



Investment Program

RETIREMENT PLANS' COMPREHENSIVE FEE ANALYSIS

Office of Retirement Services

Investment Policy Statement on Investment Fees

“The Plan will seek alignment of interests when negotiating fees while pursuing the best net of fees performance results. Investment costs shall be monitored, controlled, and whenever possible negotiated to ensure cost effectiveness. The Board shall give consideration to the impact of administrative expenses, external management fees and performance fees when establishing the asset mix policy of the Plan. The Board will be provided reports on investment costs of the Plan at least annually.”

Understanding Investment Fee Analysis

- Complex topic
- Declining return expectations → Increased focus
 - $\text{Net returns} = \text{Gross returns} - \text{Management fees} - \text{Incentive fees} - \text{Operating Expenses}$
- A function of asset allocation and asset class structuring
 - Higher complexity = higher fees
- ORS comprehensive annual fee reporting started in 2015
 - Includes embedded or unobserved fees/expenses (e.g., fees not reported on statements)
 - Few public plans have comprehensive fee reporting (CalSTRS, OCERS)
 - No public-sector standard methodology for comprehensive fee reporting
- Complies with California Government Code §7514.7

Understanding Total Expense Ratio

Net returns = Gross returns – Management fees – Incentive fees – Operating Expenses

Fee type	Description	Examples
Management fees	Fees paid to investment management firms	
Incentive fees	Performance-based fees paid to investment management firms	
Operating expenses	Costs of administering individual investment vehicles	Audit, tax, legal, custodian
Other expenses	Costs incurred at the plan level	Staff salaries and benefits, consultants, third party vendors

Calendar Year 2023 Fees

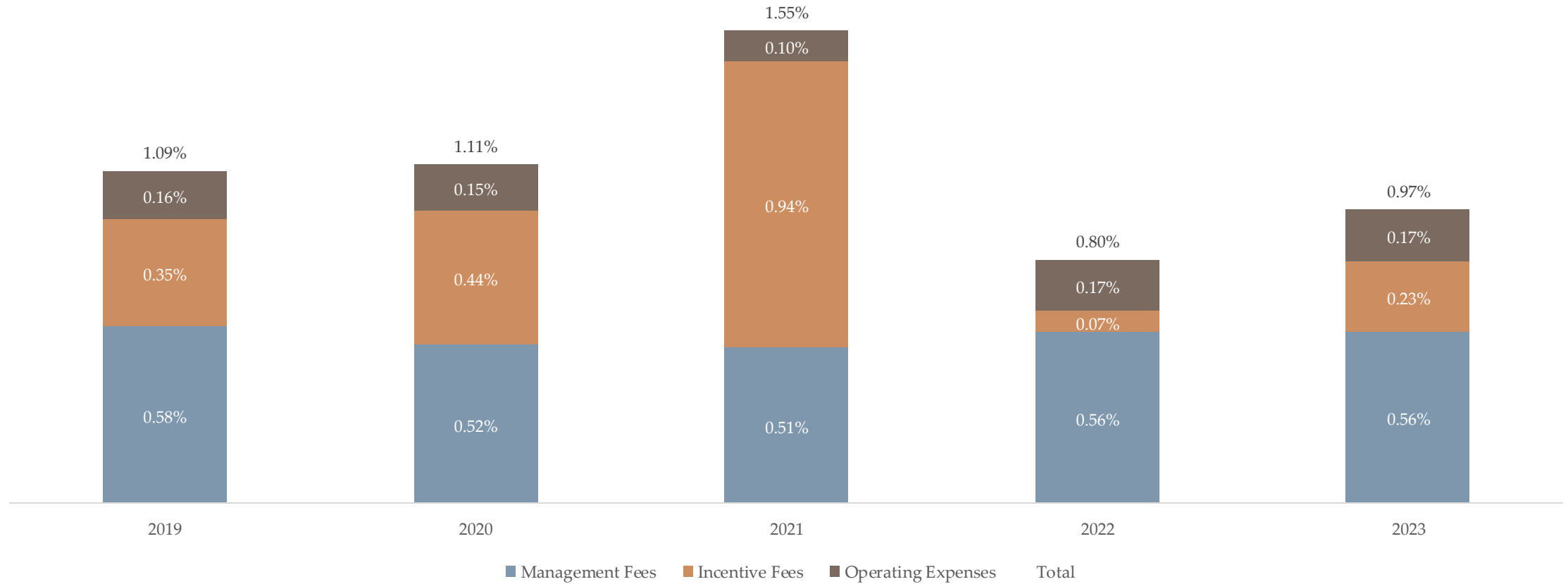
	Management Fees (\$ mm)	Incentive Fees (\$ mm)	Operating Expenses (\$ mm)	Mgmt, Incent, and Op Exp (\$ mm)	Average Balance (\$ mm)	Expense Ratio
Federated Pension	16.3	6.7	4.6	27.6	2,833	0.97%
Police & Fire Pension	26.4	10.3	8.7	45.4	4,690	0.97%
Federated Health Care	0.8	-	0.1	0.9	359	0.24%
Police & Fire Health Care	0.4	0.0	0.1	0.5	289	0.17%
All 4 ORS Plans	43.9	17.0	13.4	74.4	8,171	0.91%

Source: ORS 2023 Fee Report
Values show are in \$ millions

Investment Staff Salary and Benefits (\$ mm)	Consultants (\$ mm)	Custodian (\$ mm)	Other Vendors and Travel (\$ mm)	Total Other Costs (\$ mm)	Other Costs Fee Ratio
2.6	1.1	1.0	1.3	6.0	0.07%

Source: ORS 2023 Fee Report
Values show are in \$ millions

Total Expense Ratio (Comprehensive)



San Jose Consolidated

Net Returns: 14.1% (2019)

14.3% (2020)

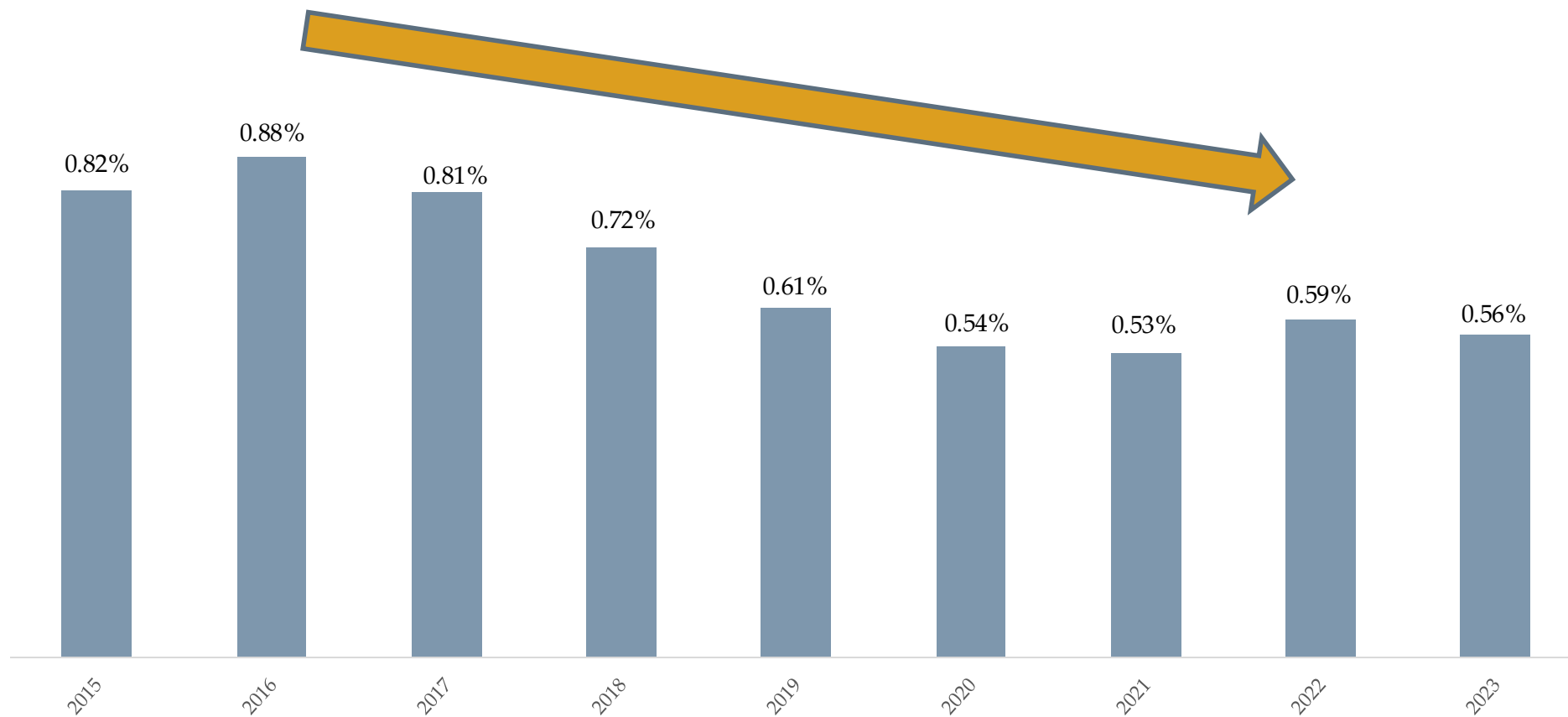
14.9% (2021)

-9.2% (2022)

9.7% (2023)

**Total Expense Ratio consolidated between both pension plans*

Management Fee Ratio Trend



Source: ORS, BNY Mellon

*Charts only represent fund management fees, not incentive or fund operating expenses

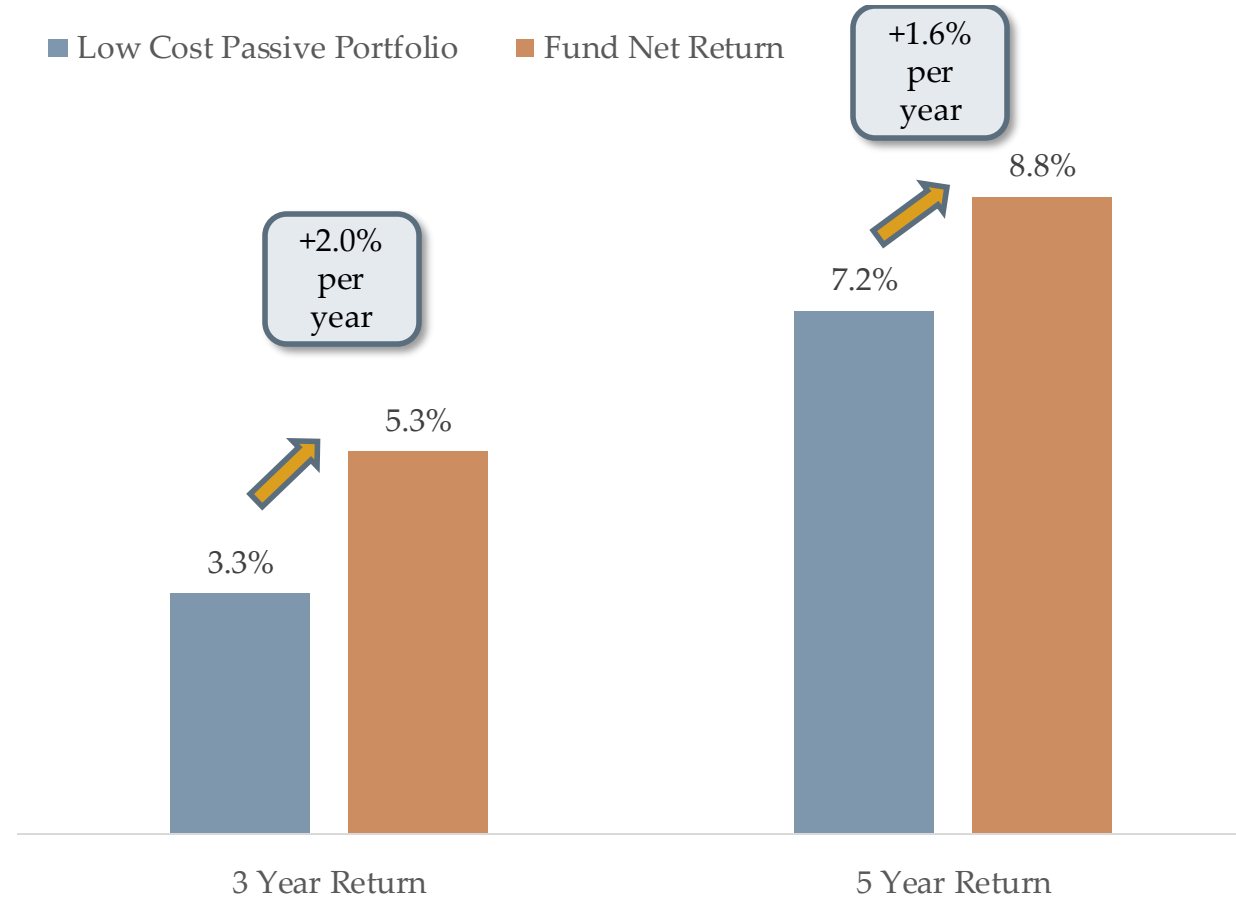
*Management Fee Ratio consolidated between both pension plans

\$18.5 million of estimated fee savings generated in 2023

Asset Class	Fee Savings (\$ mm)
Growth	17.4
Public Equity	4.3
Total Private Markets	12.8
Emerging Market Bonds	0.2
High Yield Bonds	0.0
Low Beta	0.5
Market Neutral Strategies	0.5
Other	0.8
Core Real Estate	0.8
Investment Grade Bonds	0.0
Total Plan	18.5

- Sources of fee savings include Staff negotiations, early investor discounts, and volume discounts.
- Private Markets estimated fee savings based on commitments that closed in calendar year 2023.
- Additional fee savings not modeled include fee structures of fund-of-ones compared to fund-of-funds alternative, upside performance of investments with incentive fee discounts, and fee savings from Private Markets commitments prior to 2023.

Value Added From Active Strategies



Estimated Cumulative Value Added in \$:

\$438.8 million

\$531.6 million

As of December 31, 2023

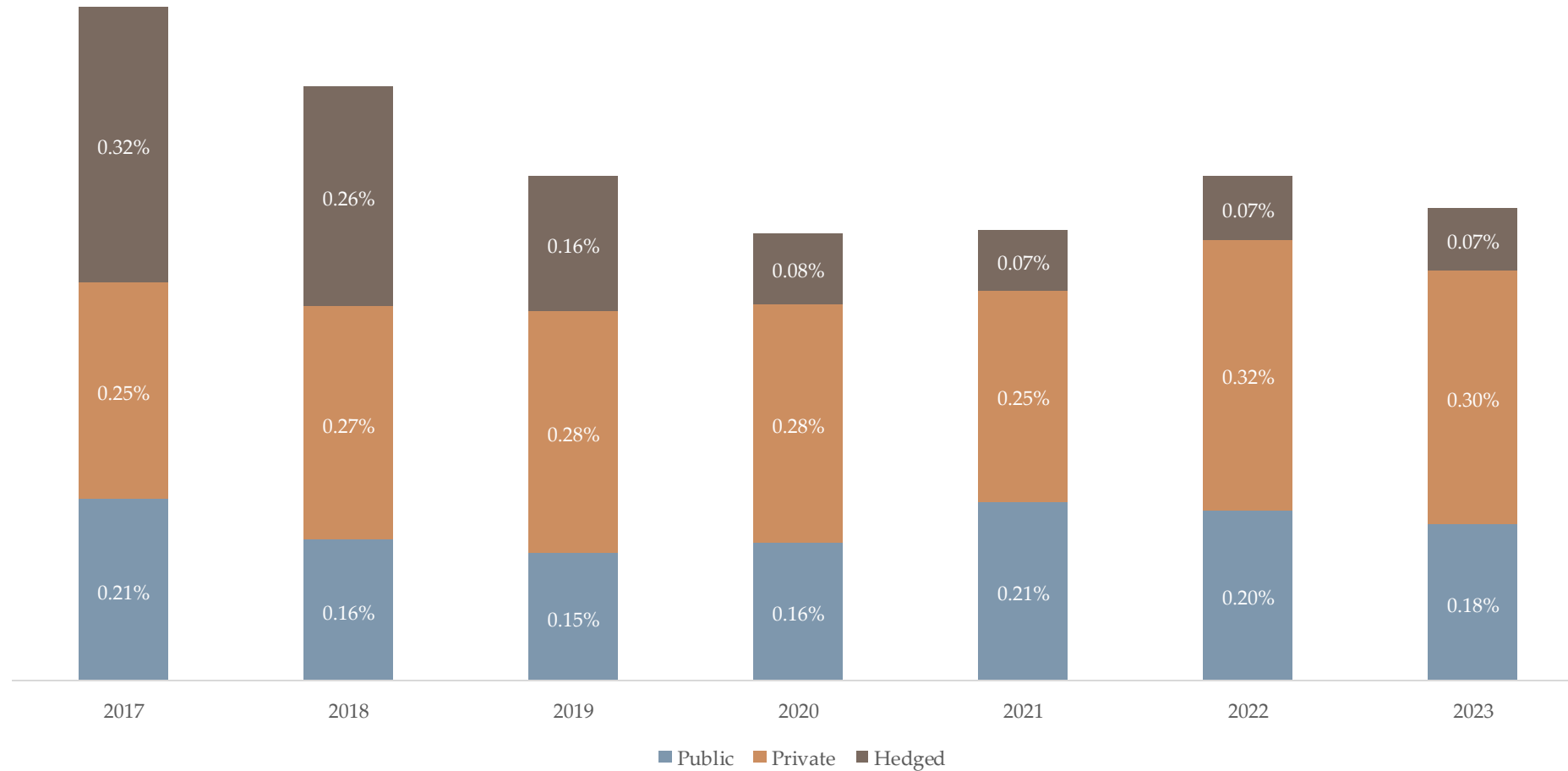
**Low-Cost Passive Portfolio: Calculation of Board strategic asset allocation targets using public market benchmarks managed on a passive basis.*

Appendix

Glossary of Terms

- Active strategies: Funds that attempt to outperform an index
- Asset allocation: Distribution of assets across a number of asset classes that each exhibit a unique combination of risk and expected return. Asset allocation is the most important determinant of long-term plan performance
- Hedged strategies: Investments that generally seek to achieve a return regardless of market direction
- Gross returns: Returns before the deduction of expenses
- Incentive fees: Performance-based fees paid to individual investment management firms. Incentive fees are a form of shared economics. Also known as “carried interest”
- Management fees: Asset-based fees paid to individual investment management firms
- Net returns: Returns after the deduction of management fees, incentive fees, and operating expenses
- Operating expenses: Costs of administering individual investment vehicles (not the retirement plans)
- Other expenses: Costs incurred at the plan level (staff, consultants, third party vendors, etc.)
- Passive strategies: Investments that intend to match the return of an index
- Private strategies: Investments in illiquid assets such as privately held companies or real estate
- Total expense ratio: Total expenses (sum of management fees, incentive fees, and operating expenses) divided by average plan assets

Contribution to Management Fee Ratio by Fund Type

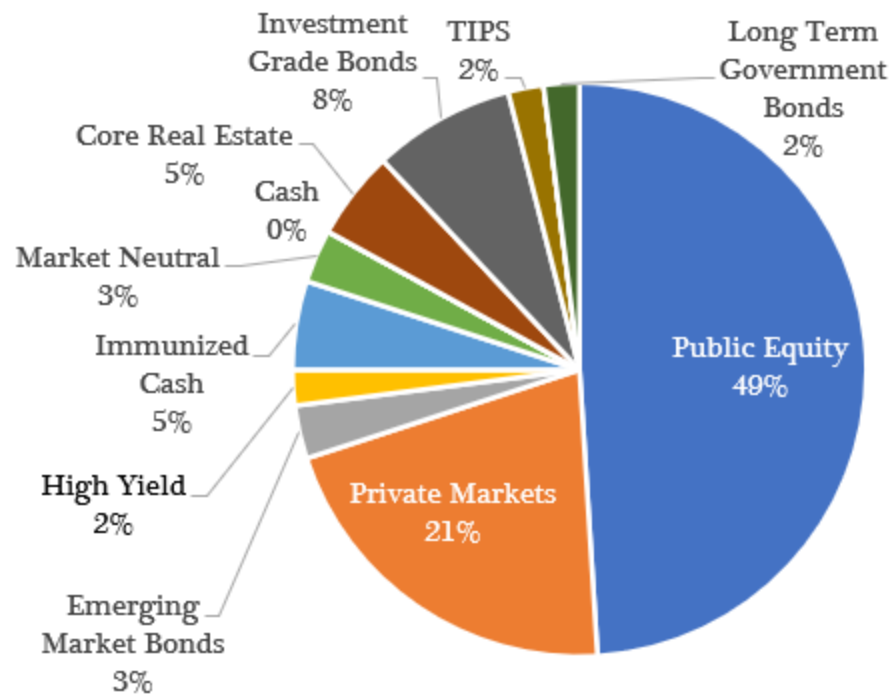


**Active strategies only*
**Consolidated between both pension plans*

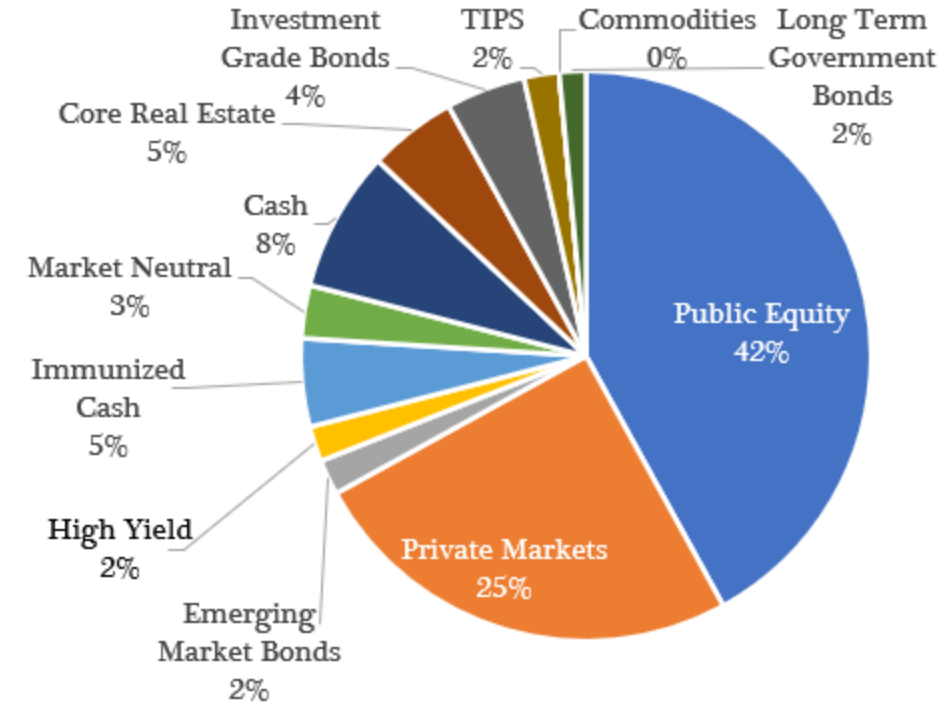
Asset Allocation Targets

As of December 31st, 2023

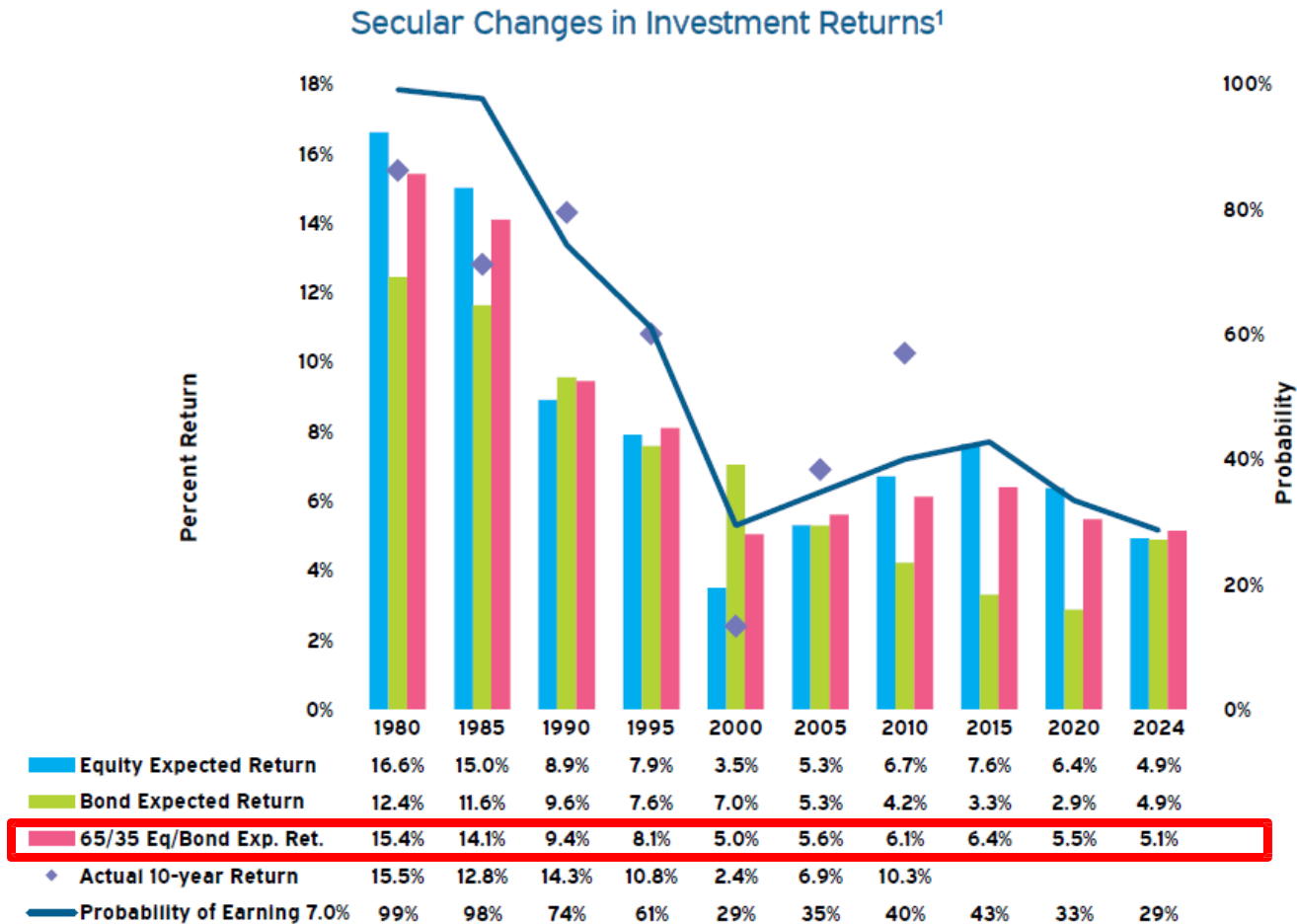
Federated Pension



Police & Fire Pension



Asset Allocation Considerations



Source: Meketa Investment Group

¹ Expected return assumptions for 1) Bonds equals the yield of the ten-year Treasury plus 100 basis points, and 2) Equities equals the dividend yield plus the earnings yield of the S&P 500 index (using the inflation-adjusted trailing 10-year earnings). Probability calculation is for the subsequent ten years.

Asset Allocation Considerations

	Fed Current (%)	P&F Current (%)	60/40 (%)
Expected Return 20 Years ¹	8.5	8.5	7.4
Standard Deviation ¹	13.4	13.2	10.7
Probability of Achieving at least a 6.625% Return			
1 Year	55.7	55.5	52.8
3 years	59.7	59.5	54.9
5 Years	62.5	62.2	56.3
10 Years	67.4	67.0	58.9
20 Years	73.8	73.3	62.5
Worst Case Returns²			
1 Year	-18.3	-18.0	-14.7
3 Years	-7.9	-7.7	-6.0
5 Years	-4.5	-4.3	-3.1
10 Years	-0.8	-0.8	-0.2
20 Years	1.8	1.9	2.0
US Equities Decline 25%	-17.5	-16.6	-14.0
US Equities decline 40%	-26.8	-25.2	-23.8

¹ Expected return and standard deviation are based on Meketa Investment Group's 2024 Annual Asset Study and reflect our 20-year expectations. Returns for periods longer than one year are annualized.

² "WorstCase" return projections encompass 99% of all possible outcomes.

Plan Return History

	10 Years Ending 6/30/24	10 Years Ending 12/31/23	10 Years Ending 6/30/23	10 Years Ending 12/31/22	10 Years Ending 6/30/22	10 Years Ending 12/31/21	10 Years Ending 6/30/21	10 Years Ending 12/31/20	20 Years Ending 6/30/24	20 Years Ending 12/31/23	20 Years Ending 6/30/23	20 Years Ending 12/31/22	20 Years Ending 6/30/22	1/31/94- 6/30/23
San Jose Federated City Employees' Retirement System	5.8%	5.9%	6.3%	5.6%	6.3%	7.6%	6.4%	5.9%	5.9%	6.5%	6.2%	6.3%	6.2%	6.8%
<i>Federated Policy Benchmarks</i>	5.8%	5.9%	6.5%	6.1%	6.6%	8.1%	6.9%	6.2%	6.3%	6.8%	6.5%	6.6%	6.4%	7.10%
<i>Federated Investable Benchmark Portfolio</i>	5.4%	5.5%	5.8%	5.4%	6.0%	7.5%	6.3%	5.7%	5.9%					
San Jose Police and Federated Department Retirement Plan	5.8%	5.8%	6.2	5.6	6.4%	7.9%	6.9%	6.3%	6.1%	6.1%	6.5%	6.6%	6.4%	8.3%
<i>Police and Fire Benchmark</i>	5.9%	6.0%	6.3%	5.8%	6.4%	8.0%	7.1%	6.7%	6.4%	6.4%	6.6%	6.7%	6.4%	7.10%
<i>Police and Fire Investible Benchmark Portfolio</i>	5.6%	5.7%	6.1%	5.6%	6.2%	7.8%	6.9%	6.9%	6.3%	6.4%	6.7%	6.9%	6.4%	
DB Plans > \$1 Billion Net Peer Universe	6.3%	6.6%	7.3%	6.9%	7.6%	9.7%	8.2%	7.9%	6.7%	6.7%	7.0%	7.2%	6.8%	6.0%
<i>Number of Plans</i>	83	159	62	54	57	68	72	73	61	114	51	40	42	44