

Dallas Police and Fire Pension and Employee Retirement Fund: Investment Portfolio Review and Discussion

Ad Hoc Committee on Pensions

Commerce Street Investment Management



Initial discussion



A few points most everyone can agree on:

- Both the Dallas Police & Fire Pension Fund and Dallas Employees' Retirement Fund are underfunded (~39% and ~73% funding ratios, respectively)
- 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 plans are being optimally managed

Source: *Dallas Police and Fire Pension Actuarial Valuation and Review as of January 1, 2023 and Employees' Retirement Fund of the City of Dallas Actuarial Valuation Report as of December 31, 2022*

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

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 Plans in many ways

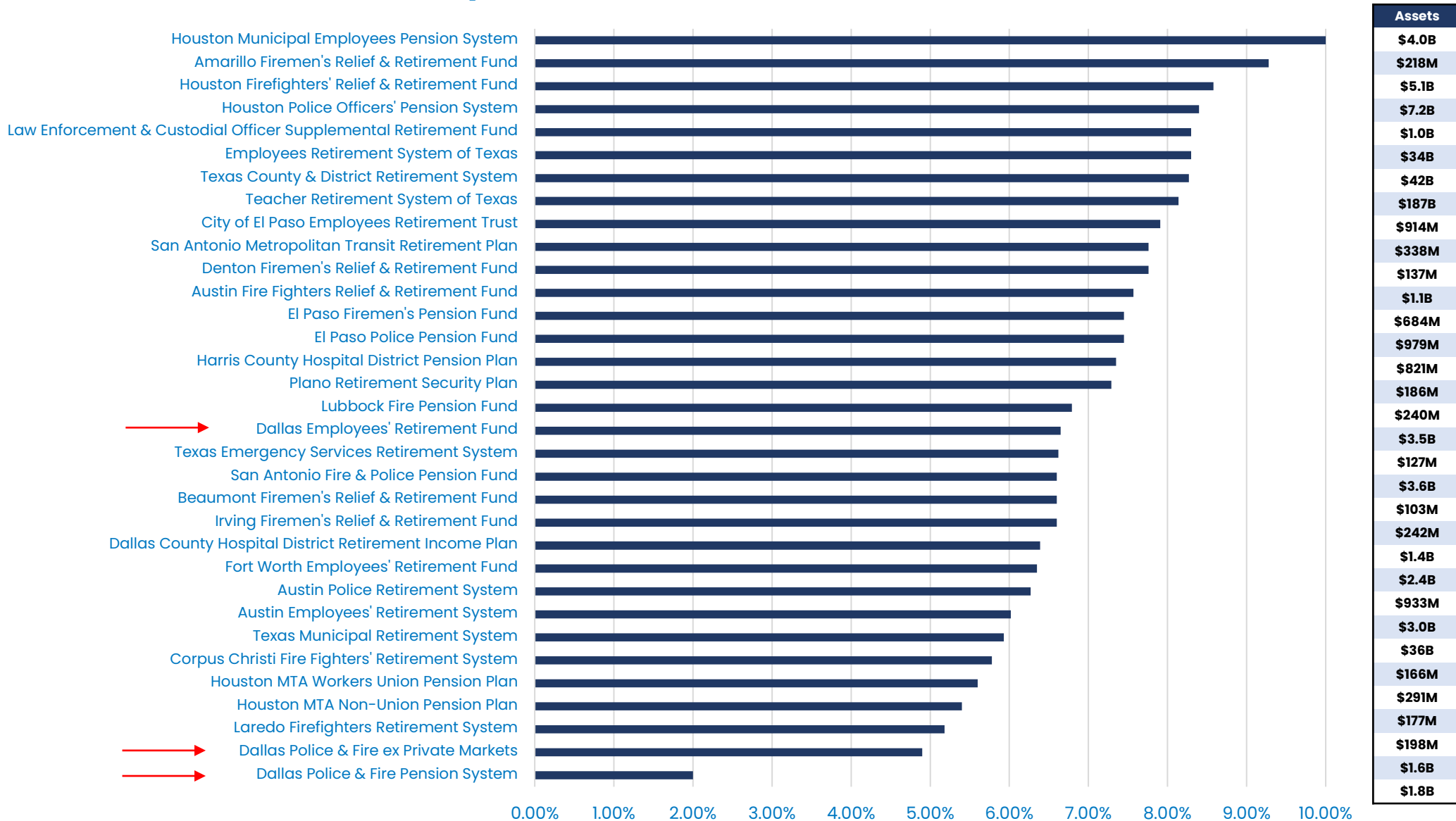
- It provides transparency for performance, management, and governance’s effectiveness
- It can give us new ideas and insight
- Done correctly, it lays the groundwork for outperformance

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

DPFP and ERF compared to their peers



10-Year Net Returns for pensions in the state of Texas with >\$100mm in assets



Source: Texas Pension Review Board. <https://data.prb.texas.gov/comparison/index.html> as of 12/31/22

DPFP and ERF vs. returns of largest Texas cities



Data as of 12/31/22	3-Year	5-Year	10-Year
Dallas Police and Fire	1.5%	2.8%	2.0%
DPFP ex Private Markets	2.3%	3.5%	4.9%
Dallas ERF	3.9%	4.7%	6.6%
Houston MEPS*	13.1%	11.1%	10.2%
Houston Firefighters*	11.0%	9.4%	8.7%
Houston Police*	9.6%	9.1%	8.4%
Texas County & District RS	8.3%	7.8%	8.3%
Austin Fire	5.8%	5.9%	7.2%
San Antonio Fire & Police	4.3%	4.6%	6.6%
Austin Police	5.1%	5.7%	6.3%
Austin ERS	1.9%	3.7%	6.0%

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

*Plans with fiscal years ending 6/30/22

DPFP and ERF vs. national and Texas returns for similar sized funds



Data as of 12/31/22	3-Year	5-Year	10-Year
Dallas Police and Fire	1.5%	2.8%	2.0%
DPFP ex Private Markets	2.3%	3.5%	4.9%
Dallas ERF	3.9%	4.7%	6.7%
National Bottom Quartile	3.8%	4.6%	6.6%
National Average	4.6%	5.5%	7.1%
National Top Quartile	5.8%	6.0%	7.7%
Texas Average*	4.1%	5.1%	6.1%
Texas Top Quartile*	4.9%	5.8%	7.0%
Texas Top Decile*	6.7%	6.7%	7.7%

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

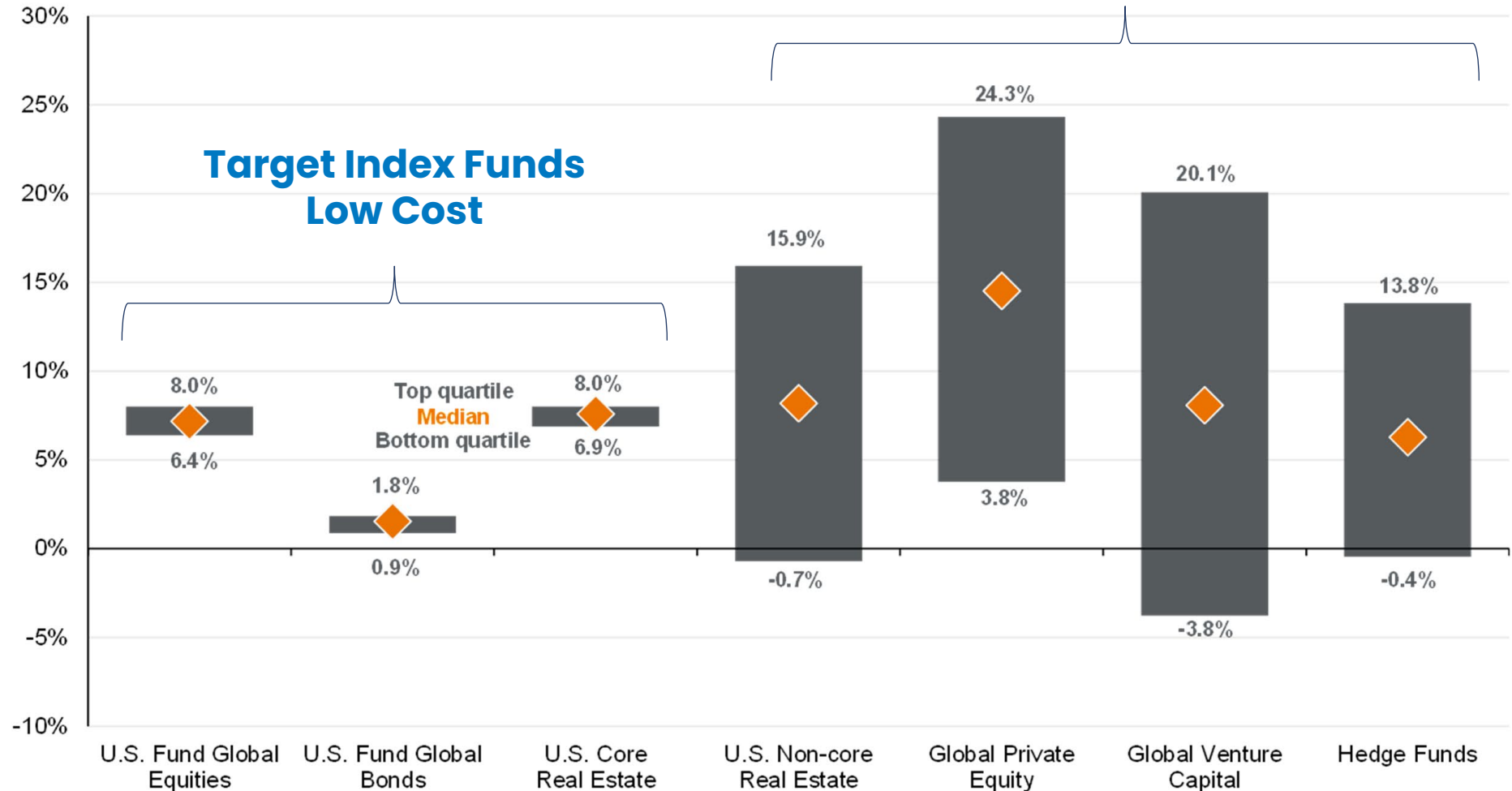
National quartile rankings provided by Meketa

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

Active managers are more valuable in private asset classes



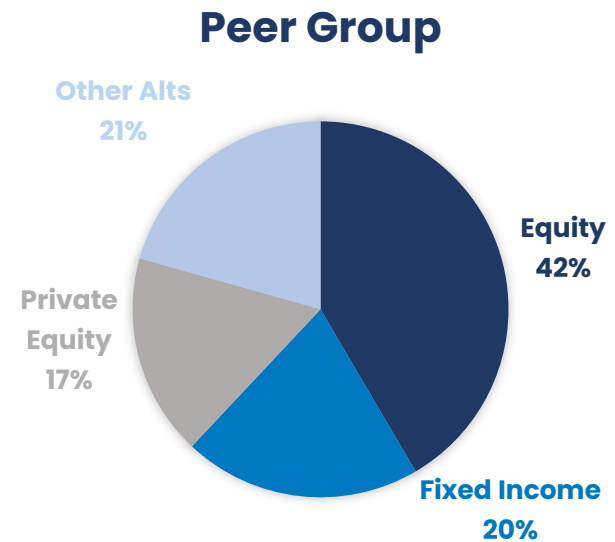
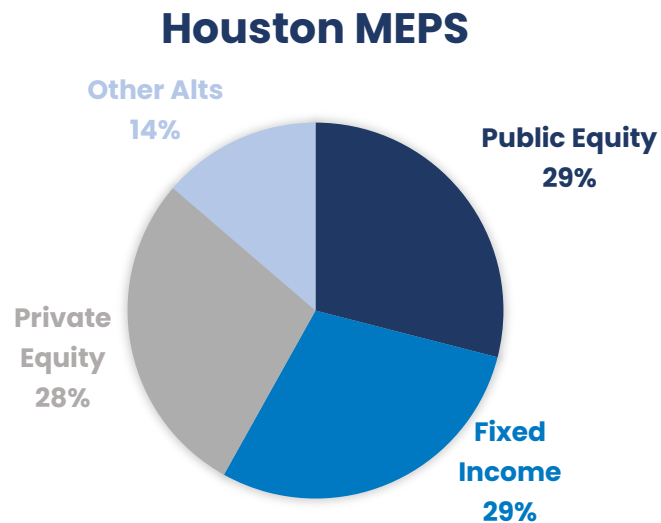
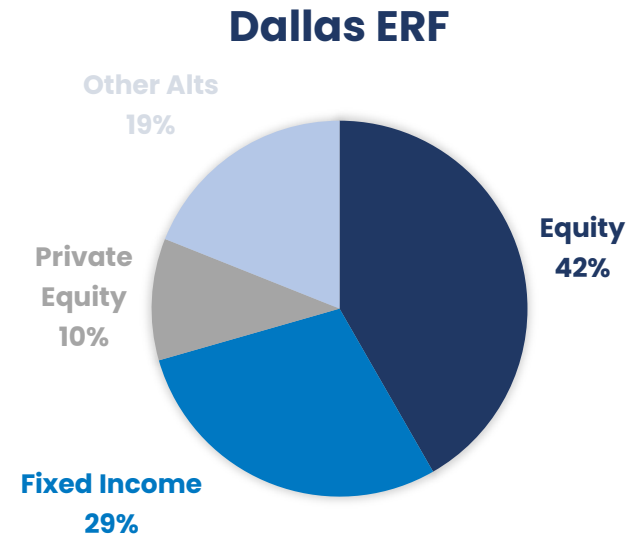
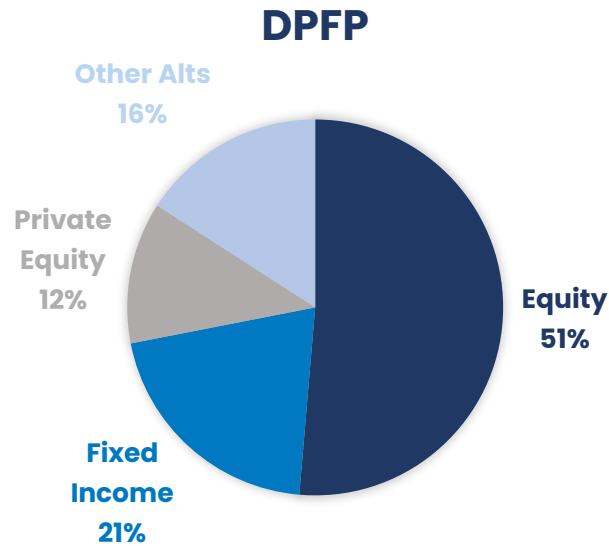
Public and private manager dispersion
Based on returns over a 10-year window*



Spend Time/Money

Source: JPMorgan Guide to the Markets

DPFP and ERF's asset allocations



Data as of 6/30/23

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

The biggest contributors to DFPF's underperformance is private equity allocation and performance



As of 6/30/23	Investment Weights		
	DFPF	HMEPS	Peer Group
Public Equity	51.4%	29.0%	43.3%
Private Equity	12.2%	28.2%	21.3%
Fixed Income	20.5%	25.8%	18.1%
Other Alts	15.8%	17.0%	21.5%

As of 6/30/23	Returns (5 Year)		
	DFPF	HMEPS	Peer Group
Public Equity	8.20%	6.90%	7.52%
Private Equity	4.80%	17.60%	17.47%
Fixed Income	1.14%	7.41%	2.64%
Other Alts	2.53%	8.02%	6.87%

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

The biggest contributor to ERF's underperformance is under-allocation to private equity

As of 6/30/23	Investment Weights		
	ERF	HMEPS	Peer Group
Public Equity	41.7%	29.0%	43.3%
Private Equity	10.5%	28.2%	21.3%
Fixed Income	28.9%	25.8%	18.1%
Other Alts	19.0%	17.0%	21.5%

As of 6/30/23	Returns (5 Year)		
	ERF	HMEPS	Peer Group
Public Equity	6.67%	6.90%	7.52%
Private Equity	14.86%	17.60%	17.47%
Fixed Income	2.05%	7.41%	2.64%
Other Alts	5.37%	8.02%	6.87%

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

A top quartile allocation with average returns would result in...



As of 9/30/23	Weighting*	3-Year	5-Year	10-Year
Public Equity	39.6%	6.9%	6.5%	7.6%
Fixed Income	21.5%	0.9%	3.6%	8.0%
Private Equity	17.4%	18.0%	17.0%	16.3%
Other Alts	17.5%	11.7%	6.1%	7.0%
Commodities	4.1%	16.2%	6.1%	-0.8%
Total	100.0%	8.8%	7.6%	8.7%
DPFP	100.0%	4.2%	3.2%	1.6%
DPFP ex Privates	100.0%	3.8%	4.4%	5.0%
ERF	100.0%	6.5%	4.7%	5.9%

*Weightings come from top quartile pensions nationally according to <https://publicplansdata.org/public-plans-database/browse-data/>

Indexes 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 – Indxx Private Credit TR + S&P Global Infrastructure + Cambridge Associates Real Estate Index (equal-weighted), Commodities – Bloomberg Commodity

Thoughts for the City of Dallas



In order to improve the performance of both funds, the City should consider:

1. Analyze in detail what top performing peers have done
2. Collaborate with both plans to identify strategies for improvement
3. Work to improve their governance policies and procedures as needed
4. Work to improve the working relationships of the key fiduciaries to these plans as needed
5. Prepare ongoing reports for the City of Dallas with the findings
6. Provide concrete recommendations for consideration to achieve best practice to improve the performance of DPFP & ERF for all stakeholders – beneficiaries, taxpayers and staff

Give confidence to citizens and stakeholders of good fiduciary stewardship when confronted with additional contributions to the pension funds

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