



AC Transit
Employees' Retirement System

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To: AC Transit Board of Directors April 2019
From: Jeffrey Lewis - Chair, AC Transit Retirement Board
Re: 2019 Semi-Annual Retirement Board Report (#1)

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

- 1) The Plan's investment results in 2018 and the first quarter of 2019.
- 2) The Plan's long-term investment results and asset allocation.
- 3) The upcoming Actuarial Valuation.
- 4) PEPRA Implementation.
- 5) Staffing.

2018 and Early 2019 Investment Results

The Plan returned a negative 5.2% in 2018. As we are all aware, both U.S. and foreign stock markets declined in 2018. Further details regarding this performance are given below. As has been written in these reports often, market declines are not a cause for alarm or worry; rather, they are something that experienced investors know will occur from time to time. We all wish equity markets did not have "down" years; however, years with negative returns are to be expected. It should be noted that prior to 2018, equity markets have not had a "down" year since the large market sell-off in 2008. U.S. equity markets have declined in 25 of the past 90 years. Given this historical record, one should expect a down year a bit more often than once every four years.

In calendar year 2019, through the end of March, the Plan has returned 7.8%. This return has made up for the losses incurred in 2018. In U.S. equity markets, the returns in the first quarter of 2019 have more than made up for the losses in 2018, while in international markets, the rally in 2019 has not made up for the losses in 2018. In the first three months of 2019, U.S. equity markets were up by 13% and foreign equity markets were also up. We do not know how the equity markets will perform in the future. The Retirement Board will continue to take a long-term view in managing its investment portfolio and will continue to view down markets as one of the necessary evils of investing in equity markets. To be overly focused or concerned over short-term market declines can lead to investment decisions that are not in the best interests of the Plan, its participants (the retirees and active workers), and the District.

The Plan had \$641 million in assets on 12/31/18, which is a decrease of \$38 million from the \$679 million in assets on 12/31/17. The broad U.S. stock market (Russell 3000) decreased by 5.2%, small cap stocks (Russell 2000) returned a negative 11.0%, non-U.S. developed market equities declined 13.8%, and emerging market equities declined

The AC Transit Employees' Retirement System is dedicated to providing a secure and predictable source of retirement income for eligible employees, retirees and beneficiaries

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14.6%. The domestic U.S. bond market (Barclays Aggregate) was unchanged for the year. As you know, 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 will be highly dependent on the performance of the equity markets.

The investment return of negative 5.2% was well below the Plan's actuarially assumed rate of 7.125%. Since the Plan's return in 2018 was below the assumed rate of return, the District's contribution as a percentage of payroll will increase (all other things being equal) in upcoming years. We have been working with the District to provide early estimates of the impact of the 2018 investment results on the District's contribution.

Longer-Term Investment Results and Asset Allocation

Since its inception in 1992, the Plan has achieved an average annual return of 7.5%. Over the last 10 years, the Plan has returned an average of 8.7% annually. (The 10-year figures no longer include the 2008 market meltdown.) Over the last 5 years, the Plan's return averaged 4.2% a year. (This figure is impacted by the negative returns of last year.)

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 (7.125%). The Board consistently reviews our asset allocation with NEPC, our investment consultant, and, when appropriate, adjusts our allocation to various asset classes.

In 2018, we hired two new managers, a real estate manager and a private debt manager, to manage relatively small parts of our portfolio. This is part of the Board's continued work to diversify the investment portfolio and reduce our reliance on equities.

Upcoming Actuarial Valuation

On an annual basis, our actuary (Cheiron) produces an Actuarial Valuation. Every four years they conduct an Experience Study. The Experience Study looks in detail at the last four years of data pertaining to factors such as retirements, ages at death, and salary increases. An Experience Study is being conducted this year. We should have preliminary results of the Valuation and Experience Study by June and will share these with the District when we receive them. At the April Retirement Board meeting we held our initial discussions pertaining to the 2019 Actuarial Valuation. The 2019 Valuation will be the first Valuation that incorporates employee contributions. This is a result of the PEPPRA Plan Amendment. As it does every year, the Retirement Board will take a close look at all the major assumptions embedded in the Actuarial Valuation. As always, the District will be involved in these discussions.

Our actuary will have very preliminary figures available at the Joint Meeting and will be prepared to answer all questions pertaining to the funded ratio of the Plan, the District's contribution going forward and the impact that the negative return last year will have on the funded ratio and contribution going forward.

PEPRA Amendment Implementation

Staff is working on implementing the PEPRA amendment. As has been mentioned in the past, implementing the structure to track employee contributions will take the involvement of both the Retirement Department and District. We are working closely with the District Payroll/Finance area to implement and track the employee contribution.

Staffing

The Retirement Board would like to thank the District Board again for upgrading the Retirement System Administrator position to a Grade 9. We are all hoping that the current recruitment will end with the hiring of an employee for this position.

The special Joint Committee of our two Boards recently met and had an extremely productive meeting. The members of the committee all agreed that the most effective way to deal with one of the staffing issues confronting the Retirement Board is to amend the contract between our two respective Boards. This amendment would authorize the Retirement Board to contract directly with firms that provide temporary services. We look forward to discussing this issue at the Joint Meeting in May.

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