AC Transit Retirement System

To: AC Transit Board of Directors May 12, 2022

From: Jeffrey Lewis - Chair, AC Transit Retirement Board

Re: 2022 Semi-Annual Retirement Board Report (#1)

Jeffrey Lewis

The first Semi-Annual Report of the year will focus on the following:

1) The Plan's investment results in 2021 and the first three months of 2022
2) Diversity and ESG (Environmental, Social & Governance)
3) The Plan's long-term investment results and asset allocation
4) The upcoming Actuarial Valuation
5) PEPRA Implementation
6) How the Retirement Department is handling COVID-19
7) Staffing within the Retirement Department

2021 and Early 2022 Investment Results

In 2021 the Plan benefited from the strong returns of worldwide equity markets, while bond returns provided negative returns as a result of an increase in interest rates. The Plan's diversified portfolio of investments returned roughly 9.2% which exceeded its actuarial assumed rate of return of 6.75%.

The Plan had $911 million in assets on 12/31/21, which was an increase of $71 million from the $840 million in assets on 12/31/20. In 2021, the broad U.S. stock market (Russell 3000) increased by 25.7%, small cap stocks (Russell 2000) returned 14.8%, non-U.S. developed market equities returned 11.2%, and emerging market equities returned a negative 2.5%. The domestic U.S. bond market (Barclays Aggregate) returned a negative 1.5%.

Through May 12th, worldwide equity markets have reversed course from the last few years and are down by roughly 15.0% for the year. Bond returns are down close to 10.0% for the year. Unless markets improve in the upcoming months, the Plan will have a negative return in 2022. Of course, we still have more than half the year for markets to recover.

In the past 10 years, U.S. equity markets have only had one year with a negative return. While we hope the next 10 years bring similar investment returns to the past 10 years, we cannot count on this to occur. As you are aware, the Plan's assets are invested in a diversified portfolio, including U.S. stocks, bonds, other fixed income investments, international stocks, emerging markets, real estate, and other types of investments. As has been mentioned numerous times in these reports, the investment results of the Plan are highly dependent on the performance of the equity markets.

Diversity and ESG

The Board continued discussing diversity and inclusion at the firms that serve as our investment managers and in the asset management industry. The Board spent considerable time in 2021 discussing this issue with a handful of the Plan's investment managers. In February of this year, the Board instructed staff to send a letter to all of our investment managers requesting a breakdown of the demographics of their professional employees. The letter informed our managers that we would be requesting this information on an annual basis.

The Board continues to discuss the issue of ESG (Environmental, Social, Governance) factors in investments, and plans on addressing this issue in depth in the upcoming months.

Longer-Term Investment Results as of 12/31/21 and Asset Allocation

Since its inception in 1992, the Plan has achieved an average annual return of 8.0%. Over the last 10 years, the Plan has returned an average of 8.7% annually. Over the last 5 years, the Plan's return averaged 9.5% annually, while for the last 3 years, the Plan's average return was 13.0%. As a reminder to the AC Transit Board, the current actuarially assumed rate of return for the Plan was reduced last year from 7.0% to 6.75%.

The Board invests for the long term and expects equity markets over the long term to produce returns in excess of our actuarially assumed rate. On the other hand, we expect the fixed-income portion of the portfolio to produce returns below our assumed rate (6.75%), but to provide diversification (given the historical lack of correlation between equity and fixed income investments). The Board's relatively smaller allocations to other categories of investments provides further diversification. The Board consistently reviews our asset allocation with NEPC, our investment consultant, and, when appropriate, adjusts our allocation to various asset classes.

In 2021 the Board decided to increase our Private Debt allocation to closer to the 5.0% target. The Board hired one of our current private debt managers, Monroe, to run an additional allocation of roughly $18 million. The Board continues to evaluate our investment portfolio and make changes when warranted; in 2022, the Board has hired two new Real Estate managers to each manage $8 million.

Upcoming Actuarial Valuation

On an annual basis, our actuary (Cheiron) produces an Actuarial Valuation. We have provided our actuary with the data they need to begin the 2022 valuation. As in past years, we will inform the District of the preliminary figures we receive from our actuary. As it does every year, the Retirement Board will take a close look at all the major assumptions embedded in the Actuarial Valuation. Of course, the District will have many opportunities to provide input in this process. At the March 17th Retirement Board meeting, we had a preliminary discussion of the assumptions that go into the assumed rate of return. The General Manager attended this meeting, and, as in prior years, he will be given opportunities to convey his views to the Retirement Board and our actuary.

PEPRA Amendment Implementation

Staff is continuing to implement the PEPRA Amendment for represented and unrepresented employees. As has been mentioned in the past, implementing the structure to track employee contributions will require the involvement of both the Retirement Department and the District. We are working closely with the District Payroll/Finance/HR area to implement and track employee contributions.

COVID-19 and the Retirement Department

The Department has been working from home for over a year now, with only occasional visits by a few employees to the office. During this time, the Department has managed to process retirements and "meet" with retirees via Zoom and Teams and through cell phone calls. Department productivity has been reduced as a result of working from home. Certain tasks take longer when the Department is not together in the office.

Staffing Within the Retirement Department

The Retirement Board has begun planning for the eventuality of Hugo Wildmann retiring and has been working with the District on a hiring plan. In addition, as a result of the PEPRA employee contribution requirement, workload within the Department will go up significantly in the upcoming years. The Retirement Board is discussing the required staffing level for the Department going forward.

Please feel free to call me, Jeffrey Lewis (510-463-3900), or Hugo Wildmann (510-891-4889) if you would like to discuss this report or request additional information.