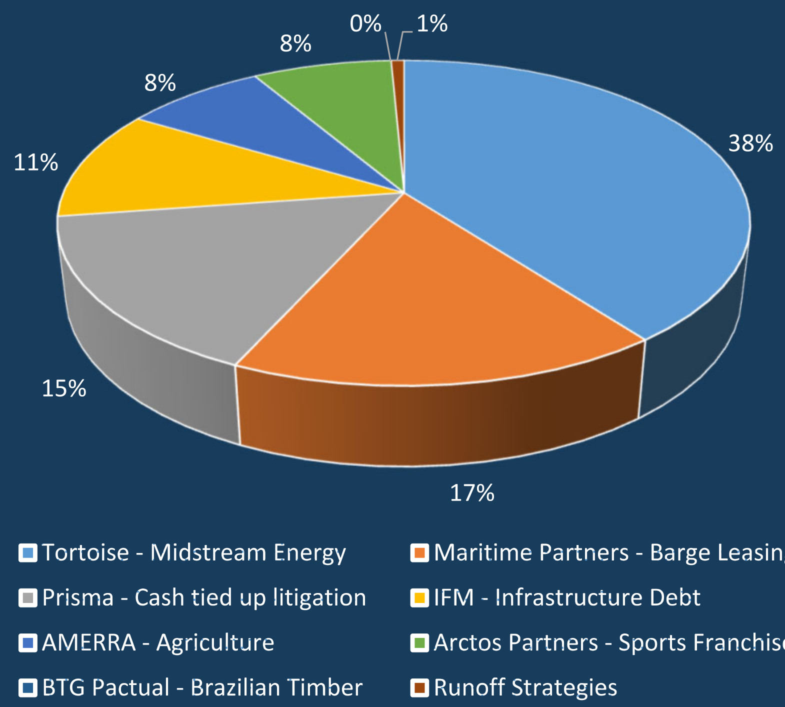
Real Return Allocation Today

Current Asset Allocation



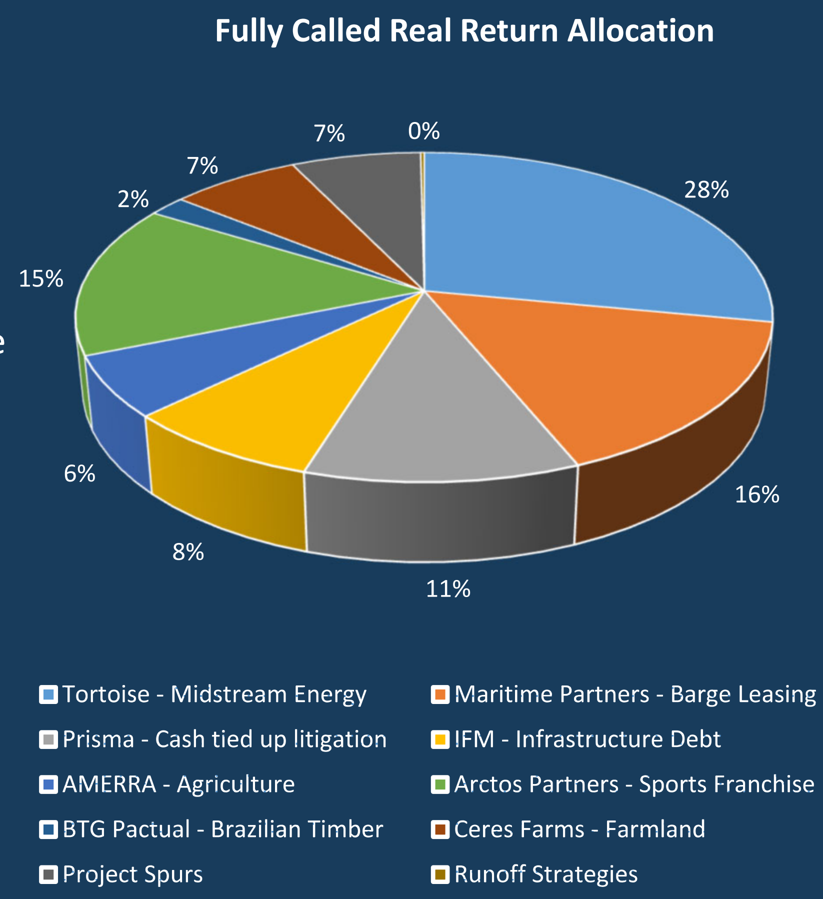
Current Real Return Allocation



CERS County Employees Retirement System

Project Spurs - Impact and Rationale

- Unique investment opportunity in scarce, hard to replicate asset with defensive characteristics
- Favorable expected risk-adjusted return from steady and growing cash flows that mitigate inflation
- Low return correlations to current Real Return investments and the broader overall portfolio
- High alignment with control owner Strategic Value Partners, who is rolling its proceeds and carried interest as well as investing additional money in the new vehicle
- CERS will realize its current investment in Spurs at >2.0x net – Staff recommendation is to roll current exposure and add additional capital alongside Strategic Value Partners
- Will get CERS an additional 0.3 – 0.4% closer to Real Return target weight within 1-3 months, funded by cash on hand and sale of proxy assets



Real Return / Private Markets Investment Process

- CIO, Investment Staff and Consultant are responsible for overseeing Private Markets portfolio, including Real Return

  - Sourcing: Ongoing (not point-in-time) review of staff and consultant contacts, consultant databases, networking, reading, peer references, and inbound approaches.

  - Due Diligence: CIO and Investment Staff are responsible for evaluating managers' strategy, team, processes, and investments
    - Includes investor and other reference calls
    - Consultants / databases utilized as needed

  - Each investment opportunity is evaluated against:
  - (1) comparable investment managers / strategies
  - (2) other available investments and their risk / return characteristics

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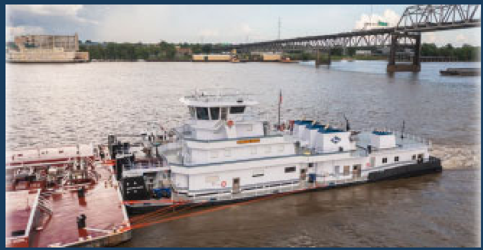
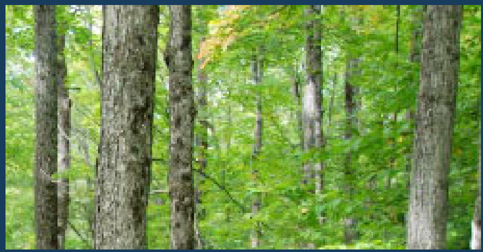
Other Real Return Strategies Reviewed / In Consideration

- Transportation leasing: Currently in diligence
- Energy credit / energy secondaries: Initial calls
- Mining credit: Early-stage evaluation
- Timberland: Early-stage evaluation
- Infrastructure: Early-stage evaluation
- Dedicated Commodities: Ongoing
- Global maritime: Passed
- Permanent cropland: Passed







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Other Real Return Strategies Reviewed / In Consideration

- Global Maritime: Passed

Opportunity: Fund that primarily invests in transactions within the commodity shipping and maritime equipment industries.

- Highly cyclical market with global oversupply risk
- Lower barriers to entry with structured loans to the riskiest borrowers
- Strategy extension beyond lending to do vessel acquisition
- Limited workout experience and capability to internally manage any collateral repossession scenarios
- Significant Key Person risk
- Alignment concerns around the team's lack of equity ownership at the GP level

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Other Real Return Strategies Reviewed / In Consideration

- Permanent Crops: Passed

Opportunity: Fund that primarily invests in permanent crop farms (e.g. wine grapes, tree nuts, apples, cherries, citrus) across the United States

- ➢ Higher exposure to weather, pest, and commodity price risk than currently approved Ceres strategy
- ➢ Significant water risk in several regions where crops like nuts and wine grapes are grown
- ➢ High upfront cost / 'J-curve' experience for crops that require long lead times before producing
- ➢ Weak historic returns (<1% net IRR through 3 and 5 years for prior funds)

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Other Real Return Strategies Reviewed / In Consideration

- Dedicated Commodities

Opportunity: Provides portfolio diversification benefits and low correlation to equities and fixed income in normalized markets while historically exhibiting positive correlation with inflation.

- Universe screened down to eight strategies/managers, with due diligence conducted on five
- Significantly trending markets with clustered performance profiles, boom-bust cycle behavior
- High overall volatility with performance that often lags over longer periods
- High correlation amongst constituents
- Smaller opportunity set, often relying on trading strategies to generate significant returns
- Less compelling risk-adjusted returns compared to currently available alternatives
- Continuing to monitor and evaluate as potential future investment opportunity

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KENTUCKY PUBLIC PENSIONS AUTHORITY

INVESTMENTS

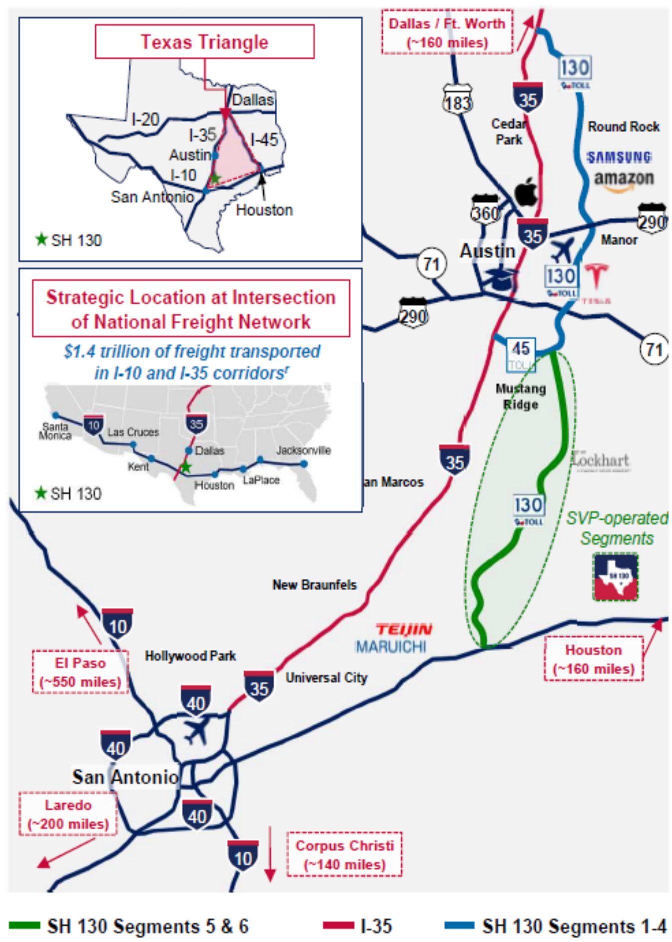
To: CERS Investment Committee

From: Anthony Chiu, Deputy CIO

Date: September 17, 2024

Subject: Investment Recommendation – Project Spurs

KPPA Investment Staff is proposing an investment with Strategic Value Partners ("SVP" or the "Firm") in a continuation vehicle ("CV") for Project Spurs ("Spurs"). As of 2Q 2024, Spurs is a 9% position in Strategic Value Special Situations IV ("SVSS IV" or "Fund IV"), a 2017 vintage fund with $2.85 billion of committed capital. This includes $65 million from KPPA, which was less than the approved $75 million due to the fund being oversubscribed.



Spurs is a 41-mile toll road asset in Texas between Austin and San Antonio that SVP acquired directly from lenders in a 2017 restructuring. Today the Firm controls 65%, with the remainder held by the US Department of Transportation through its Build America program.

SVP has created a CV structure as they see compelling value in owning Spurs for several years beyond Fund IV's term, which expires in 2025. They believe Spurs remains well-positioned for growth because of Texas's continuing economic expansion; Spurs' market share gains from the more congested and less reliable I-35; and proposed development initiatives that could significantly boost Spurs' earnings and extend the current concession (which has 38 years remaining) by an additional 20 years.

This investment opportunity is a time-sensitive one that is expected to have significant investor demand. Two large investors have committed to anchor the CV with $500 million of the $1.45 billion that SVP is raising. SVP's Partners are also rolling their Fund IV proceeds from Spurs into the new CV and contributing new capital for a total internal investment of approximately $100 million, further aligning their interests.

Staff believes Spurs will provide an attractive risk-adjusted return with low correlation to CERS' existing overall portfolio and provide complementary exposure within the Real Return allocation. Following the recent asset allocation update, CERS' target portfolio weight for Real Return is 7%. This proposed investment would help the plans continue moving toward the target weight and will be fully invested during the 4th quarter of 2024.

Investment Process and History:
Spurs was originally constructed by a subsidiary of Spanish company Ferrovial, who was awarded a 50-year concession from the Texas Department of Transportation (TxDOT) in 2006. Ferrovial's subsidiary Cintra partnered with Texas-based Zachry American Infrastructure to construct the road, which opened for traffic in October 2012.

However, a combination of overly optimistic traffic projections, excessive leverage, and an ill-fated interest rate swap caused Spurs to file for bankruptcy in March 2016. Road construction flaws also appeared shortly after opening, for which Ferrovial and Zachry were sued and resulted in a settlement.

Through its direct sourcing relationships with European banks, SVP was able to buy enough of Spurs' discounted debt to become its control owner, restructure the debt, and bring the company out of bankruptcy in June 2017. After taking control, SVP replaced the Spurs management team and board; remediated the road construction flaws; recovered proceeds through litigation from Spurs' original contractors; and repaired relations with key stakeholders like TxDOT and local chambers of commerce and foundations where Spurs passes.

Spurs has benefited from Austin and Texas's recent economic and population growth, which is expected to continue through the duration of this investment. Combined with SVP's execution of its value creation plan, Spurs' revenue and EBITDA have both doubled from 2019 to 2023 - even amidst the COVID pandemic. Traffic grew more than 60% over the same timeframe, even as toll rates also increased nearly 30%, suggesting low demand elasticity and a significant value placed on the reliability of transit time on Spurs compared to the increasingly clogged I-35.

Business / People:
As Spurs exited bankruptcy in 2017, SVP engaged transportation facility management specialist Louis Berger Services to operate and manage the asset. The CEO and COO also had previous experience as Deputy Commissioners of two states' Departments of Transportation. Additionally, a former chairperson of the Texas Transportation Commission as well as two infrastructure investors with experience from Abertis and Global Infrastructure Partners were named as independent directors.

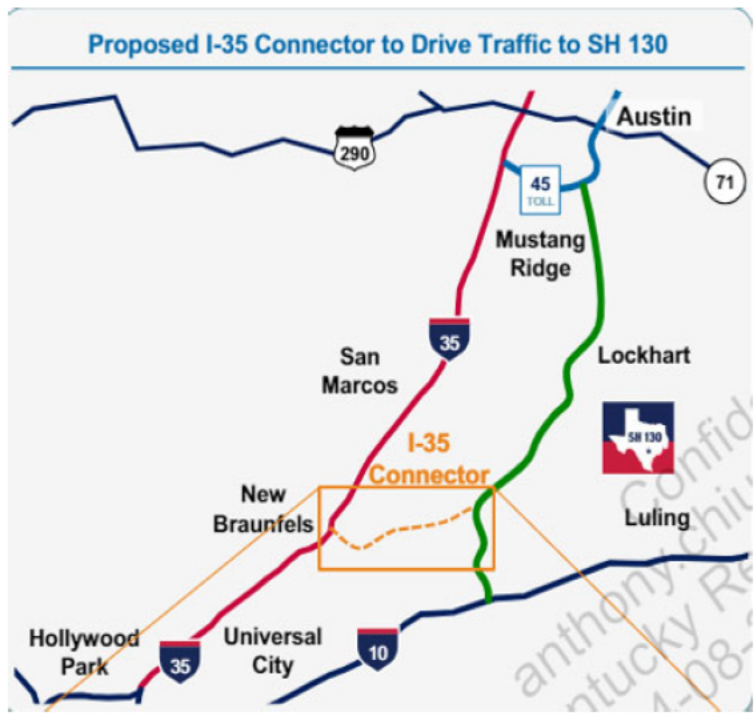
Over SVP's 7+ year investment, management and board members have cycled through and now feature several executives with experience at Transurban, a $40+ billion Australia-listed operator of toll roads in the US, Canada, and Australia. As shown below, the executive team continues to have construction and government relations experience which should aid Spurs' continued operations, growth, and potential additional concession.

After investing over $160 million to remediate and repave Spurs from 2017-22, Spurs is well-positioned to maintain and even grow margins with minimal capex needs until 2031.

Besides additional population growth and economic development, a potentially significant return driver for Spurs is a non-tolled connector road to I-35 that could drive additional traffic and gain a 20-year extension of Spurs' concession to 2082.

This would require state-level legislation and has broad support that helped it pass the Texas House in 2023. SVP is hopeful the bill will pass during the next legislative session in 1H 2025 and projects that the additional concession would boost net multiple and IRR by [redacted] respectively.

Notably, this is not incorporated in SVP's original base case projected returns of [redacted]. Subsequently, Spurs' performance in the first half of 2024 has been above forecast across the board and has increased SVP's base case to [redacted]



While this growth would of course be welcome, Staff is viewing Spurs as an attractive infrastructure asset that will likely (1) have steady cash flows that grow with inflation and (2) retain value as a scarce, essential, and difficult to replicate asset.

Even in Wilshire's low scenario that discounts SVP's traffic volume growth by 50% and assumes a below-market exit multiple of 20x EBITDA, Spurs' expected return would be [redacted] at the end of the investment's term in 2032. For reference, one of KPPA's managers who has also previously invested in Spurs' debt viewed typical toll road valuations to be in the 30-45x range. Additionally, the Northwest Parkway toll road near Denver with slower growth dynamics than Spurs traded at over 65x in May.

Performance:

SH-130 in Fund IV	Invested ($ MM)	Realized ($ MM)	Unrealized ($ MM)	Total Value ($ MM)	Gross Multiple	Gross IRR
1Q 2024	$ 152	$ 93	$ 316	$ 409	2.7x	22%

*Exiting Fund IV investor returns expected to be [redacted]
Source: Strategic Value Partners

Conclusion: Given the attractive asset, compelling market opportunity, and current Real Return allocations, Staff is recommending an investment of $60 million to be shared among all CERS plans pending successful legal negotiations. When fully funded, this would represent an additional ~0.3–0.4% of plan assets (depending on fluctuations in market value). It is anticipated this investment would be funded by existing cash or the unwinding of proxy positions based on the specific needs of each plan.

<u>Investment and Terms Summary</u>

Type of Investment: Real Return

Structure: Continuation Vehicle

Term: 8 years, with 3 one-year extensions (2 at GP discretion, 1 with Advisory Committee consent)

Management Fee: 1% on invested cost

Profit Sharing: 10% of profits above a 10% compounded annual return
12.5% of profits above a 12.5% compounded annual return
20% of profits above a 15% compounded annual return

Purpose: Provide CERS with exposure to a unique, long-lived real asset with steady and growing cash flows

Risks: Inaccurate traffic and revenue projections, leverage, regulatory / legal, illiquidity

Exp. Net Return: 7% - 10%

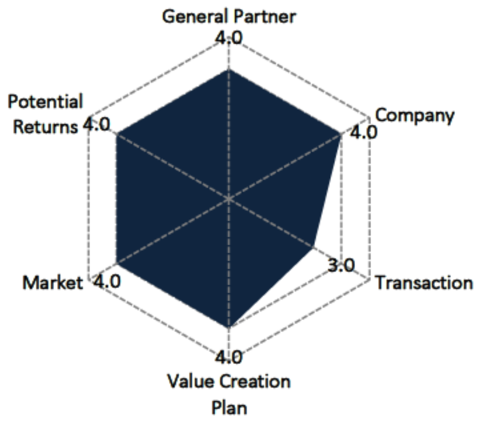
*No placement agents have been involved or will be compensated as a result of this recommendation.

Project Spurs

Final Diligence

General Partner	SVP
Vintage Year	2024
Timing	August 2024
Strategy	Core-Plus Infrastructure
Sector	Generalist
Investment Structure	Continuation Vehicle
Region	North America
Purchase Price (EV, $M)	[redacted]
Capital Structure	74% Equity, 26% Debt
Fund/LP Co-Inv. Equity ($M)	$1,220
LTM Revenue (2023A)	$72.7M
LTM Adj. EBITDA (2023A)	$60.5M
Base Case Returns	[redacted]
Base Case Hold	8 years
Fee / Carry* / Hurdle*	1% / 10% / 10%

*Tiered carry/hurdle = 10%/10%, 12.5%/12.5%, 20%/15%



Key: 5 = Top Decile; 4 = Top Quartile; 3 = Average;
2 = Bottom Half; 1 = Bottom Decile; 0 = No Information

Past performance is not indicative of future results.

General Partner

Founded in 2001 by Viktor Khosla, Strategic Value Partners ("SVP" or the "Firm") is a global investment manager specializing in opportunistic credit, distressed debt, and special situations. The Firm currently manages $18.4 billion in AUM across asset classes through a combination of both open-end and closed-end investment vehicles. Known for its expertise in stressed and distressed investments, SVP also has an established real asset track record, including $3.5 billion of invested capital in infrastructure assets, which includes 11 toll road investments. Notably, Wilshire has a longstanding relationship with the Firm, including allocations to various SVP strategies, the most recent being the Strategic Value Capital Solutions Fund II in 2023.

Company & Transaction

State Highway 130 ("SH 130" or the "Asset") is a toll road servicing the fast-growing Austin-San Antonio corridor in Texas. The Asset was originally built by Spanish transportation infrastructure company Cintra and opened in 2012. Despite SH 130 performing well since opening, in 2017 the Asset became over-levered and was struggling to service the $1.6 billion of debt on its balance sheet, which SVP acquired for ~50% of face value from two European commercial banks. SVP ultimately led SH 130's restructuring and emerged as the control equity owner in 2017, allocating $348 million across its Special Situations Fund III and Special Situations Fund IV and $452 million across two SMAs (the "Existing Funds"). SH 130 is currently owned by SVP (~65%), U.S. Department of Transportation (~32%), and others (~4%).

Currently, SVP is seeking to transfer its ~65% ownership interest in SH 130 Concession Company, LLC (the "Company"), which owns and operates the Asset, from the Existing Funds to a single-asset continuation vehicle ("CV") that will be managed by SVP. The transaction is taking place at 97.6% of NAV as of March 31, 2024, which implies total equity for the CV of approximately $1.22 billion. The proposed entry enterprise value for the Asset is [redacted], which implies a valuation of [redacted] EV/2024E EBITDA. Anchor investors for the CV are [redacted] who are responsible for setting the entry price and terms.

Value Creation Plan

SVP's anticipated value creation plan for the Asset includes various growth drivers, including government-mandated toll escalations, organic traffic volume growth, existing excess road capacity to absorb additional demand, I-35 connector development and associated 20-year concession extension, industrial development along the traffic corridor, and trucking partnerships

Track Record

Since the strategy's inception in 2008, SVP has raised approximately $10.2 billion in total commitments across five Strategic Value Special Situations Funds ("SVSS"). Funds I-IV have generated strong returns and Fund V, while relatively early, is tracking well.

Fund	Vintage	Size ($M)	Net ROI	Net IRR
SVSS V	2021	5,089	1.3x	16.0%
SVSS IV	2017	2,500	1.8x	15.2%
SVSS III	2013	1,310	2.3x	13.7%
SVSS II	2010	918	1.9x	12.6%
SVSS I	2008	346	1.9x	15.0%

Source: Strategic Value Partners as of May 31, 2024.

Investment Merits

- Marquee, difficult to replicate toll road asset
- High-quality general partner and management team, both with an extensive history in the space
- Attractive risk-adjusted return profile

Investment Concerns

- Traffic volume risk
- Elevated entry multiple
- Management fees and carried interest

State Highway 130 Overview

Vital toll road providing a high-speed, congestion-free route in the heart of the Texas Triangle

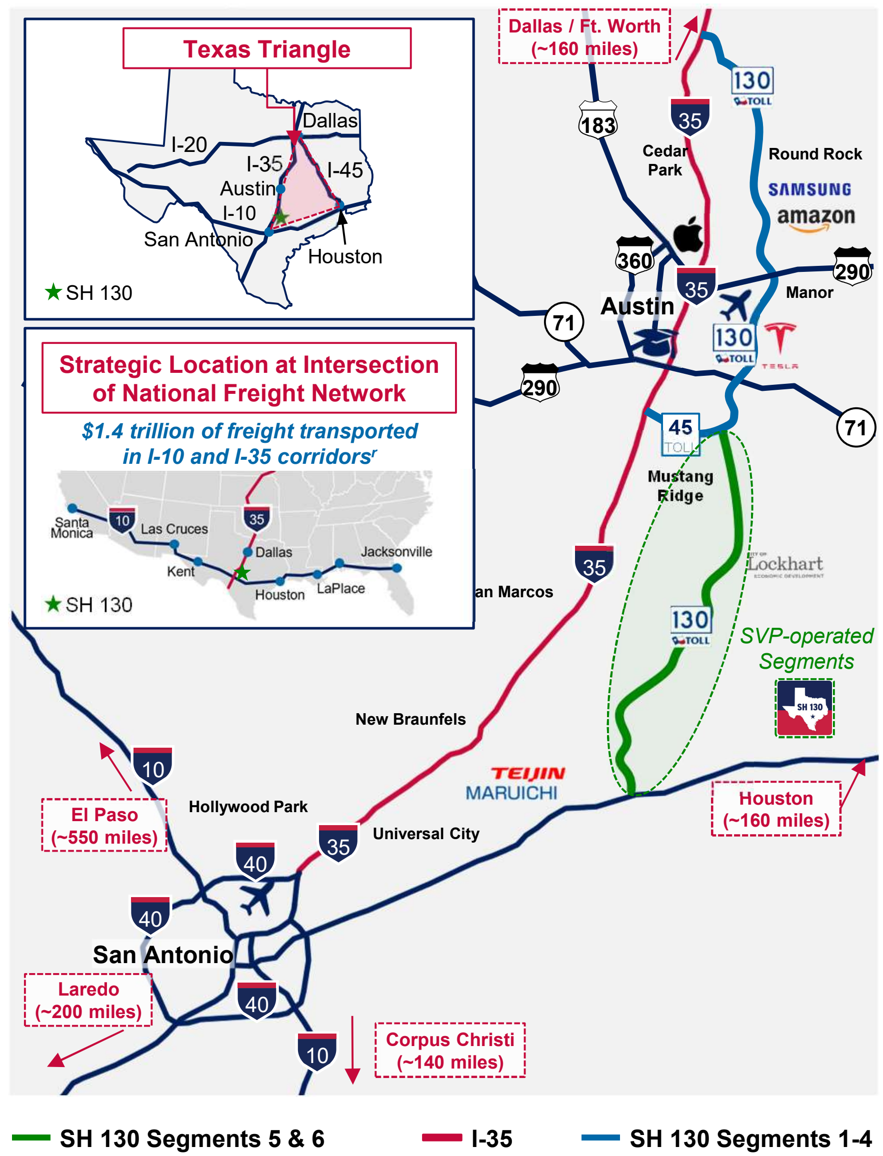
SH 130 segments 5 & 6 is a 41-mile, 4 lane toll road in Texas serving as critical link between Austin and San Antonio metropolitan areas, facilitating local and long-distance travel

- SH 130 manages, operates and maintains SH 130 Segments 5 & 6 under a 50-year concession agreement (**~39 years remaining**) with Texas Department of Transportation ("TxDOT")
- Significant customer value proposition, allowing users to bypass heavily congested traffic on I-35 **providing meaningful time savings and reliability**[k]
  - **Substantial unutilized capacity to absorb demand growth** in the corridor and continue taking share from capacity constrained competing route (I-35)[w]
  - **99% of trips with on-time arrivals on SH 130** compared to **20% of trips with on-time arrivals on I-35**[l]
- Vital asset connecting **two of the fastest growing MSAs in the country**[c] and situated strategically in a corridor experiencing **rapid commercial and industrial investment** (over $50bn capital projects currently being executed)[c]
  - Austin and San Antonio expected to continue **growing at multiples of U.S. growth rates**[c] as the region converges to a single mega MSA
- **Located at the intersection of I-10 and I-35**, SH 130 serves as an essential link in the prominent **Texas Triangle freight network**
- **United States-Mexico-Canada Agreement trade route corridor** via the Laredo border crossing (#1 U.S. inland port by trade value)[m]
- Attractive toll escalation regime providing an **embedded inflation hedge and direct GDP-linkage**, with no requirement to lower tolls

SH 130 Segments 5 & 6: Key Facts

Asset	▪ 41 miles; 2x2 lanes; 2 mainline gantries (each direction) and 12 ramp gantries; fully electronic tolling system ▪ 85 mph posted speed limit
Concession	▪ 50-year concession with 39 years remaining (2062 expiry)
Toll Regime	▪ Annual escalation based on Nominal Gross State Product per Capita for Texas, with no requirement to lower tolls ▪ Current Full Length Toll Rate (Class A / D): $9.49 / $37.87[n]
Revenue	▪ 2023 revenue ~93% above 2019 revenue (pre-COVID) ▪ ~38% light vehicles; ~62% heavy vehicles[o]

Critical Artery in Highly Congested Corridor

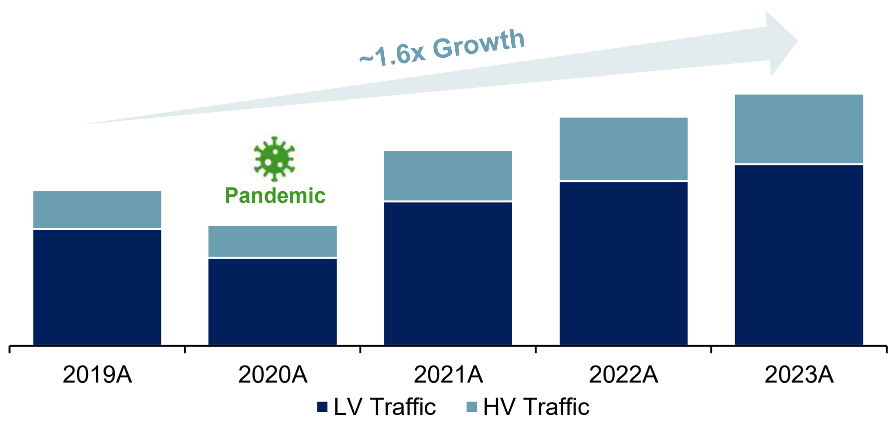


Compelling Traffic Growth and Financial Trends

Attractive historical double-digit volume and EBITDA[s] growth

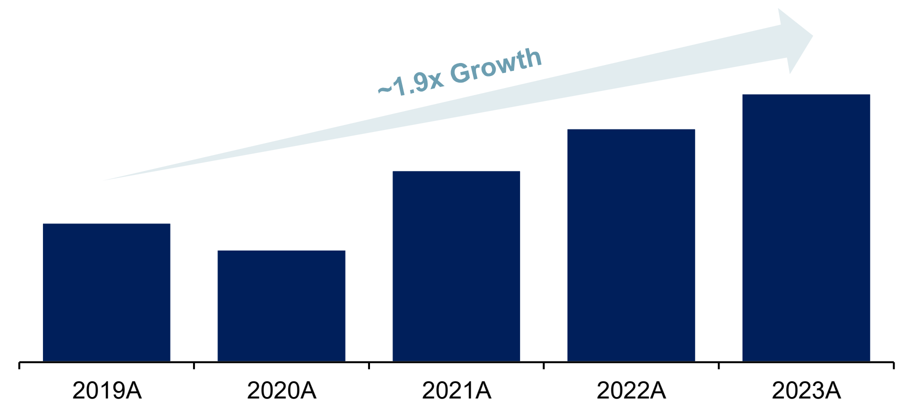
Robust Historical Traffic Growth[1]

~13% CAGR since 2019[g]



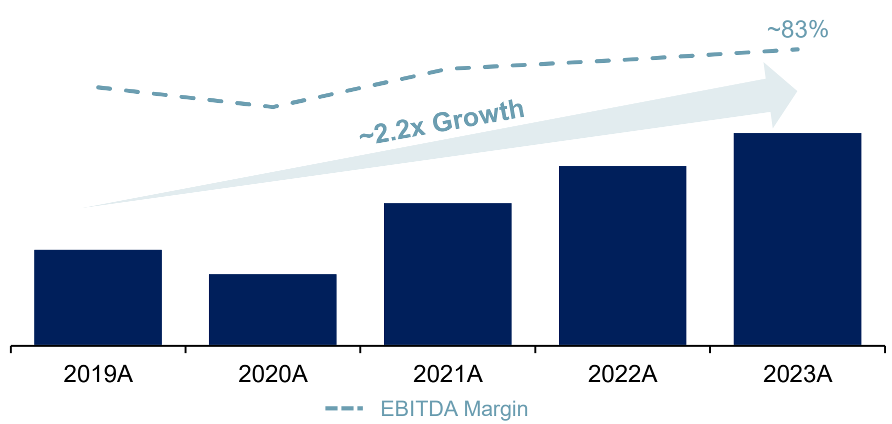
Significant Revenue Growth driven by Volume and Price[2]

~18% CAGR since 2019[g]



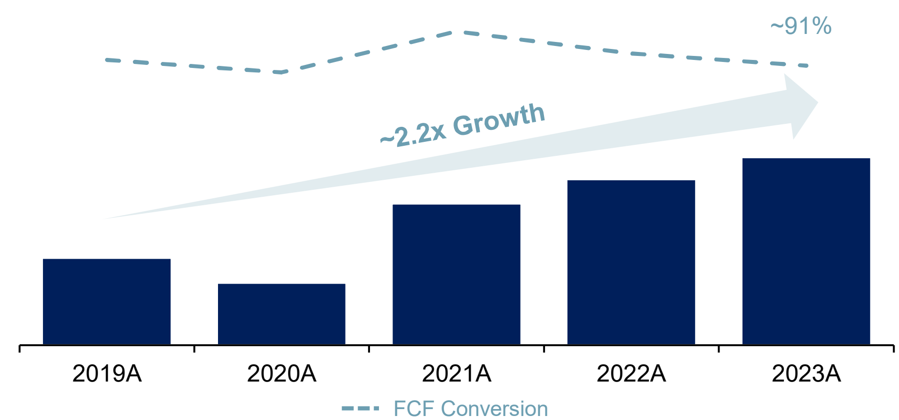
High and Growing EBITDA[s] Margins

~22% CAGR since 2019[g]



Strong FCF Profile Driven by Low Maintenance Capex[3]

~89%+ average FCF conversion since 2019[g]

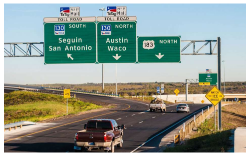


Note: Past financial performance is not indicative of future results. There can be no assurance that any expected trends or developments presented herein will continue

1. Growth rates based on number of transactions
2. Reflects toll revenue after revenue adjustments and TxDOT revenue share
3. Reflects EBITDA less recurring capex; Please refer to Endnote S on page 15 for further detail on EBITDA

SH 130 Key Investment Highlights

Well Located in Booming Economic and Demographic Corridor



- Link between two of the **fastest growing MSAs in the U.S.: Austin and San Antonio**[c]
- Essential route for US-Mexico freight movement, with **10% of all domestic truck freight**[c] passing through the corridor
- **Significant corporate investment** adjacent to SH 130 (e.g., Tesla, Amazon, Samsung, Lockhart industrial park)[h]

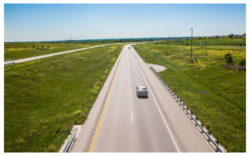
Positioned for Continued Market Share Growth by Offering Significant Value Proposition

- SH 130 offers **time savings and greater reliability,** which we believe is poised to increase from potentially **worsening I-35 congestion**[k]
- SH 130 has **taken share from I-35**[1] over time, with **headroom to continue** capturing rapid growth due to available capacity
- I-35 is expected to **remain congested despite planned expansion**[2]

Long-Dated Concession Agreement with Favorable Toll Regime

- **~39-years remaining concession life** subject to annual toll escalation with **embedded inflation hedge**
- Significant **outperformance of toll regime** relative to competing toll roads[i]
- **Favorable concession agreement terms**

Well-Maintained Asset with Efficient Operating Model



- Substantial **remediation of prior roadway issues** with **minimal near-term capex expected**[j]
- **Independent operator** with focus on optimizing for efficiency and value maximization
- Efficient operations with **fully electronic, open road tolling** with **no collection risk exposure**[p]

Compelling Traffic Growth and Financial Trends

- **Strong historical growth** in revenue and EBITDA[s] (~18% and ~22% CAGR between 2019-2023, respectively)
- Economic shock **resiliency**, with 2023 revenue ~93% above pre-COVID (2019) levels[g]
- **Double-digit revenue and EBITDA** projections[b] underpinned by economic trends and development underway

High Quality Management Team Driving Substantial Upside That the Company Can Actively Influence

- Management team comprised of **highly experienced industry veterans**
- Significant **operational and financial management achievements already accomplished**
- Additional developments underway create **substantial near-term benefit potential** (e.g., Lockhart interchange, TruckPort, and VMS)
- Government partnership efforts create **portfolio of potential 'step-change' upsides** (e.g. Connector/concession extension, I-35 Corridor partnership, Caldwell site partnership)

Exceptional Community Partner and Established ESG Practices

- **Demonstrated positive relationships** with key community stakeholders and government bodies
- Ongoing work with local and state governments to **advance priorities**
- **Strong ESG programs complement positive community engagement**, with both accomplishments to date and programs underway

1. Based on management analysis of SH 130 market share vs. I-35 using Streetlight data for trips between I-10 to SH 130 Segments 1-6 to I-35 in Jarrell vs. either of (a) I-35 all the way from NE of San Antonio to Jarrell, or (b) I-35 NE of San Antonio to SH 45SE to SH 130 Segment 1-4 to I-35 in Jarrell
2. Based on management analysis of current public plans, which continue to predict that I-35 will remain at capacity despite $5bn+ in upgrades

M E M O R A N D U M

DATE: **September 27, 2024**

TO: **CERS Board of Trustees**

FROM: **Ed Owens, III**
CEO

SUBJECT: **CEO Quarterly Report**

A few of the issues I worked on during the first quarter of the Fiscal Year are as follows:

1. **Communicating CERS Fiscal Year Investment Returns.** I worked with the Chair and KPPA Communications department to craft and distribute a CERS press release highlighting the exceptional returns recorded during the most recent fiscal year. The fiscal year end composite return for the CERS Pension plans was 11.63%; while the year-end composite return for the Insurance plans was 11.76%. These returns were outstanding although below the benchmark of 14.10%. The Investment Office detailed that the underperformance against the benchmark was driven by two overriding factors. First, in the Public Equity space, the returns continued to be concentrated in approximately seven (7) mega cap tech firms that took the market higher representing over 70% of the growth. Due to appropriate internal controls, KPPA does not allow its equity fund managers to hold that level of concentration in one firm, therefore, we were not able to replicate the markets performance. Second, there is no appropriate benchmark for the private equity asset class. Most institutional investors use a public equity mark plus 300 basis points. The impreciseness of the benchmark led most institutional investors to underperform it.

   We worked with Communications to ensure the release was sent to local newspapers and radio stations across the state as well as to the KPPA legislative newsletter lists. As a result, every legislator received the press release at their official email address.

2. **CERS Board Election Ballot.** I worked with the Chief Auditor to structure the CERS Board Election ballot. At the close of the election process there were six (6) Non-HAZ candidates and three (3) HAZ candidates for the two (2) non-HAZ seats and one (1) HAZ seat on the Board of

Trustees. The CERS Election Policy indicates that the CERS Board shall nominate no more than three (3) candidates for each position to be elected. No more than six (6) candidates can be nominated who have most of the service in a non-hazardous position and no more than three (3) candidates can be nominated that have most of the service in a hazardous position. Therefore, the ballot shall contain no more than nine (9) names. The CERS Board voted to send all nine names to the election ballot.

Each candidate was provided an opportunity to make up to a 5-minute presentation on their qualifications to the membership of CERS. If they were unable to attend the meeting, in person or virtually, each candidate was given the option to submit a statement which would be read on their behalf.

3. **Investment Policy Statement (IPS).** I have worked with the Investment Consultant, Wilshire, the KPPA Investment Office, and the CERS Investment Committee Chair to review and revise the IPS. The primary objective of the review was to ensure the oversight philosophy of the CERS Board was reflected in the IPS. Several iterations of the IPS have been produced and reviewed by the Investment Office, the legal department, and other KPPA departments.

   The IPS was presented at the most recent Investment Committee meeting for approval; however, after a very robust discussion, it was determined that additional work needed to be completed before the entire IPS could be approved. It should be noted that the CERS Board has previously ratified the committee's recommendation concerning the asset allocation and the ranges the Investment Office can operate in from the target in each asset class.

   The Investment Committee and the CERS Board realize the IPS is the most significant policy determination they will make as Trustee's and the deliberate process will ensure the most comprehensive policy and the best adjudication of their fiduciary responsibility.

4. **KPPA Enterprise Risk Assessment.** I participated in the first ever enterprise risk assessment conducted by KPPA. The assessment was coordinated by the Chief Auditor and is designed to identify those areas within the organization that have risk characteristics that require attention through policy, procedures or added personnel. The risk assessment has been implemented and I continue to be an advocate for the addition of a Senior Risk Officer.

   The primary role of the Chief Auditor and a Senior Risk officer should be different. In the absence of a Senior Risk officer, the responsibility for identifying risk should fall to the Chief Auditor. I continue to make the argument that not having a Chief Risk officer is probably the largest risk facing the organization. The agency sought authority from the Personnel Cabinet for nine (9) additional positions that were identified as needed through the KPPA strategic planning process. Those positions were denied. KPPA continues to work with the Personnel Cabinet concerning the utility of those positions.

5. **CERS Strategic Planning Process.** The CERS Committees have all completed their component strategic plans, all of which have been ratified by the CERS Board, and the component parts will be rolled into an overall CERS Board Strategic Plan. There will be two distinct areas of the CERS plan. First, we will look to align with the overall KPPA strategic plan and fit our objectives into the four (4) identified buckets. It is understood that most of our plan, relating to the overall KPPA plan, will focus on Governance.

The second portion of our strategic plan will focus on things the CERS Board can do regarding CERS investments. There was considerable energy in the special called meeting on strategic planning around identifying new products and new streams of income that could be implemented into our current process and portfolio. The Board will seek to research and identify opportunity sets in this fiscal year.

It should be noted this portion of the plan will look to be implemented in the next five (5) years. The Board will have ample time to identify, vet, and trial run any strategy before seeking implementation into the portfolio.

6. **Public Pension Oversight Board.** During the quarter, there were two (2) PPOB meetings held at the Capitol. One dealt with the investment returns of the public pension systems in the state. Our investment return was a tenth of a percentage point off of the Teachers Retirement System, however, our assets were growing at a much faster rate than any other system in the state.

KENTUCKY PUBLIC PENSIONS AUTHORITY

Ryan Barrow, Executive Director

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Kentucky Public Pensions Authority

To: KPAA Board/CERS Board

From: Ryan Barrow, Executive Director

Date: September 19, 2024

Subject: KPPA Update

I. COMMUNICATION: I started my role as the new Executive Director of KPPA on July 1st and I am truly honored to step into this position. I want to again extend my gratitude to Dave for his extended tenure, which has greatly facilitated the transition. I am excited to collaborate with you as we continue our vital work for members. Effective communication is crucial to our success, so I encourage you and KPPA team members to share your thoughts, concerns, and suggestions. I have started meeting with Board Members in Central Kentucky and will soon be reaching out the greater Louisville Area.

II. LEGISLATOR MEETINGS: As part of my onboarding at KPPA, which began with Dave Eager, we were fortunate to schedule meetings with legislators. Together with Rebecca Adkins and Erin Surratt, I have continued these discussions to expand on existing relationships with policymakers.

III. LEGISLATION TRACKING: With recent changes in staffing within our Division of Communication, we are taking the opportunity to gather input, ideas, and suggestions on how we have tracked legislation and how we should proceed in the future. An email was sent on August 30th requesting your feedback and thoughts by Friday, September 13th.

IV. LOUISVILLE OFFICE: The locations have been narrowed to three and the revised plans are being discussed with the Department for Facilities and Support Services in the Finance and Administration Cabinet.

V. CONFERENCE ATTENDANCE: In early August, Rebecca Adkins, Erin Surratt, John Chilton, Ed Owens, and I attended the National Association of State Retirement Administrators (NASRA) conference. This event brings together leaders and experts in public pension administration from across the country, offering a platform to discuss the latest trends, challenges, and best practices in our field. The insights gained and connections made during the conference will be invaluable to our agency.

VI. RATING AGENCIES: Continuing a long tradition**,** KPPA had meetings with Fitch Ratings in August and Moody's Investors Service in September. These meetings provide a valuable opportunity to discuss our agency's financial position, priorities, and long-term plans. Engaging directly with the rating agencies allows KPPA and the Commonwealth to address their inquiries and gain insights into their evaluation criteria. On September 18th, Moody's upgraded the Commonwealth of Kentucky's issuer rating to Aa2 from Aa3 and revised the outlook to stable from positive.

VII. PUBLIC PENSION OVERSIGHT BOARD (PPOB): On August 27th, Erin Surratt and I presented at the PPOB meeting. We provided an overview of the Investment Returns, Asset Allocations, and Cash Flows as of June 30th. The discussion and questions primarily focused on cash flow and the Federal Inflation Reduction Act of 2022 (H.R. 5376).

VIII. RISK MANAGEMENT: Mike Lamb and I plan to attend an upcoming training on risk management hosted by the National Conference on Public Employee Retirement Systems (NCPERS). This training will offer valuable insights into emerging risks and strategies for mitigating them. Additionally, the Risk Manager at the University of Kentucky has expressed willingness to collaborate on tools and best practices to bolster our agency's resilience against potential challenges.

IX. ALL EMPLOYEE MEETINGS: We recently held three all employee meetings on August 28th and 29th. These meetings are an important opportunity for staff to come together as an agency, share updates, discuss key initiatives, and address questions and concerns of staff.

X. KENTUCKY EMPLOYEE CHARITABLE CAMPAIGN (KECC): During our all-employee meeting, we welcomed representatives from the Crusade for Children and United Way, who spoke about how the funds they receive from KECC are utilized. KPPA has already begun promoting KECC contributions, starting with our kickoff on August 27th, which featured proceeds from DaVinci's Pizza donations. We have several unique opportunities planned for this giving season and aim to surpass our participation levels from the previous year.