

# Memorandum



CITY OF DALLAS

DATE August 21, 2024

TO Honorable Members of the Ad Hoc Committee on Pensions: Tennell Atkins (chair), Paula Blackmon, Cara Mendelsohn, Jesse Moreno, Jaime Resendez, Kathy Stewart, Chad West, Gay Donnell Willis

SUBJECT **Investment Reports for Dallas Police and Fire Pension System (DPFPS) and Employee Retirement Fund (ERF)**

This memorandum is provided in advance of your August 22, 2024, Ad Hoc Committee on Pensions. As a reminder, City staff initiated a Request for Proposals for a consultant to review the investment strategy and performance of both DPFPS and ERF. Commerce Street Investment Management (Commerce) was selected and placed under contract on April 22, 2024, to complete the review.

Commerce is an independent, Dallas-based investment management and advisory firm that provides discretionary investment management solutions for RIAs, foundations, endowments, and other institutional investors. Dory Wiley CPA CVA CFA currently serves as President and CEO of Commerce Street Holdings, LLC. He has over 34 years of experience in commercial banking, investment banking, pension investing, and investment management. From 2003-2009, he served as a member of the Board of Trustees of the Teacher Retirement System of Texas, an approximately \$140 billion pension fund, where he was Chairman of the Investment Committee, Chair of the Alternative Assets Committee, and served on Compensation, CIO recruiting, Audit, and Government Committees.

Mr. Wiley presented initial results to the Ad Hoc Committee on Pensions on June 6, 2024. Commerce has now completed their final reports for DPFPS and ERF which are attached for your information. There will not be a presentation of the materials at your upcoming Ad Hoc Committee on Pensions meeting tomorrow. However, Mr. Wiley will be available to answer questions, if needed.

Commerce provided the following information as key takeaways from their review.

## **Dallas Police and Fire Pension System (Information provided by Commerce)**

1. DPFPS is underfunded: ~39%\* funding ratio.
2. City of Dallas will have to contribute significant funds to improve the funding status.
3. The public, city officials, beneficiaries, and all stakeholders want assurance that the plan has optimal performance.
4. The goal of the review of DPFPS is an evaluation of the appropriateness, adequacy, and effectiveness of the pension's performance, and the evaluation and recommendations for overall improvements for the pension.
5. Legacy assets continue to contribute to underperformance.

6. Performance, over time, should, net of fees and investment costs, exceed appropriate benchmarks and the median of DPFPS's peers.
7. Improved performance combined with increased contributions from the City should get DPFPS to the Texas Pension Review Board funding goal in order to get a livable COLA for the participants.
8. We know that being average or above average over the last 5 years would have made a material improvement in funding status and would do so going forward.
9. Improved risk adjusted returns are needed to lower City contributions and increase funded status.
10. DPFPS has underperformed its peers both nationally and in the State of Texas over the 5 and 10-year time periods.
11. DPFPS has struggled with legacy assets the last 10 years and have made improvements with them in the last 7 years.
12. Need to target reducing volatility risk and improving risk adjusted asset allocation at DPFPS as well as PE manager selection.
13. Need to create improved private markets strategy for DPFPS going forward.
14. An improvement in long-term performance would increase the funding ratio and lessen the burden on the City and taxpayers.
15. Commerce recommends that the City of Dallas hire a qualified firm to help the City's understanding of the independently managed pension, who:
  - Helps the City's understanding of factors contributing to the performance of other top performing peers.
  - Works with city constituents to improve the City's understanding of the pensions.
  - Conducts an ongoing analysis to help the City be better informed on any issues related to performance.
  - As needed, prepares ongoing reports and clarifications for the City.
  - Is able to provide, as needed, recommendations for consideration to achieve best practice.

### **Dallas Employee Retirement Fund (Information provided by Commerce)**

1. ERF is underfunded with a ~73% funding ratio.
2. City of Dallas will have to contribute significant funds to improve the funding status.
3. The public, city officials, beneficiaries, and all stakeholders want assurance that the plan has optimal performance.
4. The goal of the review of ERF is an evaluation of the appropriateness, adequacy, and effectiveness of the pension's performance, and the evaluation and recommendations for overall improvements for the pension.
5. Performance, over time, should, net of fees and investment costs, exceed appropriate benchmarks and the median of the Plan's peers – major cities in Texas and the U.S.

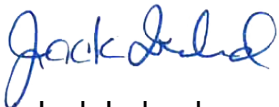
DATE August 21, 2024  
SUBJECT **Investment Reports for Dallas Police and Fire Pension System (DPFPS)  
and Employee Retirement Fund (ERF)**  
PAGE **#3 of #3**

6. While ERF has slightly underperformed its peers both nationally and in the State of Texas over the 5 and 10-year time periods, it has outperformed both the average national and average Texas plan over the most recent 3-year time period.
7. Improved risk adjusted returns would help lower contributions and increase funded status.
8. Risk adjusted asset allocation needs further evaluation with respect to an increase in private markets' allocation.
9. Target improving asset manager selection.
10. An improvement in long-term performance would increase the funding ratio and lessen the burden on the City and taxpayers.
11. Commerce recommends that the City of Dallas hire a qualified firm to help the City's understanding of the independently managed pension, who:
  - Helps the City's understanding of factors contributing to the performance of other top performing peers.
  - Works with city constituents to improve the City's understanding of the pensions.
  - Conducts an ongoing analysis to help the City be better informed on any issues related to performance.
  - As needed, prepares ongoing reports and clarifications for the City.
  - Is able to provide, as needed, recommendations for consideration to achieve best practices and improve performance.

In addition to the two reports attached from Commerce, additional attachments are provided from DPFPS and ERF as response to Commerce's reports.

Please let me know if you need additional information.

Service First, Now!



Jack Ireland  
Chief Financial Officer

c: [Attachment]

Mayor and Members of the City Council  
Kimberly Bizzor Tolbert, City Manager (I)  
Tammy Palomino, City Attorney  
Mark Swann, City Auditor  
Biliera Johnson, City Secretary Preston  
Robinson, Administrative Judge  
Dominique Artis, Chief of Public Safety (I)

Dev Rastogi, Assistant City Manager  
M. Elizabeth (Liz) Cedillo-Pereira, Assistant City Manager  
Alina Ciocan, Assistant City Manager  
Donzell Gipson, Assistant City Manager (I)  
Robin Bentley, Assistant City Manager (I)  
Elizabeth Saab, Chief of Strategy, Engagement, and Alignment (I)  
Directors and Assistant Directors

# Dallas Police & Fire Pension



## Objectives 1-8

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Commerce Street Investment Management

# Discussion Topics

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- Obj 1 Asset Allocation Analysis (6)
- Obj 2 Historical Return Analysis (18)
- Obj 3 Identification of Peer Groups (25)
- Obj 4 Risk Mitigation Strategies (30)
- Obj 5 Asset Allocation Strategy (33)
- Obj 6 Manager Selection Evaluation (38)
- Obj 7 IPS Recommendations (43)
- Obj 8 Cost Analysis (45)

# Preliminary Disclosures



The analysis that follows is the result of a few weeks' work analyzing the Plans as well as peers we found relevant

There are certain assumptions made in this analysis that could be enhanced with further ongoing collaboration with both Plans

**We recommend that the best approach to achieving a complete analysis of the Plans is to continue to collaborate with their staffs to check key assumptions, gain a better understanding of how their Plans work, and receive the most up-to-date data to give the City the clearest understanding of the pension fund**

# Initial Discussion



## A few points most everyone can agree on:

- Dallas Police & Fire Pension Fund is underfunded: ~39%\* funding ratio
- The City of Dallas will have to contribute significant funds to improve the funding status
- The public, city officials, beneficiaries, and all stakeholders want assurance that the plan has optimal performance
- The goal of the review of DFPF is an evaluation of the appropriateness, adequacy, and effectiveness of the pension's performance, and the evaluation and recommendations for overall improvements for the pension
- Legacy assets continue to contribute to underperformance
- Performance, over time, should, net of fees and investment costs, exceed appropriate benchmarks and the median of the Plan's peers
- Improved performance combined with increased contributions from the City should get DFPF to the Texas PRB funding goal in order to get a livable COLA for the participants

# Initial Observations



**We know that being average or above average over the last 5 years would have made a material improvement in funding status, and would do so going forward**

- Improved risk adjusted returns are needed to lower City contributions and increase funded status
- DPFP has underperformed its peers both nationally and in the state of Texas over the 5 and 10-year time periods
- DPFP has struggled with legacy assets the last 10 years and have made improvements with them in the last 7 years
- Need to target reducing volatility risk and improving risk adjusted asset allocation at DPFP as well as PE manager selection
- Need to create improved private markets strategy for DPFP going forward\*

\*The last in-depth private markets' plan was formulated in 2018, but DPFP hired Albourne in 2023 as a consultant to create a new strategic plan now that many of the legacy assets have been offloaded

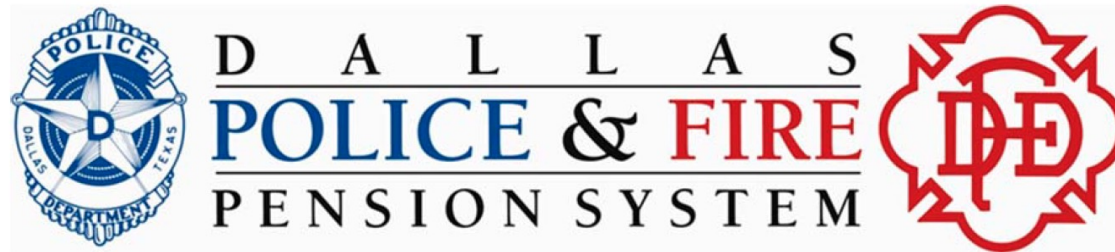


# What Commerce Street has been asked to do



## The City requested a report comprised of the following objectives:

1. Assess the overall structure and asset allocation of the investment portfolio
2. Assess the overall performance and current/historical rate of return of the investment portfolio
3. Identify appropriate state and national benchmarking for asset allocation and investment performance
4. Identify areas of potential risk and propose risk mitigation strategies
5. Evaluate the effectiveness of the current asset allocation strategy
6. Evaluate the effectiveness of the current manager selection and their strategies
7. Review the adherence to investment policies and guidelines
8. Review the current fee structure and trading costs

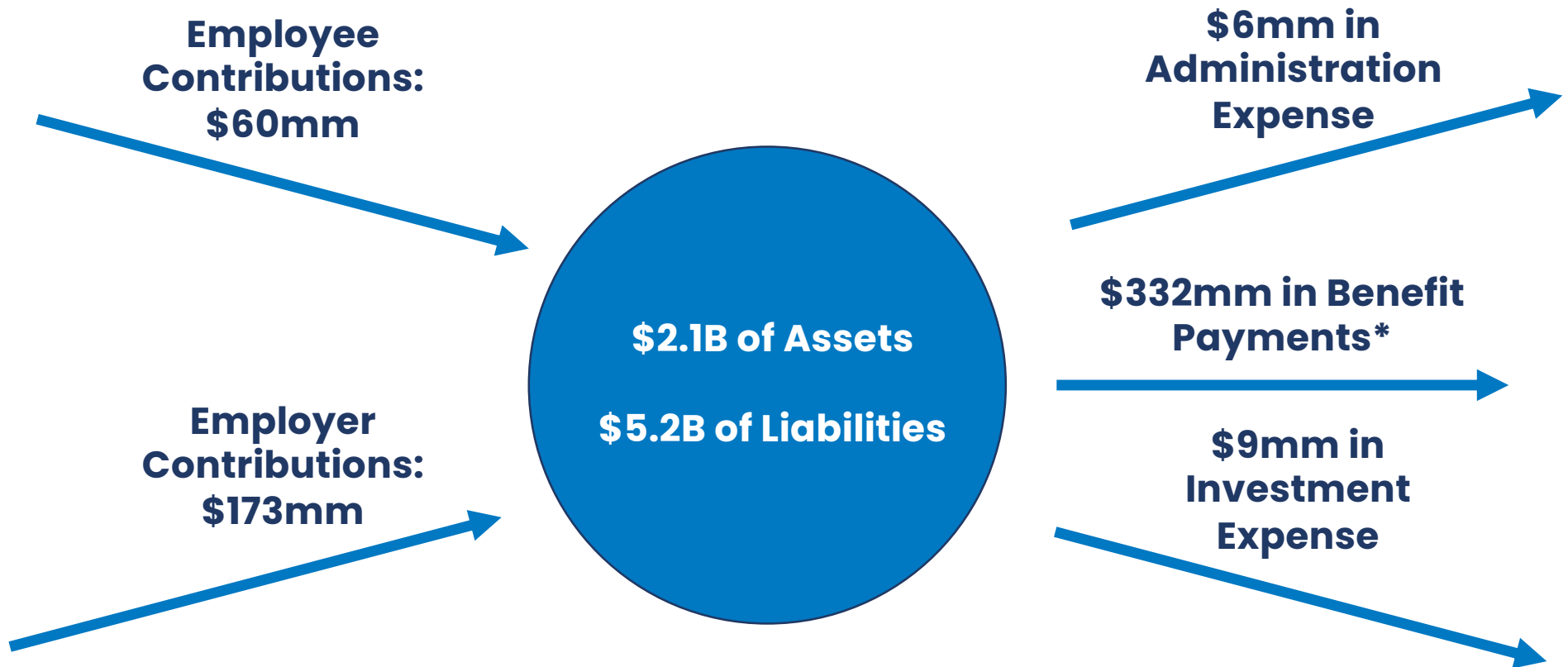


## **Objective 1: Assess the overall structure and asset allocation of the investment portfolio**

# DPFP's current inflows and outflows



## DPFP 2022 Pension Activities



Source: Dallas Police and Fire Pension System, *Actuarial Valuation and Review*, as of January 1, 2023; DPFP ACFR 2022

\*Includes contribution refunds

# DPFP's assets, outflows, and returns



	FY 2022	FY 2021
Market Value of Assets (As of 1/1)	\$2,157,840,430	\$1,943,700,593
Actuarial Value of Assets (As of 1/1)	\$2,117,978,431	\$2,127,834,406
Total Actuarial Accrued Liability	\$5,158,782,340	\$5,115,966,592
Percent Fund MVA	41.83%	37.99%
Percent Fund AVA	41.06%	41.59%
Contributions from City and Members	\$232,681,000	\$226,428,000
Benefits/refunds paid to Members	\$332,031,000	\$327,383,000
Professional/Admin Expenses	\$6,421,000	\$6,446,000
<b>Net Cash Outflow*</b>	<b>\$(105,771,000)</b>	<b>\$(107,401,000)</b>
Rate Needed to Maintain MVA	4.90%	5.53%
Actual Net Return	-2.20%	5.00%
Rate to be Fully Funded by 2105	6.50%	6.50%

**Dallas Police & Fire's recent returns have not been high enough to maintain the market value of the pension fund**

Source: Dallas Police and Fire Pension System, *Actuarial Valuation and Review*, as of January 1, 2023 and as of January 1, 2022; DPFP ACFR 2022

# DPFP benchmarking introduction



Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>DPFP (78/22)</b>	<b>10.3%</b>	<b>4.3%</b>	<b>5.2%</b>	<b>2.3%</b>
<b>DPFP ex Private Markets</b>	<b>16.7%</b>	<b>3.4%</b>	<b>7.7%</b>	<b>5.5%</b>
Policy Index (75/25)*	15.7%	4.0%	7.8%	6.9%
60 ACWI/40 AGG	15.1%	1.1%	6.9%	5.5%

**As of 12/31/23, DPFP's portfolio was comprised of 78% Equity (including Legacy)/22% Fixed Income & Credit. However, over the last 7 years, the Fund has averaged a 60/40 allocation, which is why the 60/40 benchmark is provided for informational purposes. The Policy Index is the official DPFP Benchmark.**

**A 60/40 asset allocation is not a typical long-term institutional asset allocation, while a 75/25 or 80/20 is more typical**

\*The Policy Index is composed of each of DPFP's asset class benchmarks weighted by the target allocation to the asset class. 3% 3-Mo T-Bill / 6% US 1-3 Yr Agg / 4% Agg / 4% US Corp HY / 4% US Lev Loan / 4% JPM EMD / 55% ACWI IMI / 5% MSCI EM / 5% Russell 3000 + 2% / 5% NCREIF Property / 5% NCREIF Farmland

# Recommendation: new reference benchmark



Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>DPFP (78/22)</b>	<b>10.3%</b>	<b>4.3%</b>	<b>5.2%</b>	<b>2.3%</b>
<b>DPFP ex Private Markets</b>	<b>16.7%</b>	<b>3.4%</b>	<b>7.7%</b>	<b>5.5%</b>
Policy Index (75/25)	15.7%	4.0%	7.8%	6.9%
75 ACWI/25 AGG	18.4%	3.9%	9.6%	7.0%
60 ACWI/40 AGG	15.1%	1.1%	6.9%	5.5%

**A 60/40 benchmark is appropriate when looking backwards, but as DPFP has increased its equity allocation in recent years, a 75/25 benchmark should be added in addition to the policy index to measure performance**

**The closer to the present, the more relevant the 75/25 benchmark is, and when gauged by these standards, DPFP has outperformed over the 3-year time period**

Source: Dallas Police & Fire Pension System, *Fund Evaluation Report December 31st, 2023*, and Morningstar Direct as of 12/31/23

\*An 80 ACWI/20 AGG benchmark is shown because that is DPFP's current strategic allocation

# DPFP public equities have under-performed ACWI over the last 3 years, yet have outperformed over the last 10 years



Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year
DPFP Public Equities	20.0%	5.2%	11.7%	8.8%
MSCI ACWI	22.2%	5.8%	11.7%	7.9%

- **ACWI is an appropriate benchmark for measuring performance**
- **DPFP has picked good performing public equity managers over the last 10 years**
- **Our assumption is the recent underperformance can be attributed to an under-allocation to US markets**

Source: Dallas Police & Fire Pension System, *Fund Evaluation Report December 31st, 2023*, and Morningstar Direct as of 12/31/23

# Label analysis gives us a better understanding



Asset Class	% of Portfolio
Global Equity	46.5%
Emerging Markets	4.6%
<b>Total Equity</b>	<b>51.1%</b>

On their reporting, Dallas Police & Fire lists they are invested in 46.5% "Global Equity"

Asset Class	% of Portfolio
US Equity	25.4%
Developed Markets	20.0%
Emerging Markets	5.4%
<b>Total Equity</b>	<b>50.8%</b>
Cash	0.4%

When you analyze DFPF's Global Equity funds manager by manager, there is a mix of US Equity, Developed Markets Equity, Emerging Markets Equity, and Cash

Source: Dallas Police & Fire Pension System, *Meketa Fund Evaluation Report*, as of September 30, 2023

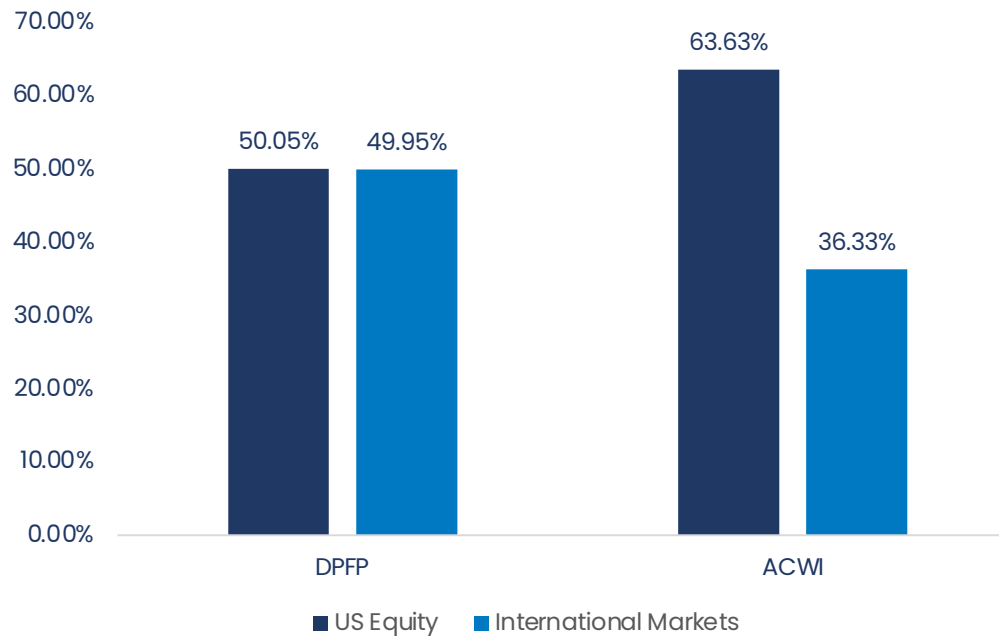


# When you compare DPFP's allocation to ACWI, it is allocated differently



DPFP's Asset Allocation compared to its benchmark is:

Under-weight US Equity  
Over-weight International Markets



Source: Dallas Police & Fire Pension System, *Fund Evaluation Report December 31st, 2023*

# Historical advantages of higher allocation to US equity\*



- Foreign equities have historically underperformed US equities
- Foreign equities have historically been more volatile than US equities
- Foreign equities have currency risk costs

Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year	20-Year
<b>S&amp;P 500</b>	26.29%	10.00%	15.69%	12.03%	9.69%
<b>Russell 3000</b>	25.36%	8.06%	14.61%	10.89%	9.06%
<b>MSCI ACWI</b>	22.20%	5.75%	11.72%	7.93%	7.55%
<b>Developed Markets Index</b>	18.24%	4.02%	4.95%	4.28%	5.59%
<b>Emerging Markets Index</b>	18.59%	3.36%	7.24%	4.01%	7.94%

20 Year	S&P 500	Russell 3000	MSCI ACWI	Developed*	Emerging*
<b>Volatility (Risk)</b>	14.89%	15.49%	15.86%	16.73%	21.80%

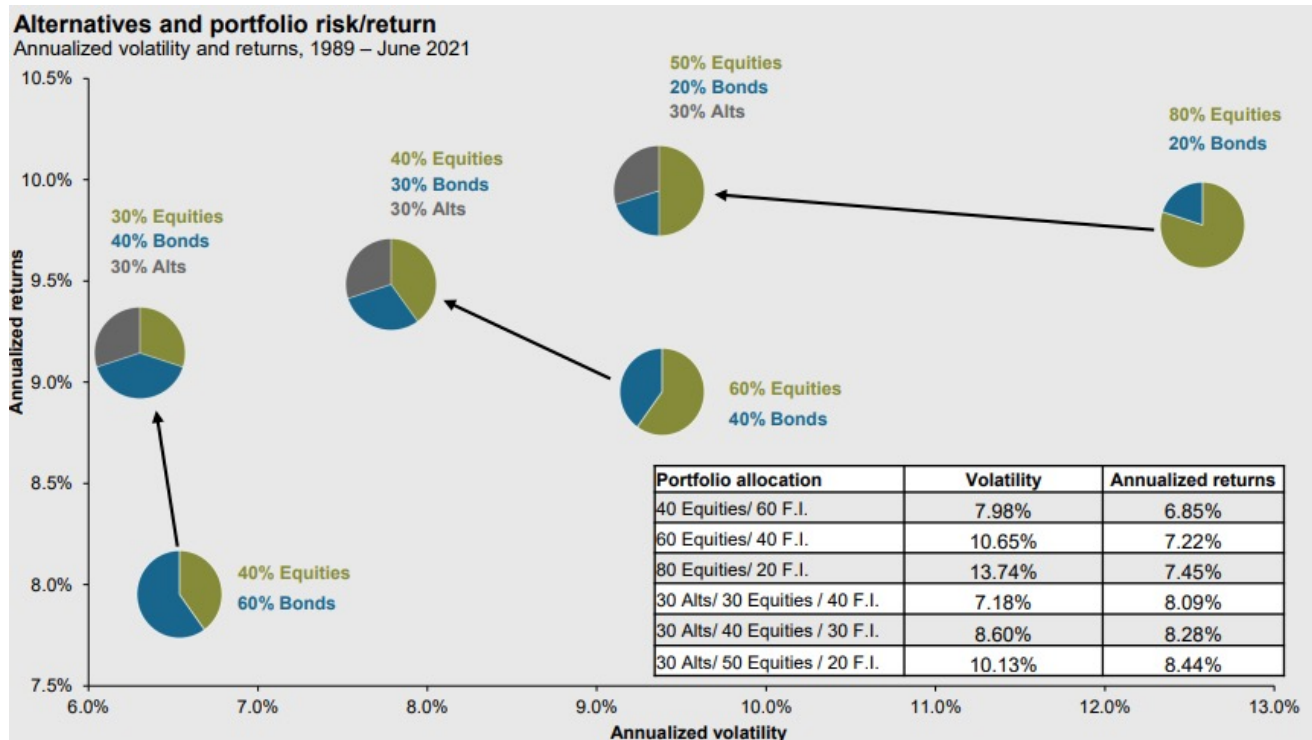
\*Past performance does not guarantee future results

Source: Morningstar Direct as of December 31st, 2023

Developed markets Index: MSCI EAFE; Emerging Markets Index: MSCI Emerging Markets

# DPFP is under-allocated to private equity: this can increase the risk in terms of volatility of the portfolio and decrease returns

Data as of 12/31/23	PE % of Portfolio
DPFP Current	11.3%
DPFP Target	5.0%
National Average*	14.7%
Texas Average*	17.8%

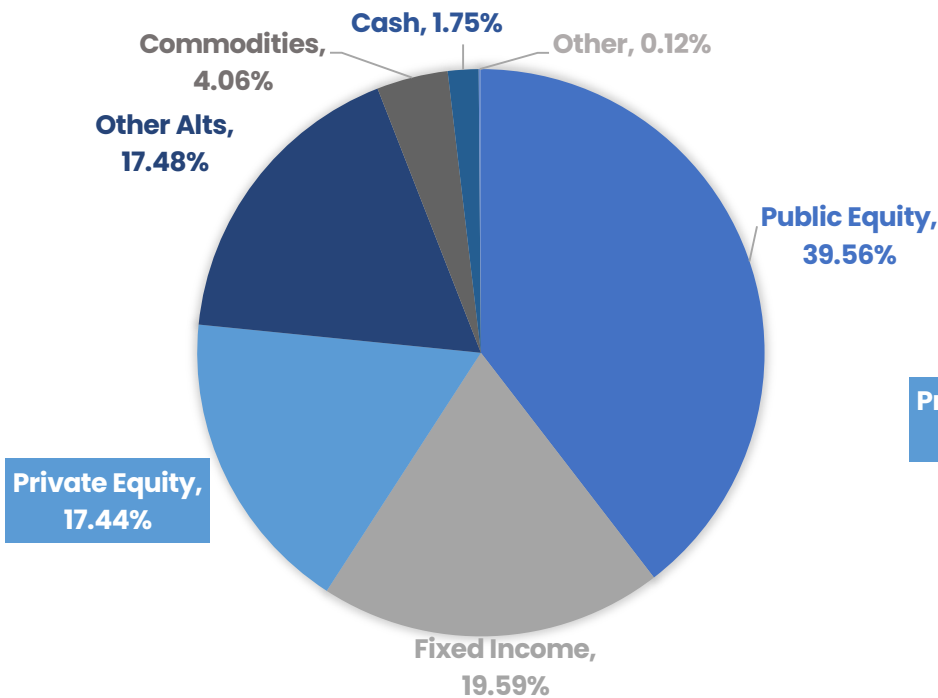


Source: JPMorgan Guide to the Markets

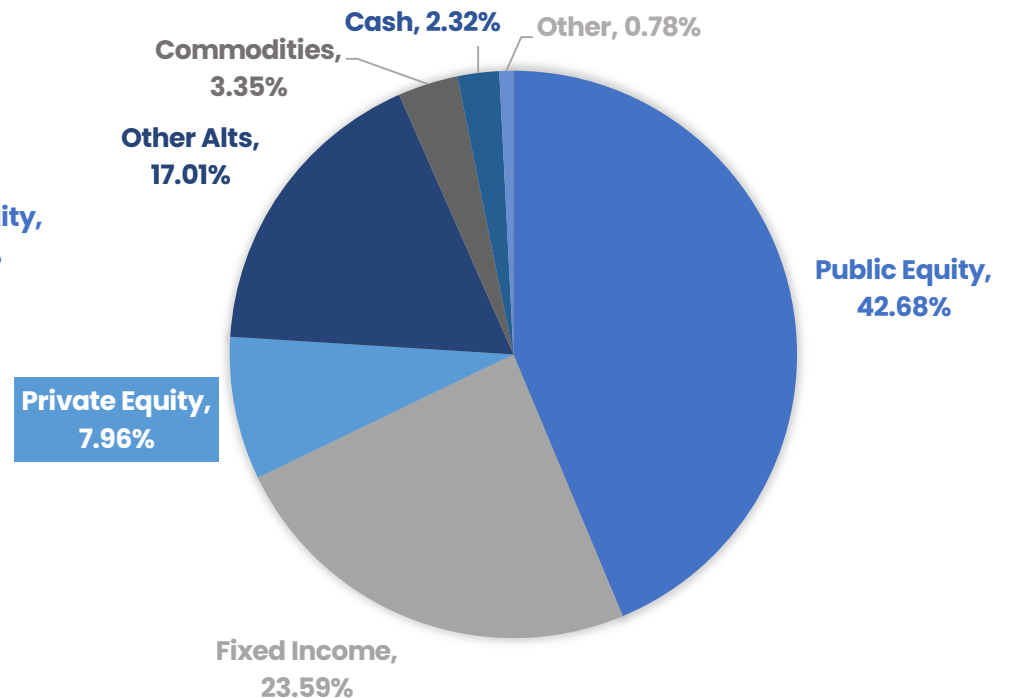
\*<https://publicplansdata.org/public-plans-database/browse-data/>

# DPFP's allocation resembles a bottom quartile more than a top quartile pension

## Top Quartile Pension Funds



## Bottom Quartile Pension Funds



**DPFP has 5% allocation to PE as its target, below even bottom quartile funds**

Source: <https://publicplansdata.org/public-plans-database/browse-data/>, data as of 12/31/22

# Reasons for under-allocating to private equity



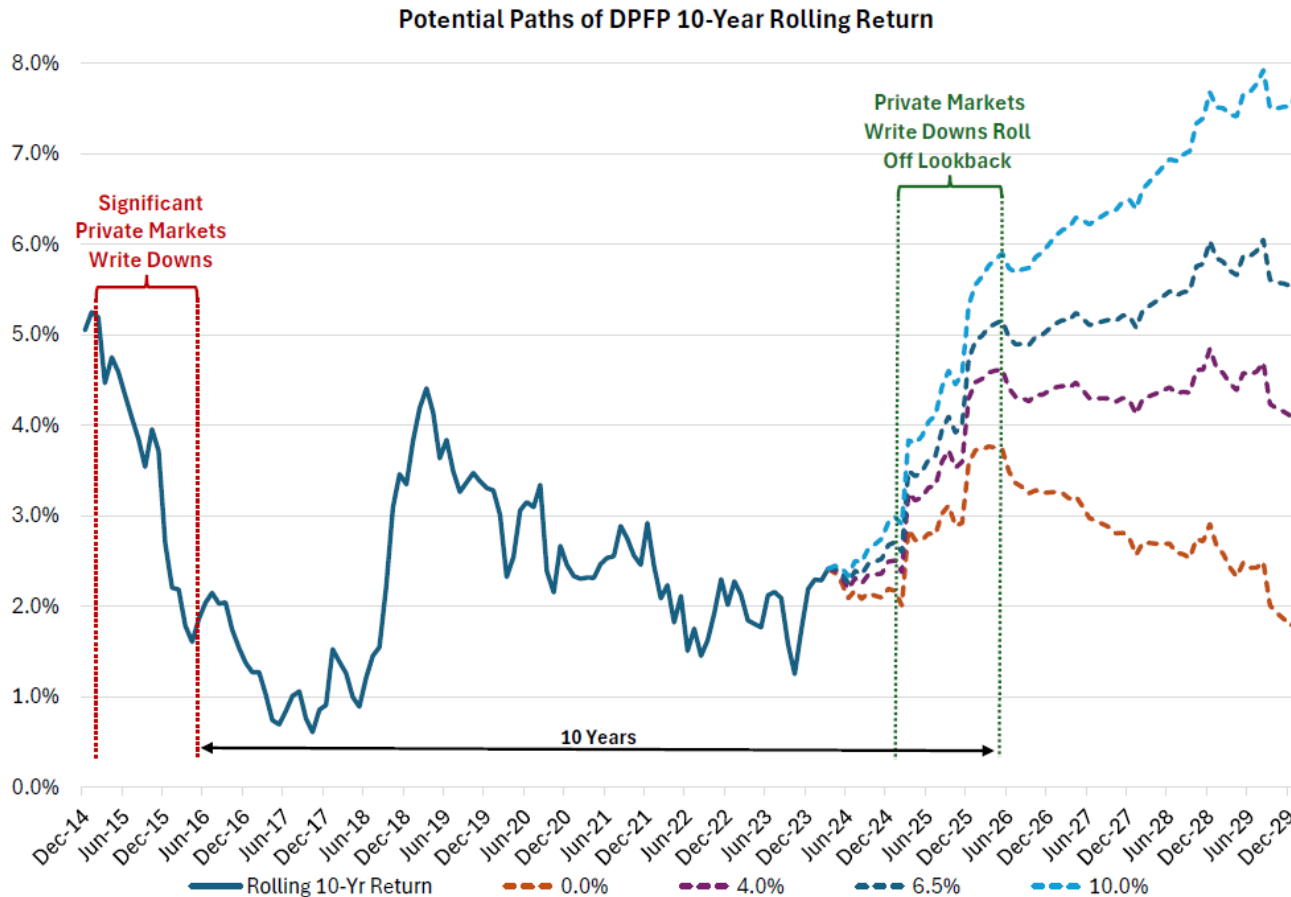
## After sitting down with DPFP staff, we learned some of the rationale and causes for the private equity allocation:

- In 2018, under the new Board, staff worked with Meketa to set a long-term private equity allocation at 5%. At the time, the actual private equity allocation was 13% and the overall private markets allocation was 49%.
- They successfully navigated off-loading \$1.4B of poor performing legacy assets since 9/30/16 and have plans to continue to do so.
- They have concerns over liquidity issues, given DPFP still has 25% of the portfolio allocated to private markets. Allocating to new private markets funds would lower the fund's liquidity profile.
- That being said, staff is working on an updated Asset Allocation Policy that would increase the target allocation to private markets from 15% to 18% and expects to begin making initial new commitments in early 2025.
- Staff is working on plans to rebuild the private markets portfolio. Specialty investment consultant, Albourne, was selected by the Board in 2023 to oversee all private market asset classes.



**Objective 2: Assess the overall performance and current/historical rate of return of the investment portfolio**

# DPFP's 10-year returns should improve when legacy asset returns from prior years roll off



Source: Total Fund net monthly returns through 3/31/2024, DPFP Staff analysis. Dotted lines represent hypothetical path of the ten year net return if a given annual return were to be consistently achieved moving forward.

**Even if the portfolio were to earn 0% over the next two years, the 10-year return will still improve**

# DPFP has performed adequately in its public equity and fixed income, but has lagged in its private market investments



Data as of 12/31/2023	1-Year	3-Year	5-Year	10-Year
DPFP Public Equity	20.0%	5.2%	11.7%	8.5%
MSCI ACWI	21.6%	5.5%	11.5%	7.8%
DPFP Fixed Income	9.8%	-0.3%	2.2%	2.7%
Bloomberg Agg	5.5%	-3.3%	1.1%	1.8%
DPFP Private Equity	-8.0%	11.4%	2.7%	-3.7%
Russell 3000 + 2%	22.8%	11.6%	11.3%	13.5%
DPFP Real Assets	0.7%	4.7%	2.5%	0.1%
Real Assets Policy Index	-1.4%	6.7%	5.7%	7.7%



# DPFP's private markets portfolio is generating negative value



## Private Equity Portfolio

Fund Name	Vintage Year	Gain/Loss	Net IRR	Quartile
Hudson Clean Energy	2009	\$(19,526,488)	(20.97%)	4*
Lone Star CRA	2008	\$22,640,961	5.34%	4
Lone Star Growth Capital	2006	\$(9,614,842)	(20.47%)	4
Lone Star Opportunities V	2012	\$(70,621,681)	(36.17%)	4
Lone Star Bridge Loan	2020	\$(362,000)	(6.19%)	4*
North Texas Opportunity Fund	2000	\$(8,592,527)	0.68%	2
Industry Ventures Partnership IV	2016	\$6,233,846	21.93%	1
Huff Energy Fund LP	2006	\$56,936,429	3.50%	N/A
<b>Total</b>		<b>\$(22,906,302)</b>	<b>(6.54%)</b>	

## Private Credit Portfolio

Fund Name	Vintage Year	Gain/Loss	Net IRR	Quartile
Huff Alternative Fund	2000	\$12,676,607	1.74%	2
Highland Crusader Fund	2003	\$16,725,841	4.67%	N/A
Riverstone Credit Partners LP	2016	\$2,038,749	5.01%	4
<b>Average</b>		<b>\$31,441,197</b>	<b>3.81%</b>	

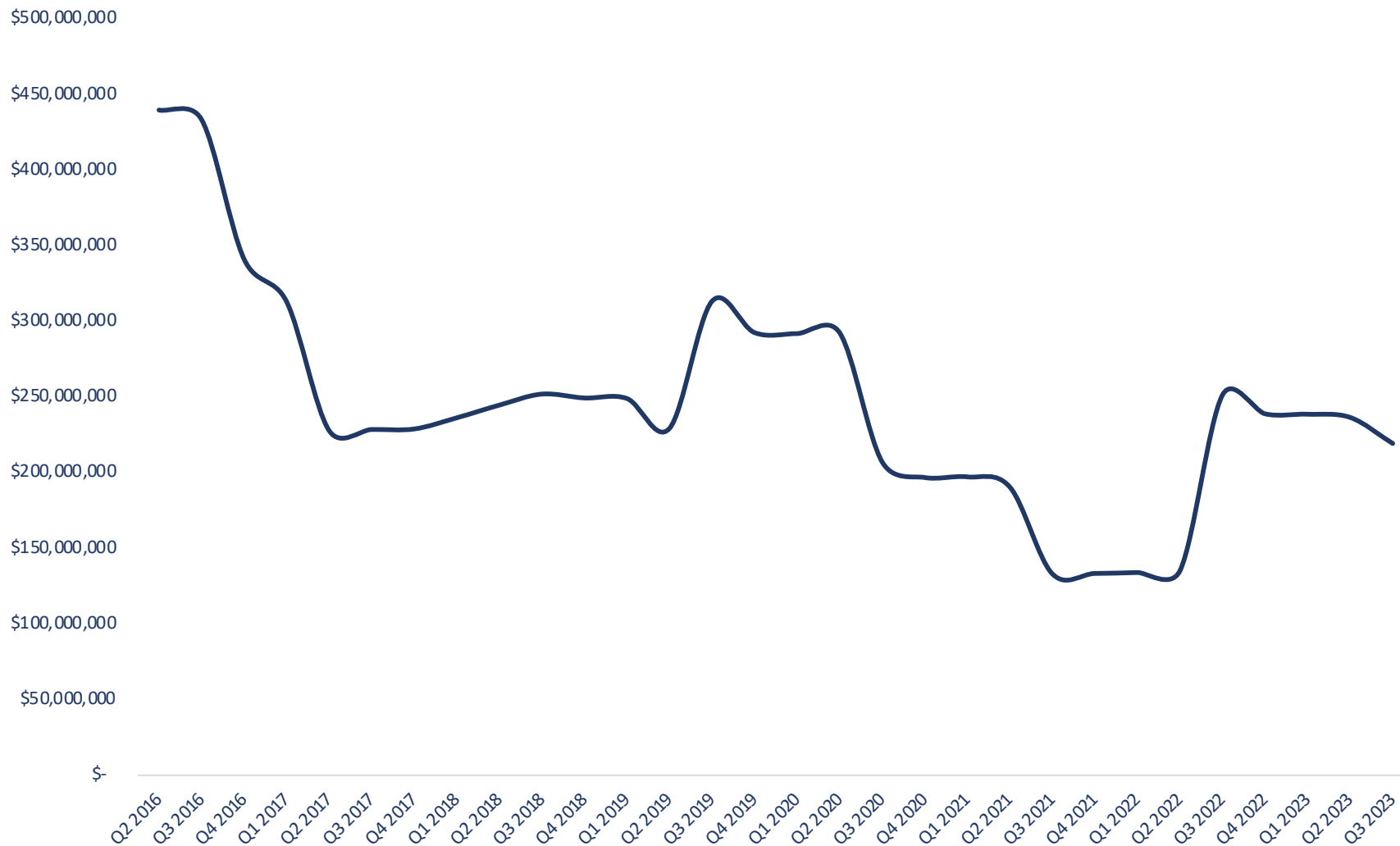
Source: 2023 Q3 Dallas Police & Fire Pension Meketa Private Markets Performance Report. <https://www.dfp.org/-financial-/investments/>. Preqin Alternative Assets Database. <https://pro.preqin.com/discover/funds>

\*Quartile ranking unavailable on Preqin, but has a negative IRR

# DPFP has been lowering its existing allocation of legacy assets and private equity



**They have successfully managed to offload legacy assets, but without replacing them, they are likely to not generate strong future returns**



# Under-allocating to private equity will make it difficult to succeed in the long-term



**Private Equity is not the problem, legacy asset PE managers are the problem**

Data as of 12/31/23 PE % of Portfolio	
DPFP Current	11.3%
DPFP Target	5.0%
National Average	14.7%
Texas Average	17.8%

Data as of 12/31/23 10 Year Returns	
DPFP	-3.7%
National Average*	15.2%
TX Peer Group Average**	15.5%

**DPFP is under-allocated to private equity compared to its peers**

Source: <https://publicplansdata.org/public-plans-database/browse-data/>

\*U.S. public pension funds earn 10-year median return of 15.2% from private equity, Pensions & Investments

\*\*Peer Group consist of similar-size funds in Texas reporting 10-Year PE Returns: Houston Firefighters Relief and Retirement Fund,, Houston Municipal Employees' Pension System, Austin Firefighters Retirement Fund, Texas County and District Retirement System, Employees' Retirement Fund of the City of Dallas

# Utilizing a top quartile allocation with indices could have resulted in top quartile returns



As of 12/31/23	Weighting*	1-Year	3-Year	5-Year	10-Year
Public Equity	39.6%	22.2%	5.8%	11.7%	7.9%
Fixed Income	21.5%	9.6%	-0.6%	3.2%	3.2%
Private Equity	17.4%	9.3%	14.1%	17.9%	15.6%
Other Alts	17.5%	8.2%	8.8%	8.0%	6.7%
Commodities	4.1%	-7.9%	10.8%	7.2%	-1.1%
<b>Top Quartile Allocation</b>	<b>100.0%</b>	<b>13.6%</b>	<b>6.6%</b>	<b>10.1%</b>	<b>7.7%</b>
<b>DPFP (78/22)</b>	<b>100.0%</b>	<b>10.3%</b>	<b>4.3%</b>	<b>5.2%</b>	<b>2.3%</b>
<b>DPFP ex Privates</b>	<b>100.0%</b>	<b>16.7%</b>	<b>3.4%</b>	<b>7.7%</b>	<b>5.5%</b>

**It should be noted that returns in asset categories have to take into account risk and liquidity**

Source: Meketa, Dallas Police & Fire Pension System: Fund Evaluation Report as of December 31, 2023

\*Weightings come from previous slide of the averages for top quartile pension funds nationally. Note that returns may differ based upon market fluctuations and allocation drift.

Indices used: Public Equity – MSCI ACWI, Fixed Income – 50% Bloomberg Agg + 50% Bloomberg US Corporate High Yield, Private Equity – Cambridge Associates Private Equity Index, Other Alts – Indxx Private Credit TR + S&P Global Infrastructure + Cambridge Associates Real Estate Index (equal-weighted), Commodities – Dow Jones Commodity



## **Objective 3: Identify appropriate state and national benchmarking for asset allocation and performance**

# Benchmarking basics

**“If you can’t measure it, you can’t manage it” – Peter Drucker**

## **We should define a strong peer group**

- If peers are significantly outperforming us, then we should understand why we are underperforming
- Underperformance will show up in asset allocation and manager selection

## **Benchmarking helps the City and the Plan in many ways**

- It provides transparency for performance, management, and governance’s effectiveness
- It can give us new ideas and insight
- Done correctly, it lays the groundwork for outperformance

**If we are below average, we must get to average; if we are average, let us work our way to above average**

# DPFP vs. largest Texas cities



Data as of 6/30/23	1-Year	3-Year	5-Year	10-Year
<b>Dallas Police and Fire</b>	<b>17.7%</b>	<b>4.3%</b>	<b>4.1%</b>	<b>2.1%</b>
<b>DPFP ex Private Markets</b>	<b>13.2%</b>	<b>6.4%</b>	<b>5.5%</b>	<b>5.7%</b>
Houston Firefighters	4.2%	11.7%	8.5%	8.0%
Houston Police	7.8%	12.0%	8.6%	8.3%

Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>Dallas Police and Fire</b>	<b>10.3%</b>	<b>4.3%</b>	<b>5.2%</b>	<b>2.3%</b>
<b>DPFP ex Private Markets</b>	<b>16.7%</b>	<b>3.4%</b>	<b>7.7%</b>	<b>5.5%</b>
Austin Fire	8.4%	4.4%	8.3%	6.8%
Austin Police	11.5%	5.1%	9.4%	6.4%
San Antonio Fire & Police	11.9%	4.3%	-	6.4%

Source: Texas Pension Review Board. <https://data.prb.texas.gov/plans/index.html>

# DPFP vs. national and Texas averages



Data as of 12/31/23	3-Year	5-Year	10-Year
<b>Dallas Police and Fire</b>	<b>4.3%</b>	<b>5.2%</b>	<b>2.3%</b>
<b>DPFP ex Private Markets</b>	<b>3.4%</b>	<b>7.7%</b>	<b>5.5%</b>
National Top Quartile	5.5%	9.0%	7.1%
National Average	4.5%	8.4%	6.4%
National Bottom Quartile	3.6%	7.7%	6.1%
Texas Top Quartile*	5.3%	9.0%	6.6%
Texas Average*	5.1%	8.6%	6.5%
Texas Bottom Quartile*	4.3%	7.9%	6.2%

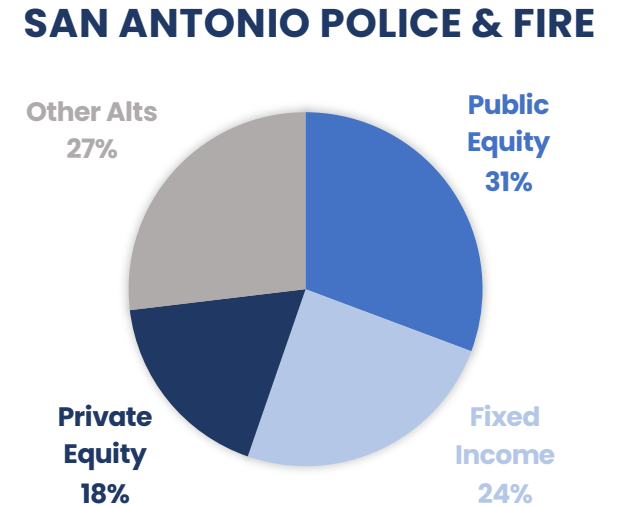
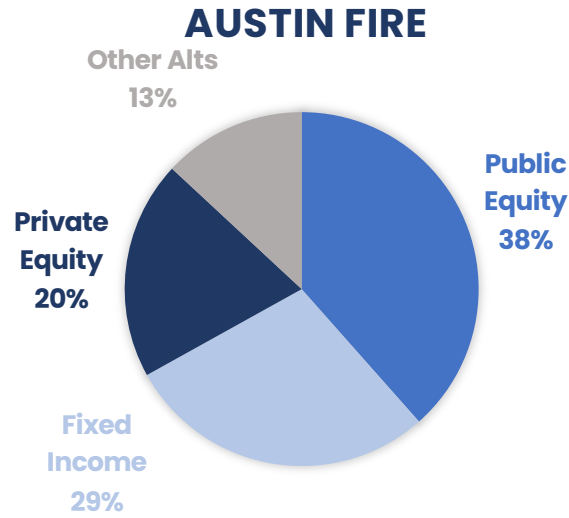
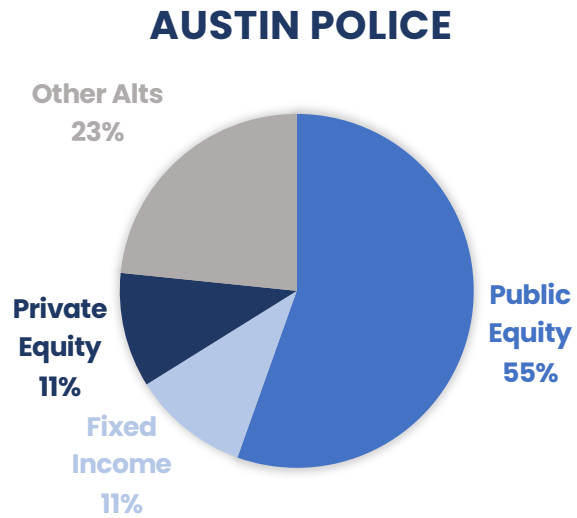
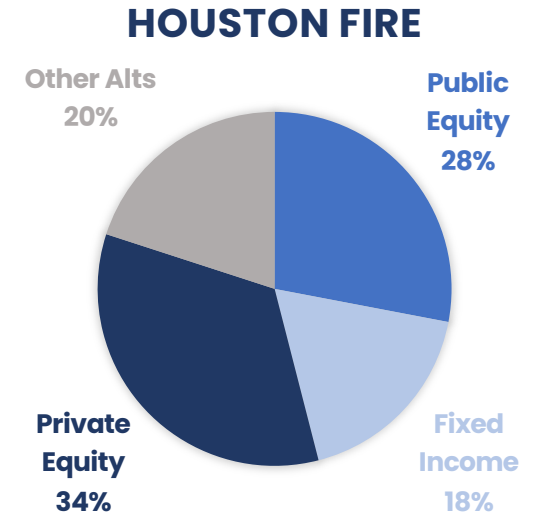
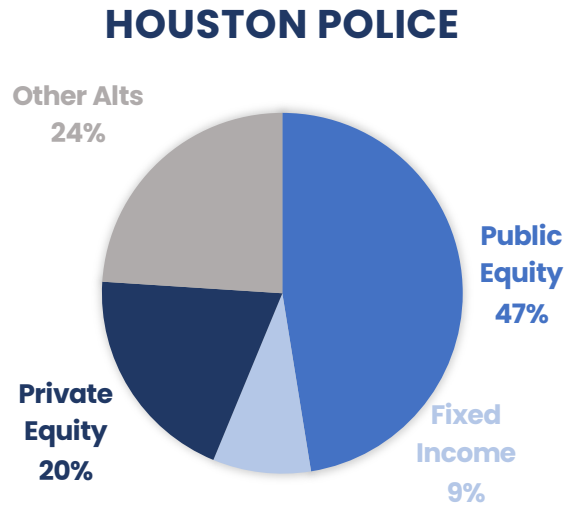
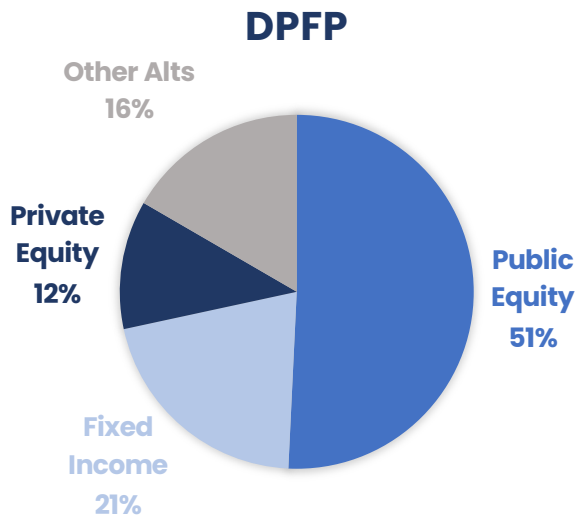
Source: <https://publicplansdata.org/public-plans-database/browse-data/>

National quartile rankings provided by Meketa

\*Quartile rankings only taken from Texas Plans with fiscal years ending 12/31/23

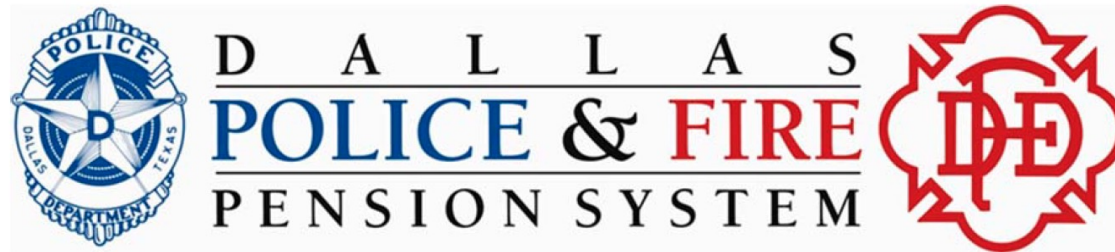


# DPFP allocation vs. largest Texas cities



Source: Year End Reports as of 12/31/22 from each pension

Note these are different than DPFP's current allocation. To compare to peers, you have to do so over the same time frame.



## **Objective 4: Identify areas of potential risk and propose risk mitigation strategies**

# Some pension risks to consider

Liabilities – Current and Future

Governance Risk

Asset Allocation Risk

Manager Selection Risk

Monitoring Risk

# The City of Dallas needs to increase its knowledge of DPFP



There are many parties affected by the running of the pension: the police and firefighters, the staff of DPFP, and the taxpayers of Dallas.

**To best ensure the health of all stakeholders, the City of Dallas should take it upon itself to become more knowledgeable of the Plan**

**The City needs to increase its knowledge on these elements of the Plan:**

- Asset allocation, risk, and liquidity
- Policies and procedures
- Reporting and benchmarking

**This can be enabled by the City hiring:**

- Internal staff or dedicated outside experts that work with the City and the Pension with ongoing communication and two-way feedback



## **Objective 5: Evaluate the effectiveness of the current asset allocation strategy**

# The biggest contributor to DPFP's under-performance is the under-allocation to and poor performance of PE and other alternatives



As of 6/30/23	Allocation		Returns (5 Year)	
	DPFP	TX Peer Group	DPFP	TX Peer Group
Public Equity	51.4%	43.3%	8.2%	7.5%
Private Equity	12.2%	21.3%	4.8%	17.5%
Fixed Income	20.5%	18.1%	1.1%	2.6%
Other Alts	15.8%	21.5%	2.5%	6.9%

**While their Texas peers (selected for illustrative purposes) earned 17.5% on PE and 6.9% on other alts, DPFP was under-allocated to private equity by 9.1% and other alts by 5.7%**

# Reasons the private markets target allocation for DFPF should be higher

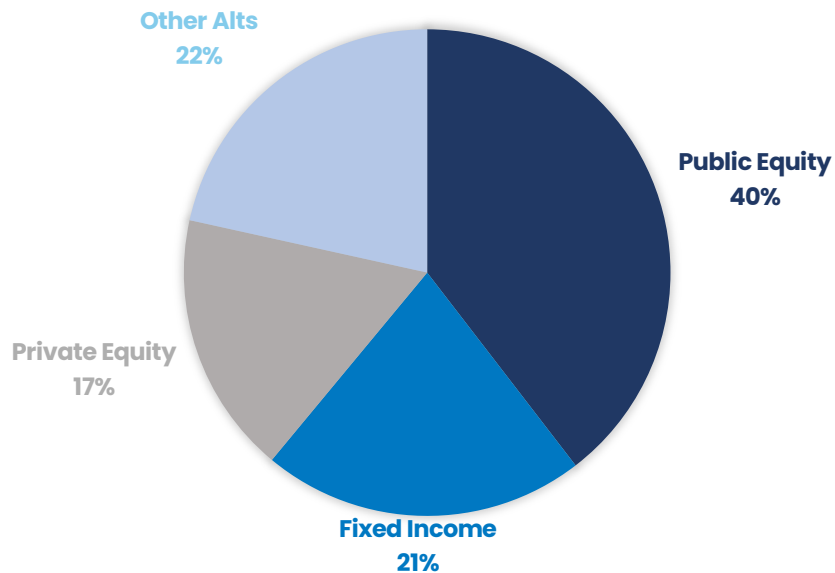


**While we understand the issues that have plagued DFPF's private markets portfolio in the past, it would be most beneficial to the Fund to raise its target allocation to private markets:**

- The private market target allocation was set in 2018, so enough time has passed for re-evaluation
- DFPF will need to increase long-term risk adjusted returns to reduce the City's contribution limits
- Private equity (and other private assets) is an asset class that historically has the highest expected risk adjusted return
- New private equity investments can create other issues that must be dealt with
- But, new investments can be made into private assets without causing J-Curve/liquidity issues, such as interval funds, secondaries, and private credit

# Under-allocation to PE/PM all but ensures DFPF will not be a top-performing pension fund and improve its funding status

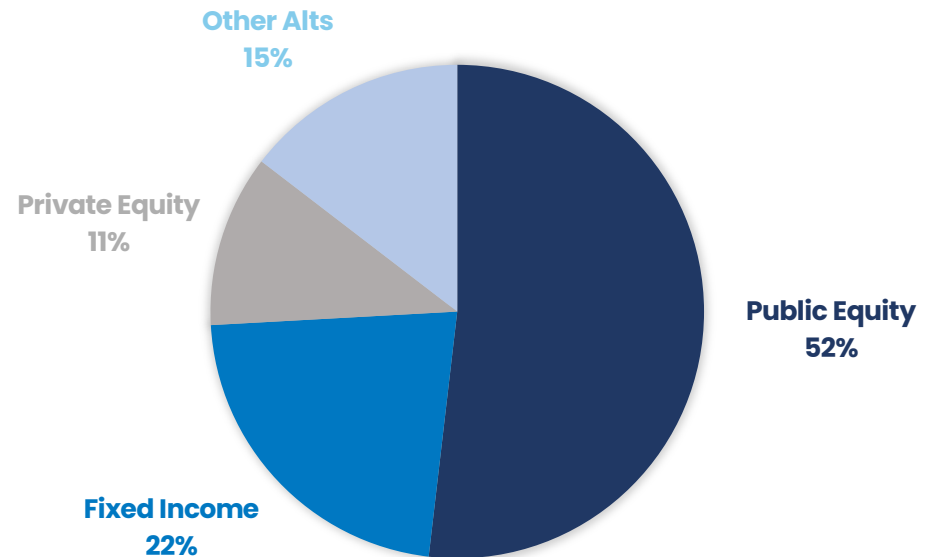
**National Top Quartile Pensions**



**Total Returns**

1-Year	3-Year	5-Year	10-Year
-3.6%	8.5%	8.1%	8.6%

**DFPF**



**Total Returns**

1-Year	3-Year	5-Year	10-Year
-2.2%	1.5%	2.8%	2.0%

Source: <https://publicplansdata.org/public-plans-database/browse-data/> as of 12/31/22



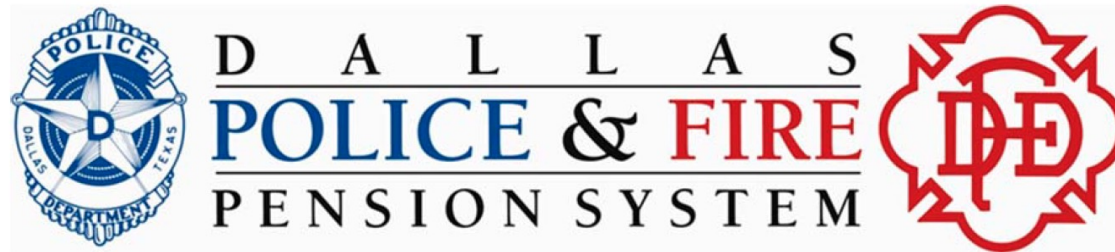
# The picture this paints

- Without better investment performance, Dallas Police and Fire will have a more difficult time with cash outflows from the Plan and improving its funding ratio
- Private equity is an asset class that more easily allows for the Fund to generate excess returns

## Which is what DFPF's peers are doing

	5-Year Annualized PE Returns
<b>DPFP</b>	<b>4.3%</b>
Dallas ERF	16.0%
Houston MEPS	17.6%
Fort Worth ERF	19.1%
Texas TRS	13.9%
Texas MRS	18.3%
Texas CDRS	16.9%
Houston Firefighters	17.4%
Austin Fire	20.1%
Austin Police	11.7%
<b>Average</b>	<b>16.8%</b>

Data as of 12/31/22



## **Objective 6: Evaluate the effectiveness of the current manager selection and their strategies**

# DPFP's private markets pre-2016 manager selection is a large driver of its underperformance



As of 6/30/23	Returns (5 Year)	
	DPFP	TX Peer Group
Public Equity	8.2%	7.5%
Private Equity	4.8%	17.5%
Fixed Income	1.1%	2.6%
Other Alts	2.5%	6.9%

**The gap between DPFP's private market returns and their peers will continue to drive underperformance if left unaddressed**

Peer Group consist of similar-size funds in Texas: Houston Firefighters Relief and Retirement Fund, Houston Police Officers' Pension System, Houston Municipal Employees' Pension System, Austin Police Retirement System, Austin Firefighters Retirement Fund, Fort Worth Employees' Retirement Fund, Texas County and District Retirement System

# DPFP has performed competitively in its public equity portfolio compared to Texas peers



Data as of 6/30/23	3-Year	5-Year	10-Year
DPFP	10.9%	8.2%	9.3%
HMEPS	9.4%	6.8%	8.2%
Houston Police	12.6%	9.1%	9.7%
Austin Police	11.6%	8.1%	9.4%
Fort Worth ERF	10.7%	6.1%	-

# PE manager selection was a problem for DFPF pre-2016



Fund Name	Vintage Year	DPI	Net IRR	Quartile
Huff Alternative Income Fund	1995	1.67	17.8%	2
Oaktree Fund IV	2001	1.65	28.0%	1
Merit Energy Partners E-1	2004	2.13	14.5%	N/A
Pharos Capital Partners IIA	2004	0.64	1.0%	3
Merit Energy Partners F-1	2005	0.43	(17.2%)	4*
Highland Credit Ops	2006	0.85	(2.0%)	4*
Levine Leichtman Capital Partners Deep Value Fund	2006	1.03	0.7%	4
Ashmore Global Special Situations Fund IV	2007	0.62	(9.0%)	4
BankCap Partners Fund I	2007	1.25	2.6%	4
HM Capital Sector Performance Fund	2007	0.94	(4.0%)	4
Oaktree Loan Fund 2x	2007	1.01	0.3%	4
Pharos Capital Co-Investment, LLC	2007	0.50	(10.0%)	4*
CDK Southern Cross	2008	0.00	(20.1%)	4*
Levine Leichtman Capital Partners IV	2008	1.66	20.0%	2
Merit Energy Partners G	2008	0.68	(10.0%)	4*
Pharos Capital Co-Investment, LP	2008	1.69	8.0%	N/A
Yellowstone Capital	2008	0.29	(27.7%)	4*
Lone Star Fund VII	2010	1.71	47.0%	2
Merit Energy Partners H	2010	-0.14	(13.8%)	4*
Oaktree Power Opportunities Fund III	2010	1.61	1.03%	3
Kainos Capital Partners	2012	1.76	24.8%	2
BankCap Partners Opportunity Fund	2013	0.93	(6.0%)	4
Levine Leichtman Capital Partners V	2013	1.64	17.20%	3
Levine Leichtman Capital Partners Private Capital Solutions	2013	2.16	14.0%	N/A
Lone Star Fund VIII	2013	1.05	7.90%	4
Pharos Capital Partners III	2013	1.19	13.0%	1
Lone Star Fund IX	2014	1.12	12.2%	3

Over half of the funds are **Bottom Quartile Performers**

Over one-third of the funds have a **Negative IRR**

**Only 2 funds** are Top Quartile Performers

Source: 2023 Q1 Dallas Police & Fire Pension Meketa Private Markets Performance Report. <https://www.dfpf.org/-financial-/investments/>. Preqin Alternative Assets Database. <https://pro.preqin.com/discover/funds>

\*Quartile ranking unavailable on Preqin, but has a negative IRR

# Pre-2016 PE manager selection remains a problem for DFPF



## Private Equity Portfolio (\$219mm)

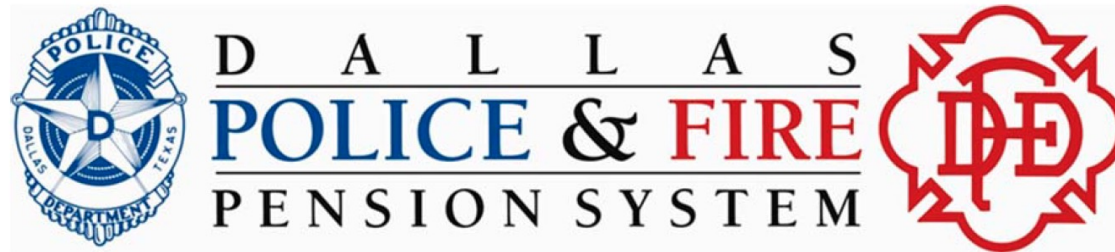
Fund Name	Vintage Year	Gain/Loss	Net IRR	Quartile
Hudson Clean Energy	2009	\$(19,526,488)	(20.97%)	4*
Lone Star CRA	2008	\$22,640,961	5.34%	4
Lone Star Growth Capital	2006	\$(9,614,842)	(20.47%)	4
Lone Star Opportunities V	2012	\$(70,621,681)	(36.17%)	4
Lone Star Bridge Loan	2020	\$(362,000)	(6.19%)	4*
North Texas Opportunity Fund	2000	\$(8,592,527)	0.68%	2
Industry Ventures Partnership IV	2016	\$6,233,846	21.93%	1
Huff Energy Fund LP	2006	\$56,936,429	3.50%	N/A
<b>Total</b>		<b>\$(22,906,302)</b>	<b>(6.54%)</b>	

## Private Credit Portfolio (\$3.8mm)

Fund Name	Vintage Year	Gain/Loss	Net IRR	Quartile
Huff Alternative Fund	2000	\$12,676,607	1.74%	2
Highland Crusader Fund	2003	\$16,725,841	4.67%	N/A
Riverstone Credit Partners LP	2016	\$2,038,749	5.01%	4
<b>Average</b>		<b>\$31,441,197</b>	<b>3.81%</b>	

Source: 2023 Q3 Dallas Police & Fire Pension Meketa Private Markets Performance Report. <https://www.dfpf.org/-financial-/investments/>. Preqin Alternative Assets Database. <https://pro.preqin.com/discover/funds>

\*Quartile ranking unavailable on Preqin, but has a negative IRR



## **Objective 7: Review the adherence to investment policies and guidelines**

# The DPFP Investment Policy Statement observations



## Based on our initial review of the IPS, there are several potential enhancements that we would suggest:

- While DPFP has a robust monitoring policy for Public Managers, the language in Section 7.B could more explicitly outline current staff procedures (quarterly manager calls and written internal reviews, annual review with consultant researcher, etc.)
- In Section 7.A Investment Manager Search and Selection, make clear that IAC reviews and approves written Search Process document
- Add language to clarify that the consultant flags underperforming managers to the Board/IAC on a quarterly basis
- Consider adding a section on Control Procedures to the IPS that addresses how the consultant will provide information to the board regarding performance objectives for each manager, manager probation and watch list criteria, evaluation and analysis of underperformance.





## **Objective 8: Review the current fee structure and trading costs**

# DPFP's expenses are below average when compared to peers



System	Fiscal Year End	Net Total Assets	SB 322 Total Direct & Indirect Expenses	SB 322 Total Investment Expense	Annual Audit Investment Expense
Dallas Police & Fire Pension System–Combined Plan	12/31/2022	\$1,824	0.64%	0.80%	0.48%
Houston Police Officers' Pension System	6/30/2023	\$7,208	2.20%	2.21%	0.11%
San Antonio Fire & Police Pension Fund	12/31/2022	\$3,586	1.19%	1.22%	0.41%
Houston Municipal Employees Pension System	6/30/2023	\$4,072	1.08%	1.16%	0.24%
Houston Firefighters' Relief & Retirement Fund	6/30/2023	\$5,109	0.98%	1.16%	0.18%
Fort Worth Employees' Retirement Fund	9/30/2023	\$2,605	1.03%	1.11%	0.15%
Austin Police Retirement System	12/31/2022	\$933	0.83%	0.88%	0.21%
Dallas Employees' Retirement Fund	12/31/2022	\$3,516	0.54%	0.56%	0.55%
Austin Employees' Retirement System	12/31/2023	\$3,279	0.22%	0.26%	0.16%
<b>Average</b>			<b>0.97%</b>	<b>1.04%</b>	<b>0.28%</b>

Source: <https://www.prb.texas.gov/wp-content/uploads/2024/07/2024.07.25-Board-Meeting-Packet.pdf>

# Considerations for the City of Dallas



**We recommend that the City of Dallas hire a qualified firm to help the City's understanding of the independently managed pension, who:**

1. Helps the City's understanding of factors contributing to the performance of other top performing peers
2. Works with city constituents to improve the City's understanding of the pensions
3. Conducts an ongoing analysis to help the City be better informed on any issues related to performance
4. As needed, prepares ongoing reports and clarifications for the City of Dallas
5. Is able to provide, as needed, recommendations for consideration to achieve best practice

**An improvement in long-term performance would increase the funding ratio and lessen the burden on the City and taxpayers**

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Past Performance is no Guarantee of Future Results

Diversification of your overall investment portfolio does not assure a profit or protect against a loss in declining markets

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## DPFP RESPONSE TO FINAL COMMERCE STREET REPORT

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Date: August 9, 2024  
To: City of Dallas and DPFP Board  
From: DPFP Investments Staff  
Subject: Commerce Street Investment Management Final Report on DPFP

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### **Executive Summary**

The City of Dallas engaged Commerce Street to provide a report evaluating the investment practices of both the Dallas Police and Fire Pension System (DPFP) and Dallas Employee's Retirement Fund. DPFP expresses its appreciation to the City of Dallas and Commerce Street Investment Management for the opportunity to comment on the Commerce Street report.

Over the past several months, DPFP's investment staff has met with Commerce Street on several occasions in an attempt to inform them of both institutional investment practices and how DPFP operates the plan. While some of the initial errors and misstatements in drafts of the report were corrected, the report provided by Commerce Street remains an incomplete and inaccurate representation of DPFP. Unfortunately, Commerce Street has chosen to omit substantial and material information provided by DPFP that offers readers appropriate context for understanding the System's past underperformance, current governance structure, and how DPFP is positioned to succeed in the future.

As required by state law, DPFP and all other public pension plans in Texas submit to the Pension Review Board (PRB), a formal Investment Practices and Performance Evaluation (IPPE) conducted by a firm with substantial experience in evaluating institutional investors. The IPPE report evaluates the appropriateness, adequacy, and effectiveness of a retirement system's investment practices and performance. The most recent DPFP IPPE, which can be found on the [PRB Website here](#), is a far more comprehensive and informed evaluation than the Commerce Street report. DPFP staff has provided the IPPE report to Dallas City Council Members, City of Dallas staff, and Commerce Street on several occasions.

The primary recommendation of the Commerce Street report appears to be that the City of Dallas should hire a qualified firm or internal staff to gain a better understanding of DPFP. The City already appoints a majority of the DPFP Board. The Board along with a very skilled and experienced Investment Advisory Committee (IAC) and Investment Consultants acting as fiduciaries provide robust oversight of all aspects of the investment function. DPFP does not believe that the City hiring internal staff or an outside group with no fiduciary responsibility could add any value.

The following pages outline selected areas where DPFP agrees with Commerce Street's observations but also highlights seemingly intentionally omitted information, and unsupported, misleading, or disputed investment claims within the final version of the Commerce Street report.

**DPFP Agreement with Commerce Street Observations**

- **Legacy assets (p. 3) and poor manager selection in the mid-2000s (p. 41, 42) are largely responsible for historical underperformance.**
  - DPFP agrees with this assessment and has hired a specialty private markets consultant, Albourne, to assist in building a robust and institutional quality private markets portfolio moving forward.
- **Commerce Street has recommended increasing the target allocation to private equity.**
  - DPFP staff is currently recommending an increase to the private markets target allocation – including increasing the private equity allocation and creating a new private credit allocation – as part of the Asset Allocation Study which has been underway since March 2024.

**Intentionally Omitted Information**

- **Objective 4: Identify areas of potential risk and propose risk mitigation strategies (p. 30).**
  - The report fails to provide any analysis of risks, nor does it offer any substantive recommendations for how these risks might be mitigated. Commerce Street was provided with extensive information as well as detailed explanations on the elements of plan risks listed on page 32 of the report (asset allocation, risk, and liquidity; policies and procedures; and reporting and benchmarking). Commerce Street omitted this information from the final report.
- **Objective 7: Review the adherence to investment policies and guidelines (p. 43).**
  - Commerce Street fails to evaluate whether DPFP adheres to investment policies and guidelines. The below excerpt from the most recent IPPE report includes this evaluation:

**Conclusions**

Subsection	Overall Status	Adhering to established policies?
A. Investment Policy Statement analysis	Meets Industry Best Practices	Yes
B. Asset allocation (and liability) process review and execution	Meets Industry Best Practices	Yes
C. Fees review and procedures	Meets Industry Best Practices	Yes
D. Governance processes	Meets Industry Best Practices	Yes
E. Investment manager selection and monitoring	Meets Industry Best Practices	Yes

- DPFP provided an in-depth explanation to Commerce Street of the Investment Policy Statement (IPS) with the intent of ensuring their understanding of institutional investment policies. DPFP also described the annual IPS review and Board approval process, as well as emphasizing that our IPS complies with both CFA and Texas PRB guidelines.
- Commerce Street’s recommendation that DPFP add a “Control Procedures” section to the IPS is not necessary. The IPS clearly addresses these objectives in Appendix C.

### **Unsupported, Misleading, or Disputed Investment Claims**

- **“Dallas Police & Fire’s recent returns have not been high enough to maintain the market value of the pension fund” (p. 8).**
  - DPF is unclear what this sentence intends to convey. If Commerce Street means to say that they would expect the market value to have dropped, this is not factually supported as DPF’s market value has been relatively stable since 2017. The table on page 8 does not support their conclusion as it shows an increase in both the market value of assets and the funded ratio.
  
- **“Need to target reducing volatility risk and improving risk adjusted asset allocation at DPF as well as PE manager selection” (p. 4); Having more private equity would reduce the risk of the portfolio (p. 15); and “Private equity (and other private assets) is an asset class that has the highest expected risk-adjusted return” (p. 35)**
  - Adding private equity does not decrease the risk of the portfolio – this is a fundamental concept that is widely accepted amongst institutional investors. Further, institutional investors concur that private equity is one of the riskiest asset classes.
  - The chart on page 15 of the report implies that adding alternatives to a portfolio reduces the volatility; however, volatility risk present in alternatives is far greater than what is measured by appraisal-based indices.
  - The 2023 Horizon Survey of Capital Market Assumptions, which compiles investment assumptions from institutional consultants across the country, presents a clear illustration of the higher risk inherent in private equity. The median annualized geometric return expectation for private equity over the next ten years is 9.5%, with a standard deviation of 22.6%. Compare this with a median return expectation of 6.9% and a standard deviation of 16.6% for domestic large cap equities.
  - While private equity has been one of the top performing asset classes looking backward, institutional consultants broadly acknowledge that the environment may very well be different moving forward.
  
- **“DPF’s portfolio was comprised of 78% Equity (including Legacy)/ 22% Fixed Income & Credit” (p. 9).**
  - DPF’s Policy Index, which is well defined in the IPS and was provided to Commerce Street on multiple occasions, is not a 75% Equity/25% Fixed Income index. Furthermore, Commerce Street is over-generalizing “equity” in their statement by including real estate, infrastructure, and agriculture investments in the “equity” category.
  - Additionally, Commerce Street’s assertion that a 75/25 or 80/20 allocation is more typical is not accurate, and no support is provided for this statement.

- **Benchmarks presented are not DFPF’s official benchmarks (p. 11, 20).**
  - For example, MSCI ACWI is presented rather than MSCI ACWI IMI, which is a broader representation of the investible public equity universe and is DFPF’s official benchmark for public equities.
  
- **Foreign equities are worse than domestic equities (p. 14).**
  - DFPF agrees that from the end of 2023 looking backward, domestic equities have performed better than foreign equities with less volatility. However, there is severe end-point bias. Analysis of rolling historical returns confirms that there are also periods when foreign equities have outperformed.
  - DFPF takes a global approach, hiring institutional quality investment managers who make informed decisions about where the best opportunities exist in the entirety of the opportunity set. This at times leads them to over- or underweight different geographies. Many institutional investors take a global approach to their public equity portfolio.
  
- **“Utilizing a top quartile allocation with indices could have resulted in top quartile returns” (p. 24).**
  - This analysis is flawed. Of course, choosing the best performing asset allocation on a backwards-looking basis would produce the best returns knowing that allocation drives a majority of return outcomes.
  - Additionally, many of the indices included are not investible, meaning an investor cannot simply “utilize” passive exposure to invest in private equity, private credit, or private real estate.
  
- **“We should define a strong peer group” (p. 26).**
  - Commerce Street’s selected peer group is inconsistent throughout the report. The peer group changes across pages 26, 27, 29, 34, 37, and 39.
  - Additionally, Commerce Street fails to explain why a small and rotating group of Texas-specific peers would be more robust than comparing with top performing peers across the nation (which DFPF does on a regular basis through quarterly consultant reporting).
  
- **Austin Police Asset Allocation (pg. 29)**
  - While Commerce Street asserts that more private equity is the solution to higher returns, Austin Police – which has the lowest private equity allocation of the peer plans shown – has one of the highest 1, 3, and 5 year returns as presented on page 27 for peer plans reporting returns as of 12/31/23.



- **“Under-allocation to PE/PM all but ensures DPFP will not be a top-performing pension fund and improve its funding status” (p. 36).**
  - This claim by Commerce Street seems to be based solely on historical performance of the private equity asset class, which any institutional investor would acknowledge is no guarantee of future results. Commerce Street fails to make any case, let alone a convincing one, that private equity is the best solution to achieving higher risk-adjusted returns.
  
- **“The gap between DPFP’s private market returns and their peers will continue to drive underperformance if left unaddressed” (p. 39).**
  - This statement seems to suggest that the private markets underperformance is not being addressed. DPFP has made significant progress in unwinding legacy investments in a prudent manner and continues to spend a significant amount of time addressing private markets.

# Employees' Retirement Fund of the City of Dallas



## Objectives 1-8

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Commerce Street Investment Management

# Discussion Topics

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- Obj 1 Asset Allocation Analysis (6)
- Obj 2 Historical Return Analysis (9)
- Obj 3 Identification of Peer Groups (14)
- Obj 4 Risk Mitigation Strategies (22)
- Obj 5 Asset Allocation Strategy (25)
- Obj 6 Manager Selection Evaluation (29)
- Obj 7 IPS Recommendations (34)
- Obj 8 Cost Analysis (36)



# Preliminary Disclosures



The analysis that follows is the result of a few weeks' work analyzing the Plans as well as peers we found relevant

There are certain assumptions made in this analysis that could be enhanced with further ongoing collaboration with both Plans

**We recommend that the best approach to achieving a complete analysis of the Plans is to continue to collaborate with their staffs to check key assumptions, gain a better understanding of how their Plans work, and receive the most up-to-date data to give the City the clearest understanding of the pension fund**

# Initial Discussion

## A few points most everyone can agree on:

- Dallas Employees' Retirement Fund is underfunded with a ~73% funding ratio
- The City of Dallas will have to contribute significant funds to improve the funding status
- The public, city officials, beneficiaries, and all stakeholders want assurance that the plan has optimal performance
- The goal of the review of ERF is an evaluation of the appropriateness, adequacy, and effectiveness of the pension's performance, and the evaluation and recommendations for overall improvements for the pension
- Performance, over time, should, net of fees and investment costs, exceed appropriate benchmarks and the median of the Plan's peers – major cities in Texas and the U.S.

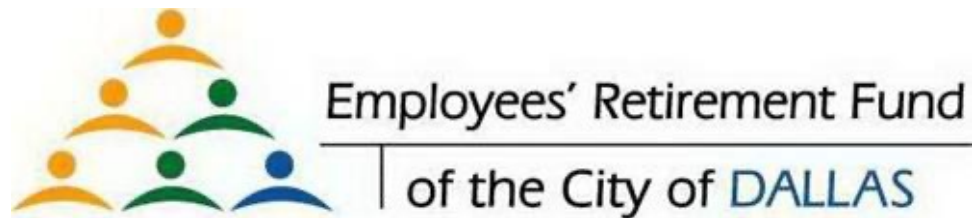
# Initial Observations

- While ERF has slightly underperformed its peers both nationally and in the state of Texas over the 5 and 10-year time periods, it has outperformed both the average national and average Texas plan over the most recent 3-year time period
- Improved risk adjusted returns would help lower contributions and increase funded status
- Risk adjusted asset allocation needs further evaluation with respect to an increase in private markets' allocation
- Target improving asset manager selection
- The time period and required rate of return to achieve full funding are both reasonable

# What Commerce Street has been asked to do

## The City requested a report comprised of the following objectives:

1. Assess the overall structure and asset allocation of the investment portfolio
2. Assess the overall performance and current/historical rate of return of the investment portfolio
3. Identify appropriate state and national benchmarking for asset allocation and investment performance
4. Identify areas of potential risk and propose risk mitigation strategies
5. Evaluate the effectiveness of the current asset allocation strategy
6. Evaluate the effectiveness of the current manager selection and their strategies
7. Review the adherence to investment policies and guidelines
8. Review the current fee structure and trading costs



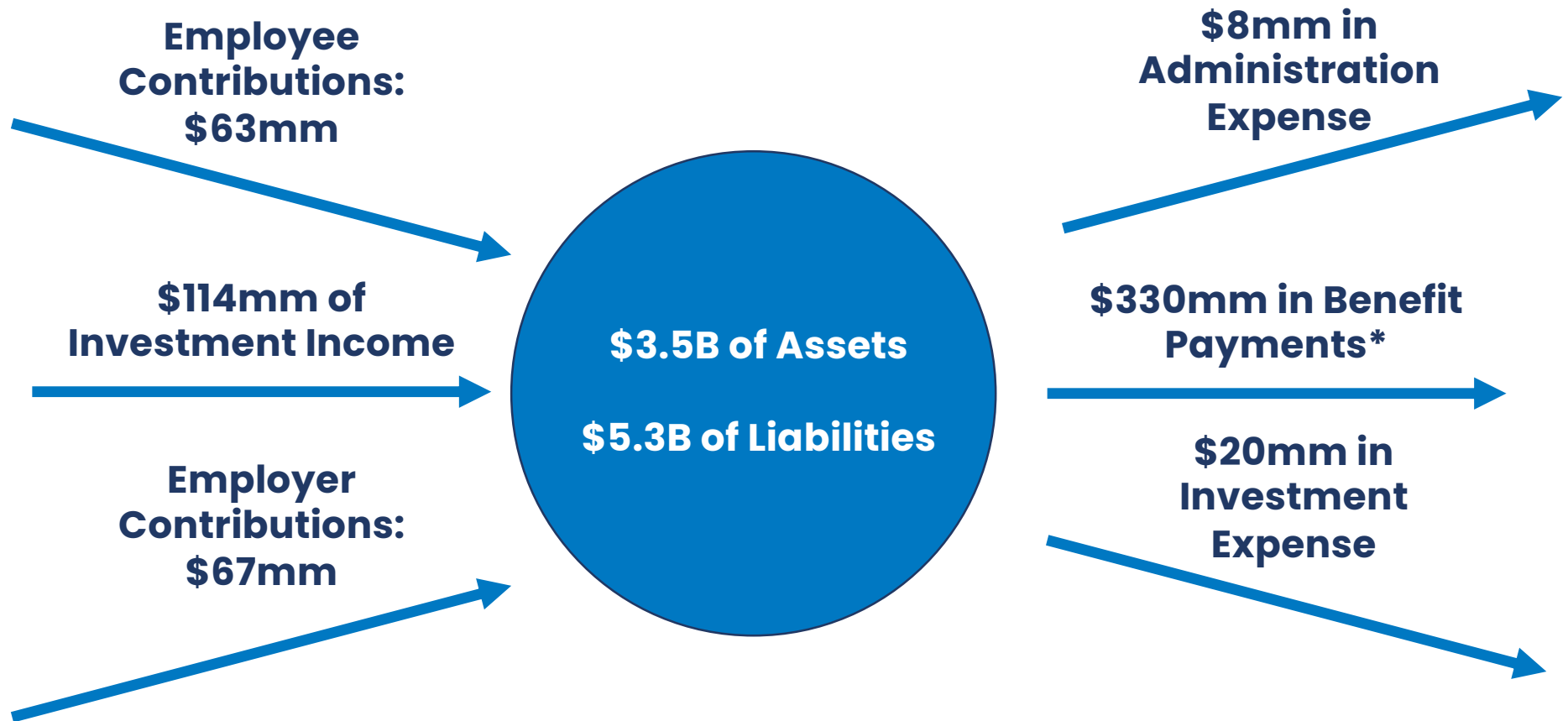
## **Objective 1: Assess the overall structure and asset allocation of the investment portfolio**



# Dallas ERF's current inflows and outflows



## Dallas ERF 2022 Pension Flows



Source: Employees Retirement Fund of the City of Dallas, *Actuarial Valuation Report*, as of December 31, 2022

\*Includes contribution refunds

# ERF has outperformed its overall benchmark, but its public equities have underperformed their benchmark in several time periods



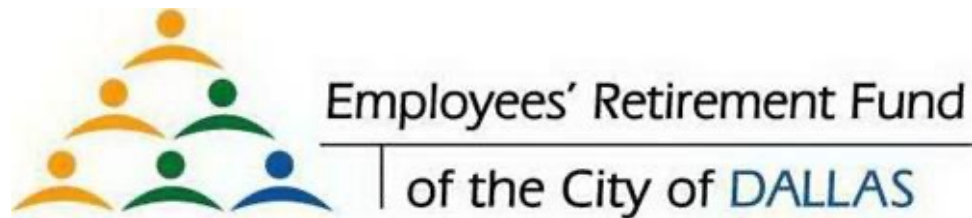
As of 12/31/22	1-Year	3-Year	5-Year	10-Year
<b>Dallas ERF</b>	<b>-8.5%</b>	<b>3.9%</b>	<b>4.6%</b>	<b>6.6%</b>
70 ACWI/30 AGG	-16.7%	2.1%	3.8%	6.0%

As of 12/31/22	1-Year	3-Year	5-Year	10-Year
<b>ERF Public Equities</b>	<b>-14.5%</b>	<b>3.6%</b>	<b>4.5%</b>	<b>8.1%</b>
MSCI ACWI	-18.4%	4.0%	5.2%	8.0%

As of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>Dallas ERF</b>	<b>10.1%</b>	<b>5.4%</b>	<b>7.7%</b>	<b>6.0%</b>
70 ACWI/30 AGG	17.2%	3.2%	8.6%	6.2%

As of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>ERF Public Equities</b>	<b>16.7%</b>	<b>5.4%</b>	<b>10.2%</b>	<b>7.6%</b>
MSCI ACWI	22.2%	5.8%	11.7%	7.9%

Source: Wilshire; ERF of the City of Dallas Executive Summary Q4 2023 and Q4 2022 and Morningstar Direct as of December 31, 2023 and December 31, 2022.

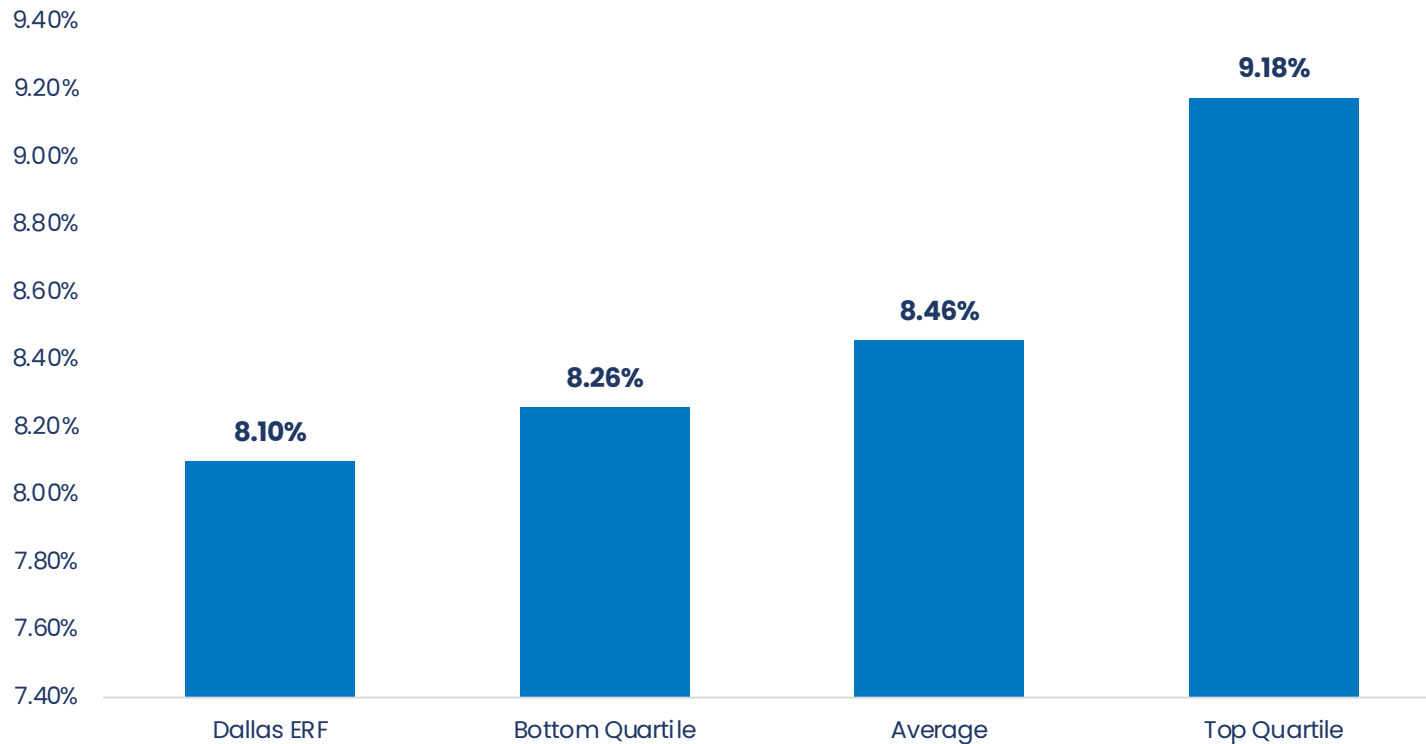


## **Objective 2: Assess the overall performance and current/historical rate of return of the investment portfolio**

# Dallas ERF's public equity returns are slightly below national average



**10-Year Public Equity Returns  
As of 12/31/22**



**This is largely due to manager selection, which will be covered under Objective 6**

Source: <https://publicplansdata.org/public-plans-database/browse-data/>

Only plans with FY ending 12/31/22 were included

# ERF's public equity managers perform well against Wilshire's benchmarks



Global Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>17.0%</b>	<b>5.1%</b>	<b>10.6%</b>	<b>7.1%</b>
MSCI AC World Index	22.2%	5.8%	11.7%	7.9%
Top Quartile	23.7%	7.7%	13.2%	8.9%
Average	19.3%	5.2%	11.4%	7.5%
Bottom Quartile	12.7%	2.3%	9.4%	6.1%

Global Low Volatility Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>9.8%</b>	<b>5.0%</b>	<b>7.1%</b>	<b>-</b>
MSCI AC World Min Vol Index	7.7%	3.3%	6.5%	-
Top Quartile	8.4%	3.7%	6.9%	-
Average	8.3%	3.6%	6.8%	-
Bottom Quartile	8.2%	3.5%	6.5%	-

Domestic Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>23.1%</b>	<b>9.7%</b>	<b>14.7%</b>	<b>10.8%</b>
Custom Benchmark	26.1%	9.0%	15.4%	11.7%
Top Quartile	25.5%	10.2%	15.1%	11.2%
Average	18.5%	8.0%	13.1%	9.2%
Bottom Quartile	13.2%	4.1%	10.9%	7.8%

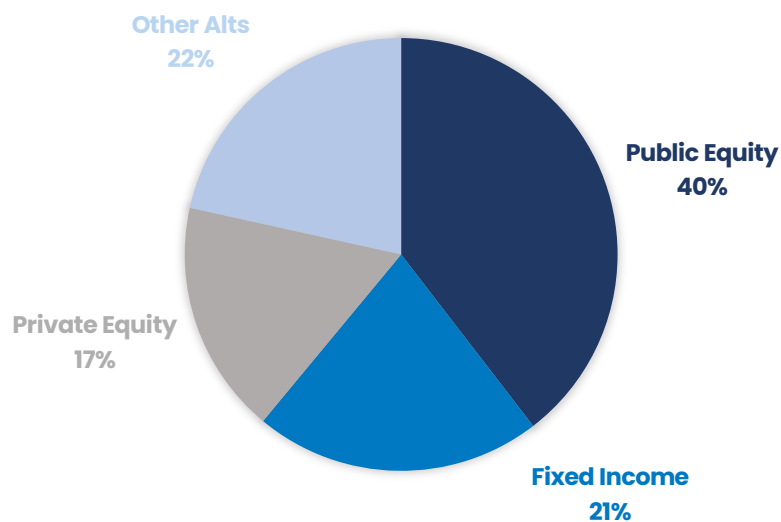
International Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>16.3%</b>	<b>1.8%</b>	<b>8.4%</b>	<b>4.7%</b>
Custom Benchmark	15.6%	1.5%	7.2%	4.0%
Top Quartile	19.6%	5.1%	9.4%	5.4%
Average	16.9%	2.4%	7.9%	4.5%
Bottom Quartile	13.7%	-1.0%	6.5%	3.8%

**Wilshire is a highly regarded consultant in the industry, and has helped set benchmarks for all of ERF's equity managers**

Source: Wilshire's ERF of the City of Dallas, Executive Summary for Q4 2023

# The “lag” on ERF’s portfolio is not just in public equities, but in its asset allocation

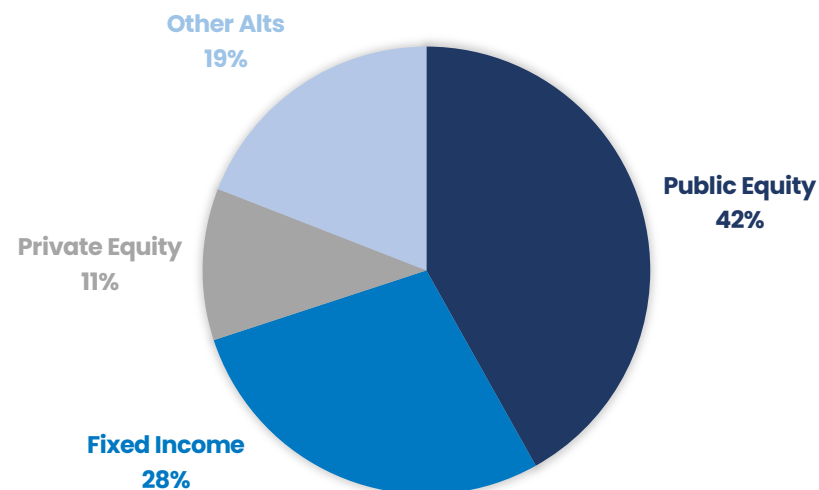
**National Top Quartile Pensions  
Average Allocation (rounded)**



**Returns**

1-Year	3-Year	5-Year	10-Year
-3.6%	8.5%	8.1%	8.6%

**Dallas ERF**



**Returns**

1-Year	3-Year	5-Year	10-Year
-8.5%	3.9%	4.6%	6.6%

**Only slight modifications are needed to improve overall performance**

Source: <https://publicplansdata.org/public-plans-database/browse-data/>, Wilshire; ERF of the City of Dallas Executive Summary Q4 2022

# Utilizing a top quartile allocation with indices could have resulted in top quartile returns



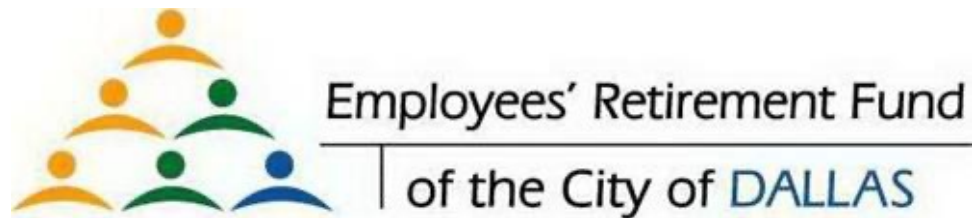
As of 12/31/23	Weighting*	1-Year	3-Year	5-Year	10-Year
Public Equity	39.6%	22.2%	5.8%	11.7%	7.9%
Fixed Income	21.5%	9.6%	-0.6%	3.2%	3.2%
Private Equity	17.4%	9.3%	14.1%	17.9%	15.6%
Other Alts	17.5%	8.2%	8.8%	8.0%	6.7%
Commodities	4.1%	-7.9%	10.8%	7.2%	-1.1%
<b>Top Quartile Allocation</b>	<b>100.0%</b>	<b>13.6%</b>	<b>6.6%</b>	<b>10.1%</b>	<b>7.7%</b>
<b>ERF (70/30)</b>	<b>100.0%</b>	<b>10.1%</b>	<b>5.4%</b>	<b>7.7%</b>	<b>6.0%</b>

**It should be noted that returns in asset categories have to take into account risk and liquidity**

Source: Wilshire, *ERF of the City of Dallas: Executive Summary Q4 2023*

\*Weightings come from previous slide of the averages for top quartile pension funds nationally. Note that returns may differ based upon market fluctuations and allocation drift.

Indices used: Public Equity – MSCI ACWI, Fixed Income – 50% Bloomberg Agg + 50% ICE BofA US High Yield, Private Equity – Cambridge Associates Private Equity Index, Other Alts – Inxx Private Credit TR + S&P Global Infrastructure + Cambridge Associates Real Estate Index (equal-weighted), Commodities – Bloomberg Commodity



## **Objective 3: Identify appropriate state and national benchmarking for asset allocation and performance**



# Benchmarking basics

**“If you can’t measure it, you can’t manage it” – Peter Drucker**

## **We should define a strong peer group**

- If peers are significantly outperforming us, then we should understand why we are underperforming
- Underperformance will show up in asset allocation and manager selection

## **Benchmarking helps the City and the Plan in many ways**

- It provides transparency for performance, management, and governance’s effectiveness
- It can give us new ideas and insight
- Done correctly, it lays the groundwork for outperformance

**If we are below average, we must get to average; if we are average, let us work our way to above average**

# ERF's peer group

**Not all pensions are in similar situations or have similar constraints**

**We consulted with ERF staff to determine what an appropriate peer group for the pension would be. The criteria they recommended:**

- Plans with assets between \$2B-\$6.5B (ERF has assets of ~\$3.6B)
- Plans with funded ratios between 60%-94% (ERF has funded ratio of ~73%)
- Plans located in the same region facing similar political/economic conditions

# Pensions that met this criteria

Data as of 6/30/23	Assets (thousands)	Funded Ratio
Alaska Teachers	\$6,100,204	78%
Fairfax County Uniformed	\$2,081,471	78%
Detroit Police and Fire	\$2,717,705	77%
Louisiana Schools	\$2,177,431	77%
Louisiana Municipal Police	\$2,739,116	76%
Fairfax County (VA) ERS	\$5,103,374	76%
Fairfax County Schools	\$3,058,883	74%
Dallas ERF	\$3,511,284	73%
Oklahoma Fire	\$3,221,798	73%
Baltimore Fire and Police	\$3,105,850	73%
Connecticut Municipal	\$3,391,151	73%
Montana Teachers	\$4,971,900	72%
Phoenix ERS	\$3,517,451	72%
North Dakota Teachers	\$3,259,558	71%
Vermont State Employees	\$2,523,349	70%
Houston Municipal	\$3,836,122	69%
Missouri DOT and Highway	\$3,247,983	69%
North Dakota PERS	\$3,899,549	67%
South Carolina Police	\$6,400,701	66%

Source: <https://publicplansdata.org/public-plans-database/browse-data/>

# ERF is competitive in this peer group

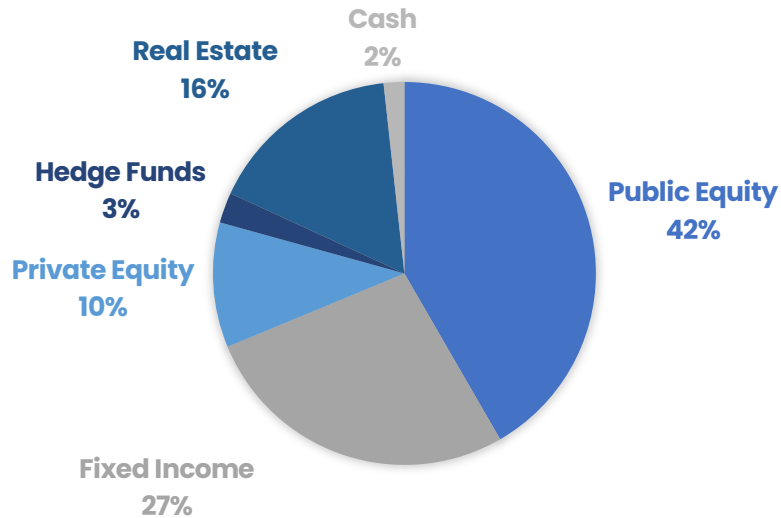


Data as of 6/30/23	Assets (Thousands)	Funded Ratio	3 Year Return	5 Year Return	10 Year Return
Oklahoma Fire	\$3,221,798	73%	-	7.7%	9.5%
Houston Municipal	\$3,836,122	69%	15.7%	10.5%	9.5%
Missouri DOT and Highway	\$3,247,983	69%	14.0%	9.5%	9.3%
Detroit Police and Fire	\$2,717,705	77%	11.5%	8.2%	8.8%
Alaska Teachers	\$6,100,204	78%	9.4%	7.7%	8.2%
Montana Teachers	\$4,971,900	72%	9.8%	7.6%	8.2%
Louisiana Schools	\$2,177,431	77%	11.0%	7.4%	7.7%
North Dakota Teachers	\$3,259,558	71%	8.4%	6.8%	7.6%
North Dakota PERS	\$3,899,549	67%	8.6%	6.9%	7.6%
South Carolina Police	\$6,400,701	66%	10.8%	7.2%	7.1%
Baltimore Fire and Police	\$3,105,850	73%	8.5%	6.2%	6.8%
Connecticut Municipal	\$3,391,151	73%	7.5%	6.1%	6.7%
<b>Dallas ERF</b>	<b>\$3,605,596</b>	<b>73%</b>	<b>8.3%</b>	<b>5.6%</b>	<b>6.6%</b>
Fairfax County Schools	\$3,058,883	74%	6.9%	6.0%	6.6%
Phoenix ERS	\$3,517,451	72%	7.2%	5.8%	6.5%
Vermont State Employees	\$2,523,349	70%	7.5%	6.4%	6.5%
Louisiana Municipal Police	\$2,739,116	76%	6.9%	5.4%	6.4%
Fairfax County Uniformed	\$2,081,471	78%	7.2%	4.9%	5.9%
Fairfax County (VA) ERS	\$5,103,374	76%	6.0%	5.5%	5.6%

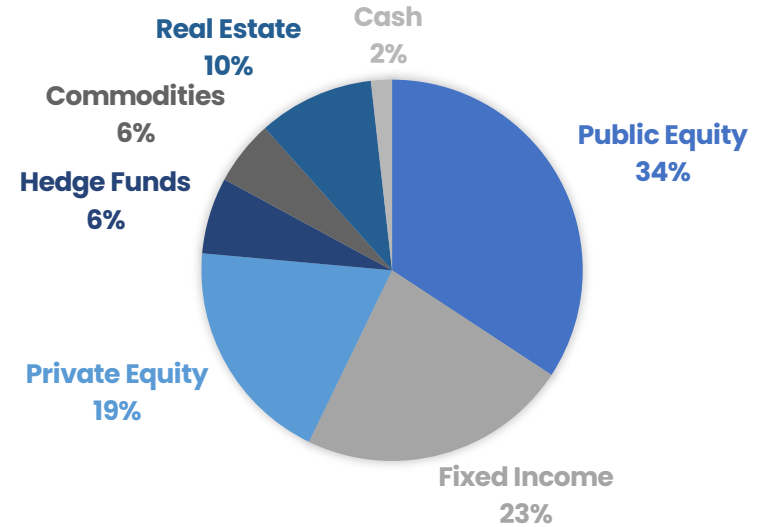
Source: <https://publicplansdata.org/public-plans-database/browse-data/>

# ERF's allocation is in line with the average of this peer group

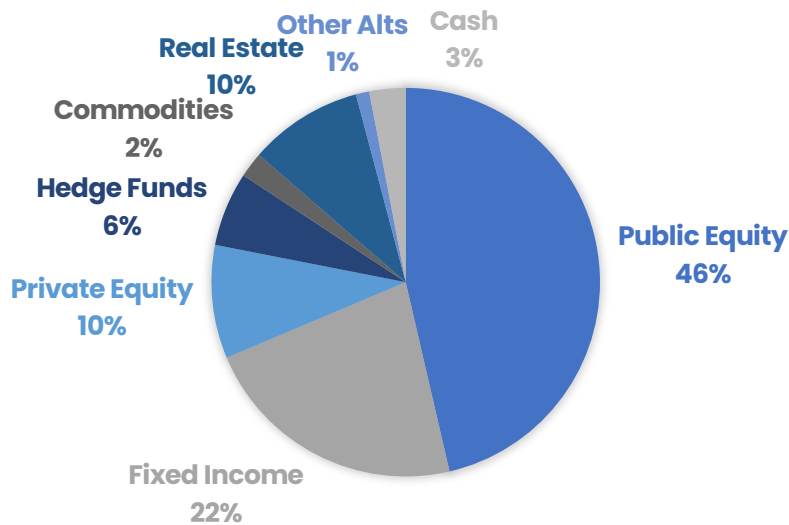
### Dallas ERF



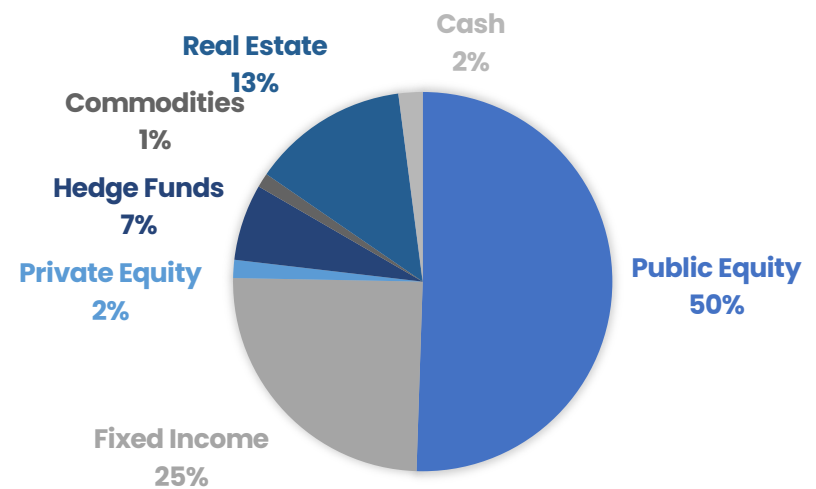
### Top Quartile



### Average



### Bottom Quartile



Source: <https://publicplansdata.org/public-plans-database/browse-data/>

Data as of 6/30/23

# ERF vs. largest Texas cities



Data as of 6/30/23	1-Year	3-Year	5-Year	10-Year
<b>Dallas ERF</b>	<b>7.2%</b>	<b>8.3%</b>	<b>5.7%</b>	<b>6.6%</b>
Houston MEPS*	6.2%	15.7%	10.5%	9.5%

Data as of 12/31/23	1-Year	3-Year	5-Year	10-Year
<b>Dallas ERF</b>	<b>10.1%</b>	<b>5.4%</b>	<b>7.7%</b>	<b>6.0%</b>
Texas County & District RS	11.1%	8.5%	10.5%	7.8%
Fort Worth ERF	8.9%	5.2%	10.5%	6.2%
Austin ERS	12.3%	2.3%	3.7%	5.7%

Source: Texas Pension Review Board. <https://data.prb.texas.gov/plans/index.html> and Wilshire, *Dallas Employees' Retirement Fund: Quarterly Investment Summary Q2 2023 and Q4 2023*

\*City of Dallas staff requested direct comparison to HMEPS. HMEPS may not be the most representative comparison, but it is the retirement fund of the most comparable city to Dallas in the state of Texas.

# ERF vs. national and Texas averages

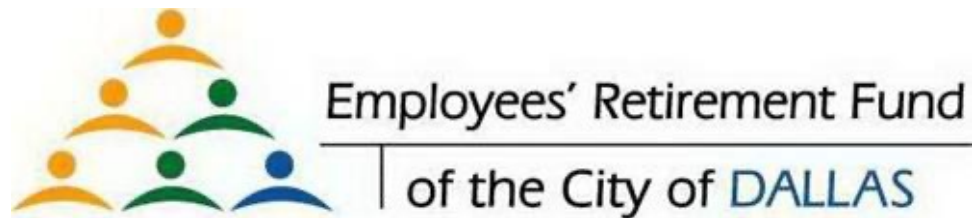


Data as of 12/31/23	3-Year	5-Year	10-Year
<b>Dallas ERF</b>	<b>5.4%</b>	<b>7.7%</b>	<b>6.0%</b>
National Top Quartile	5.6%	8.9%	6.8%
National Average	4.5%	8.2%	6.2%
National Bottom Quartile	3.7%	7.7%	5.7%
Texas Top Quartile*	5.3%	9.0%	6.6%
Texas Average*	5.1%	8.6%	6.5%
Texas Bottom Quartile*	4.3%	7.9%	6.2%

Source: <https://publicplansdata.org/public-plans-database/browse-data/> and <https://data.prb.texas.gov/plans/index.html>

National quartile rankings provided by Wilshire

\*Quartile rankings only taken from Texas Plans with fiscal years ending 12/31/23



## **Objective 4: Identify areas of potential risk and propose risk mitigation strategies**



# Some pension risks to consider

Liabilities – Current and Future

Governance Risk

Asset Allocation Risk

Manager Selection Risk

Monitoring Risk

# The City of Dallas needs to increase its knowledge of ERF

There are many parties affected by the running of the pension: the employees of the City, the staff of ERF, and the taxpayers of Dallas

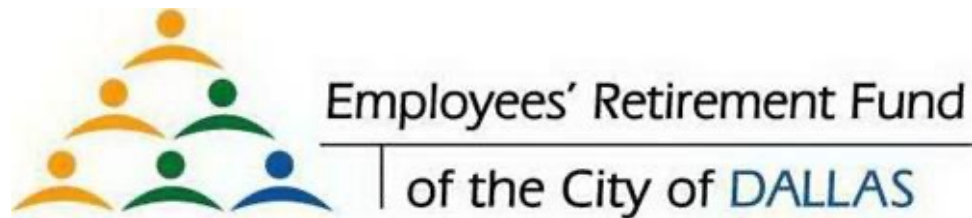
**To best ensure the health of all stakeholders, the City of Dallas should take it upon itself to become more knowledgeable of the Plan**

**The City needs to increase its knowledge on these elements of the Plan:**

- Asset allocation, risk, and liquidity
- Policies and procedures
- Reporting and benchmarking

**This can be enabled by the City hiring:**

- Internal staff or dedicated outside experts that work with the City and the Pension with ongoing communication and two-way feedback



## **Objective 5: Evaluate the effectiveness of the current asset allocation strategy**

# The biggest help to improving ERF's performance might be an increased allocation to private markets



As of 6/30/23	Investment Weights		Returns (5 Year)	
	ERF	TX Peer Group	ERF	TX Peer Group
Public Equity	41.7%	43.3%	6.7%	7.5%
Private Equity	10.6%	21.3%	14.9%	17.5%
Fixed Income	28.8%	18.1%	2.1%	2.6%
Other Alts	19.0%	21.5%	6.3%	6.9%

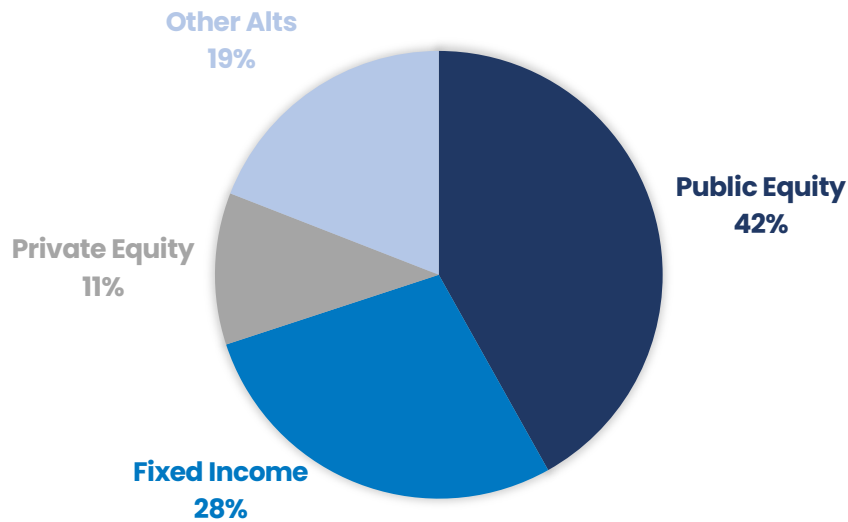
Peer Group consist of similar-size funds in Texas: Houston Firefighters Relief and Retirement Fund, Houston Police Officers' Pension System, Houston Municipal Employees' Pension System, Austin Police Retirement System, Austin Firefighters Retirement Fund, Fort Worth Employees' Retirement Fund, Texas County and District Retirement System

# Allocation differences between the employee pension funds of Texas' two largest cities

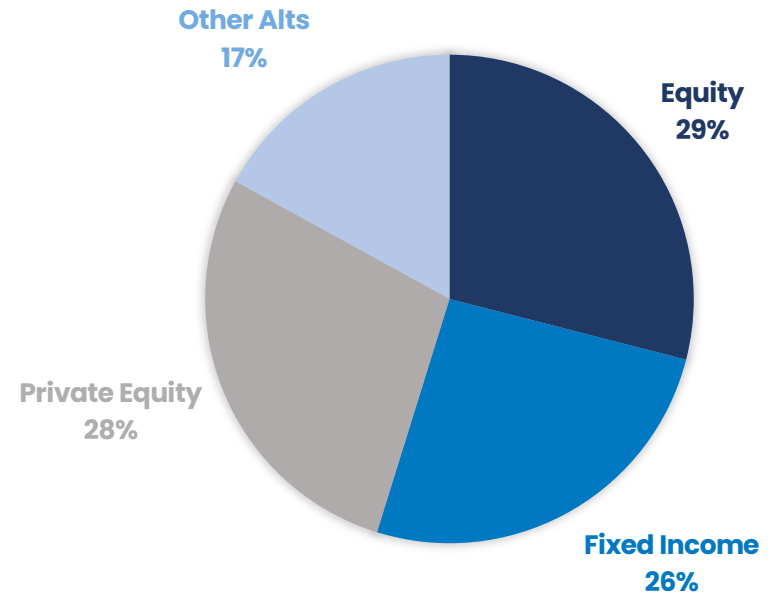


Total equity exposure comparable, but ERF has much less private equity

**Dallas ERF**



**Houston MEPS**



**Total Returns**

1-Year	3-Year	5-Year	10-Year
7.2%	8.3%	5.6%	6.6%

**Total Returns**

1-Year	3-Year	5-Year	10-Year
6.2%	15.7%	10.5%	9.5%

Data as of 6/30/23

# Moving allocation from public equity to private equity could have increased returns over longer time periods

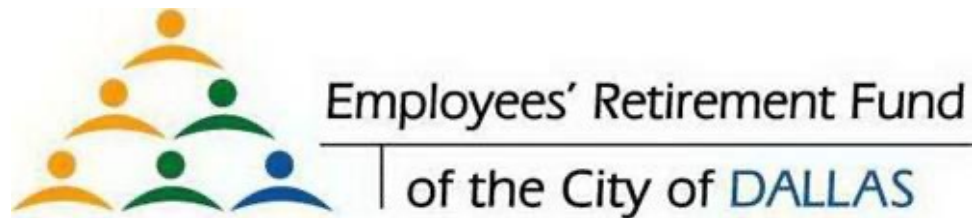
As of 12/31/23	1-Year	3-Year	5-Year	10-Year
ERF Public Equities	16.7%	5.4%	10.2%	7.6%
ERF Private Equity	1.9%	17.4%	13.2%	12.9%

As of 12/31/23		1-Year	3-Year	5-Year	10-Year
ERF Total Equity	Public 42% PE 10%	13.8%	7.7%	10.8%	8.6%
Pro Forma ERF	Public 32% PE 20%	11.0%	10.1%	11.4%	9.7%

**ERF's private equity returns are slightly below average to peers and comparable PE funds, but still high enough where further allocation would have improved returns**

**It should be noted that returns in asset categories have to take into account risk and liquidity**

Source: Wilshire's ERF of the City of Dallas, Executive Summary for Q4 2023



## **Objective 6: Evaluate the effectiveness of the current manager selection and their strategies**

# Manager selection is an important contributor to fund performance



As of 6/30/23	Returns (5 Year)	
	ERF	TX Peer Group
Public Equity	6.7%	7.5%
Private Equity	14.9%	17.5%
Fixed Income	2.1%	2.6%
Other Alts	6.3%	6.9%

Peer Group consist of similar-size funds in Texas: Houston Firefighters Relief and Retirement Fund, Houston Police Officers' Pension System, Houston Municipal Employees' Pension System, Austin Police Retirement System, Austin Firefighters Retirement Fund, Fort Worth Employees' Retirement Fund, Texas County and District Retirement System



# ERF's public equity managers are competitive when compared to Wilshire's peer rankings



Global Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>17.0%</b>	<b>5.1%</b>	<b>10.6%</b>	<b>7.1%</b>
MSCI AC World Index	22.2%	5.8%	11.7%	7.9%
Top Quartile	23.7%	7.7%	13.2%	8.9%
Average	19.3%	5.2%	11.4%	7.5%
Bottom Quartile	12.7%	2.3%	9.4%	6.1%

Global Low Volatility Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>9.8%</b>	<b>5.0%</b>	<b>7.1%</b>	<b>-</b>
MSCI AC World Min Vol Index	7.7%	3.3%	6.5%	-
Top Quartile	8.4%	3.7%	6.9%	-
Average	8.3%	3.6%	6.8%	-
Bottom Quartile	8.2%	3.5%	6.5%	-

Domestic Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>23.1%</b>	<b>9.7%</b>	<b>14.7%</b>	<b>10.8%</b>
Custom Benchmark	26.1%	9.0%	15.4%	11.7%
Top Quartile	25.5%	10.2%	15.1%	11.2%
Average	18.5%	8.0%	13.1%	9.2%
Bottom Quartile	13.2%	4.1%	10.9%	7.8%

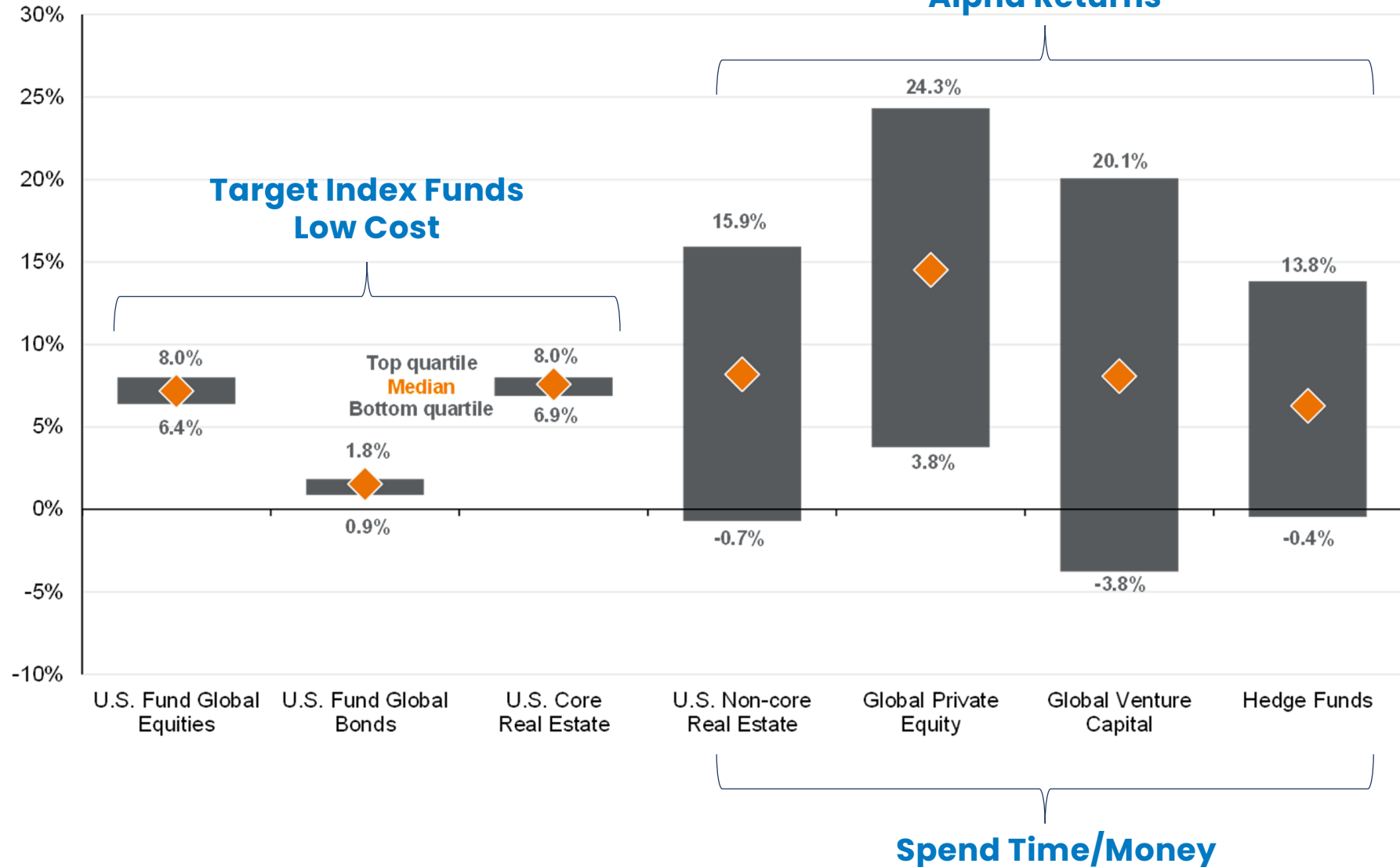
International Equity	1 Year	3 Year	5 Year	10 Year
<b>Dallas ERF</b>	<b>16.3%</b>	<b>1.8%</b>	<b>8.4%</b>	<b>4.7%</b>
Custom Benchmark	15.6%	1.5%	7.2%	4.0%
Top Quartile	19.6%	5.1%	9.4%	5.4%
Average	16.9%	2.4%	7.9%	4.5%
Bottom Quartile	13.7%	-1.0%	6.5%	3.8%

Source: Wilshire's ERF of the City of Dallas, Executive Summary for Q4 2023

# Where to spend time in manager selection

## Public and private manager dispersion

Based on returns over a 10-year window\*



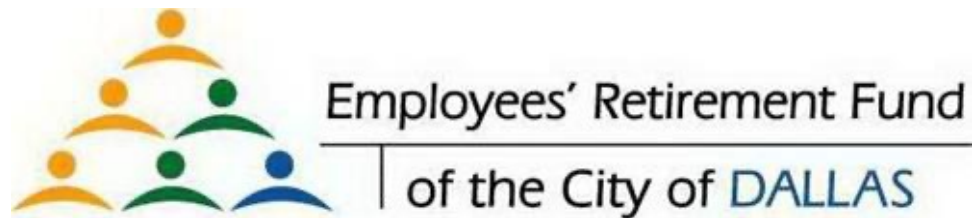
# ERF's private equity fund returns are slightly below average

Fund Name	Vintage Year	Net Multiple	Net IRR
Hamilton Lane Secondary Fund II	2009	1.4x	13.4%
Hamilton Lane Secondary Fund III	2012	1.3x	9.5%
Hamilton Lane Secondary Fund IV	2017	1.6x	17.2%
Hamilton Lane Secondary Fund V	2020	1.5x	19.3%
Hamilton Lane Secondary Fund VI-A	2023*	1.6x	91.3%
Hamilton Lane Fund VII Composite	2010	1.5x	6.0%
Hamilton Lane Fund VIII (Global)	2012	1.5x	7.0%
GCM Grosvenor - Partnership, LP	2011	1.7x	14.2%
GCM Grosvenor - Partnership II, LP (2014)	2014	1.6x	15.6%
GCM Grosvenor - Partnership II, LP (2015)	2015	1.6x	10.0%
GCM Grosvenor - Partnership II, LP (2017)	2018	1.4x	14.4%
GCM Grosvenor Advance Fund	2021*	1.1x	11.1%
GCM Grosvenor - Partnership II, LP (2022)	2022*	1.0x	-12.9%
Fairview Capital - Lone Star Fund I	2015	2.0x	14.1%
Fairview Capital - Lone Star Fund II	2018	1.5x	14.0%
Fairview Capital - Lone Star Fund III - A	2021*	1.0x	-1.6%
Fairview Capital - Lone Star Fund III - B	2022*	1.0x	-52.6%
Fairview Capital - Private Markets Fund VI	2022*	0.9x	-12.1%
<b>Total (5 Yr)</b>		<b>1.6x</b>	<b>13.20%</b>
<b>Preqin Average IRR For Comparable PE Funds</b>		<b>1.9x</b>	<b>17.12%</b>

Source: Wilshire's ERF of the City of Dallas, Executive Summary for Q4 2023

Quartile rankings from Preqin

\*These funds are young and still experiencing the J-curve effect

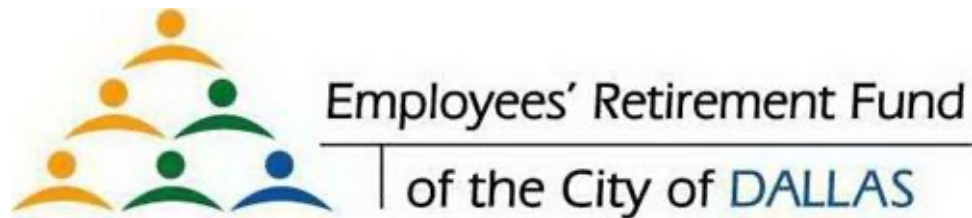


## **Objective 7: Review the adherence to investment policies and guidelines**

# The ERF Investment Policy Statement observations

**Based on our initial review of the IPS, it reflects best practices, and we would suggest a couple minor improvements:**

- Consider adding a section in the General Investment Policy that addresses the specific duties and responsibilities of The Board, Staff, Consultants, Investment Managers, and Custodian. It is best practice to provide the roles of Staff and their interaction with the Board and Consultant in the day-to-day management of the investments.
- Consider including the Manager Selection and Monitoring Policy (“MS&MP”) as an appendix in the General Investment Policy.



## **Objective 8: Review the current fee structure and trading costs**

# ERF's expenses are below average when compared to its peers



System	Fiscal Year End	Net Total Assets	SB 322 Total Direct & Indirect Expenses	SB 322 Total Investment Expense	Annual Audit Investment Expense
Dallas Police & Fire Pension System–Combined Plan	12/31/2022	\$1,824	0.64%	0.80%	0.48%
Houston Police Officers' Pension System	6/30/2023	\$7,208	2.20%	2.21%	0.11%
San Antonio Fire & Police Pension Fund	12/31/2022	\$3,586	1.19%	1.22%	0.41%
Houston Municipal Employees Pension System	6/30/2023	\$4,072	1.08%	1.16%	0.24%
Houston Firefighters' Relief & Retirement Fund	6/30/2023	\$5,109	0.98%	1.16%	0.18%
Fort Worth Employees' Retirement Fund	9/30/2023	\$2,605	1.03%	1.11%	0.15%
Austin Police Retirement System	12/31/2022	\$933	0.83%	0.88%	0.21%
Dallas Employees' Retirement Fund	12/31/2022	\$3,516	0.54%	0.56%	0.55%
Austin Employees' Retirement System	12/31/2023	\$3,279	0.22%	0.26%	0.16%
<b>Average</b>			<b>0.97%</b>	<b>1.04%</b>	<b>0.28%</b>

Source: <https://www.prb.texas.gov/wp-content/uploads/2024/07/2024.07.25-Board-Meeting-Packet.pdf>

# Considerations for the City of Dallas



**We recommend that the City of Dallas hire a qualified firm to help the City's understanding of the independently managed pension, who:**

1. Helps the City's understanding of factors contributing to the performance of other top performing peers
2. Works with city constituents to improve the City's understanding of the pensions
3. Conducts an ongoing analysis to help the City be better informed on any issues related to performance
4. As needed, prepares ongoing reports and clarifications for the City of Dallas
5. Is able to provide, as needed, recommendations for consideration to achieve best practices and improve performance

**An improvement in long-term performance would increase the funding ratio and lessen the burden on the City and taxpayers**



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August 21, 2024

TO: Jack Ireland, Chief Financial Officer, City of Dallas

FROM: Cheryl Alston, Executive Director, Dallas ERF

RE: **Employees' Retirement Fund of the City of Dallas Response to Commerce Street Report**

After our review of the Commerce Street report, we have three comments. They are the following:

1. **A good asset allocation policy balances return, risk and liquidity and not just return. The Commerce Street report only focuses on returns.**
  - Private equity does provide a higher return, but it also comes with higher risk and lower liquidity.
  - Dallas ERF does not simply copy another pension plan's asset allocation. Dallas ERF conducts asset liability modeling, cash flow analysis and a detailed review of asset class assumptions to model several asset allocation scenarios before a decision is made.
2. **Our governance model consists of finance and investment experts.**
  - The Dallas ERF board consists of seven trustees with over one hundred years of finance and investment experience.
  - The Dallas ERF Board hired an investment consulting firm, Wilshire Associates, with access to sophisticated analytics, extensive access to market intelligence and an innovative portfolio construction process.
  - Dallas ERF does not believe that an additional consultant is necessary. However, if the City of Dallas does proceed then the hiring should be in collaboration with the Fund board to confirm that the firm is qualified.
3. **Dallas ERF trustees are fiduciaries. Wilshire Associates is a fiduciary.**
  - Why is that important? Fiduciaries are persons or organizations that act on behalf of others and are required to put the clients' interests ahead of their own, with a duty to preserve good faith and trust.
  - Dallas ERF requires organizations providing advice to the board to agree to be a fiduciary.
  - Any organization that is hired by the City of Dallas to provide investment advice should also be a fiduciary. In addition to fiduciary responsibilities, the consultant must be recused from seeking investments or business opportunities from the Fund according to the Ethics policy.

Everything in life comes with trade-offs. Investing is no different. With each and every investment that we make there is a trade-off between risk, return and liquidity. The higher the return, the higher the risk and often lower the liquidity. As the asset allocation decision drives more than 90% of a portfolio's return, it

serves as a critical process that can assist fiduciaries in managing the key risks facing institutional investors.



- **What is Return?** The geometric or compound return differs from the arithmetic return in how it is calculated. The former takes into account the compounding that occurs from period to period, whereas the latter does not. Because of this, investors usually consider the geometric or compound mean to be the more accurate measure of returns.
- **What is Risk?** Ask a lay person what risk is, and they will probably say something along the lines of, “the possibility of loss or harm.” In the world of investing, there are a variety of ways to assess risk, but the industry standard method is to look at volatility – or the tendency of an investment’s value to fluctuate in price. From a statistical perspective, we measure this using what is called standard deviation.
- **What is Liquidity?** Liquidity is how easily or quickly a security or investment can be bought or sold in the secondary market.

The table below shows the projected return, risk, and liquidity over a 10-year period.

- Core Bonds have a return of 4.75% with lower risk (4.7) and a high cash yield (5.1%).
- US Stocks has a return of 5.00% with medium risk (17.0) and a cash yield of (1.45%)
- Private Equity has a return of 7.25% with higher risk (30.00) with a cash yield of (0.00%)
- We believe private equity has a role in the portfolio, but the amount of private equity is different for each pension plan.
- Asset class assumptions are not static. The assumptions evolve with the macro-economic environment.

### Wilshire December 2023 Correlation Matrix

	Equity					Fixed Income							Real Estate					
	U.S. Stock	Dev. ex-U.S. Stock	Emg. Mrkt. Stock	Global ex-U.S. Stock	Global Stock	U.S. Buyouts	Cash	Core Bond	LT Core Bond	U.S. TIPS	High Yield	Direct Lending	Non-U.S. Bond	U.S. Real Estate Secs.	Global RI Estate Secs.	Core Prvt Real Estate	U.S. CPI	
Expected Compound Return (%)	5.00	6.00	6.25	6.35	5.60	7.25	3.80	4.75	4.70	4.15	5.90	8.35	2.85	5.60	5.75	5.35	6.05	2.25
Expected Arithmetic Return (%)	6.35	7.50	9.20	8.00	6.95	11.10	3.80	4.85	5.15	4.30	6.35	8.80	2.95	7.00	7.00	6.00	7.20	2.25
Expected Risk (%)	17.00	18.00	26.00	19.00	17.05	30.00	0.75	4.70	9.85	6.00	10.00	10.00	4.00	17.50	16.45	12.00	16.00	1.75
Cash Yield (%)	1.45	3.10	2.50	2.95	2.00	0.00	3.80	5.10	5.25	4.35	9.20	9.95	3.65	3.90	3.90	3.25	3.80	0.00