



Board of Retirement Regular Meeting

Sacramento County Employees' Retirement System

Agenda Item 16

MEETING DATE: February 17, 2021

SUBJECT: Alternative Assets Consultant Recommendation

SUBMITTED FOR: ___ Consent X Deliberation and Action ___ Receive and File

RECOMMENDATION

Staff recommends the Board renew and extend the contract with Cliffwater, LLC for alternative assets consulting services, for a three-year term, and authorize SCERS' Chief Executive Officer to negotiate and execute documents necessary to update the contract.

PURPOSE

This item supports the Strategic Management Plan objective to leverage external experts to maximize investment guidance and results.

SUMMARY

Staff recommends the Board retain Cliffwater as SCERS' alternative assets consultant and renew the contract with Cliffwater for a three-year term. The recommendation is based on Cliffwater's decade-long partnership in the development of SCERS' alternative assets portfolio that has delivered strong performance in aggregate, and Staff's view that the firm will meet SCERS' consulting needs over the next several years.

Cliffwater brings a strong culture, a solid approach to portfolio construction, good accessibility to differentiated investment managers, differentiated manager due diligence through the depth of their research, and a strong working relationship with the SCERS Board and Staff. In addition, Cliffwater proposed the lowest fee for SCERS. The other finalists come from solid firms with good resources, reputations, breadth of coverage, and track records—any could be recommended in isolation. While Cliffwater, as a boutique consulting firm, may not have the same level of firm resources as other larger firms, Cliffwater's known qualities and services remain a good fit for SCERS.

DISCUSSION

Consultant Responsibilities

The alternative assets investment consultant focuses on the following alternative SCERS asset classes that collectively comprise 26% of the total portfolio:

-
- Absolute Return
 - Private Equity
 - Private Credit
 - Real Assets

Specific duties and scope of service of the alternative assets investment consultant include:

- Development of long-term and annual strategic plans, and portfolio construction, across SCERS' alternative asset classes.
- Providing access to a broad range of alternative investment managers, and conducting initial and ongoing investment and operational due diligence of alternative asset managers.
- Investment performance and risk monitoring, measurement, and analytics.
- Development and maintenance of cash flow, liquidity, and pacing projections of SCERS' alternative asset classes.
- Collaborative work with SCERS' Staff, SCERS' Board, and SCERS' other consultants and advisors.
- Review of investment manager fund documents, and assisting SCERS in interpreting and negotiating key terms in contracts and manager fees.
- Creation of appropriate benchmarks to monitor performance.
- Board education.

Reasons for Issuing RFP

Cliffwater has served as SCERS' alternative assets consultant since 2011, and SCERS had not issued an alternative assets consultant request for proposals (RFP) since then. Staff viewed issuing the RFP in 2020 as a way to gauge the current market for alternative assets consultants and not necessarily as a signal that Cliffwater should be replaced. The RFP allowed SCERS to compare Cliffwater to other alternative assets consultants across several categories.

SCERS also wanted to assess topics related to alternative assets consulting, including:

- Institutional investing within alternative asset classes continues to evolve, with an increasing number of alternative asset classes, various approaches to implementation, and a more significant number of investment managers to underwrite.
- SCERS' alternative asset classes are maturing, and there are several considerations for implementation going forward, including:
 - Decisions between follow-on investments with existing general partners (GPs) and new investments with new GP relationships
 - The number of underlying funds in SCERS' portfolio, and managing against fund and manager proliferation
 - Use of co-investments and secondary investments to complement primary investments
 - Use of strategic partnerships to have greater control of the investment guidelines and better fee alignment.
- Evolving technology systems and software allow for more dynamic monitoring, analytics, performance attribution, fee/expense aggregation, and increased reporting frequency.

Having sufficient analytical tools available to Staff to properly oversee and manage the portfolio has become an increasingly important consideration.

Evaluation Process

Staff created the RFP to evaluate the capabilities of alternative assets consultant candidates across a number of categories, including conflicts of interest, client information, client servicing team, consulting services, manager research, operational due diligence, risk management, performance, client access to fund managers, performance reporting and monitoring, and fees.

Staff sent the RFP to a group of alternative assets consultants in February 2020 identified by Staff as strong candidates and posted the RFP to the SCERS website. The responses were due on March 6, 2020, approximately two weeks before SCERS went into remote operations due to COVID-19. Seven firms submitted responses to the RFP.

After evaluating the RFP response submissions, Staff identified four finalist candidates interviewed by Staff, including SCERS' CEO, and a Board member in late October 2020. The finalist meetings allowed SCERS to drill deeper into capabilities and gauge the fit/compatibility with the Board, Staff, SCERS' other investment consultants, and SCERS' organizational culture. The firms identified for the discussions were:

1. Albourne
2. Aksia/TorreyCove
3. Aon
4. Cliffwater (incumbent).

Summary of Finalists

Aon

Aon has a strong private equity practice comprised of a deep bench of professionals with practical private equity experience. As the infrastructure asset class grew out of private equity in the early 2000s, followed by private debt, this team commenced covering these asset classes (along with other credit professionals), and has grown in scale over time. Aon has a significant general consulting business serving various client types, including numerous public employee retirement plans. Aon also offers real estate consulting through its acquisition of The Townsend Group, which serves as SCERS' dedicated real estate consultant.

Aon (inclusive of Townsend) is well staffed with 201 investment consultants, 50 performance analysts, 19 operational analysts, and 97 investment analysts. The combined group has 451 clients using AON for private equity investments. Aon works with a diverse set of investors, including over 100 public pension plans. Of the 451 clients, 100 are managed on a discretionary basis. Aon represents five California pension plans, and Townsend works with five pension plans, inclusive of SCERS. While well resourced on the client-facing and research side, Aon's client-facing technology is under-resourced. The analytical and statistical analyst tools are made available for the consulting team but not Staff. SCERS would have to request analysis, which can hinder portfolio construction and monitoring.

Aon offers potential clients a wide range of possible services, including general consulting, outsourced CIO, and a wide range of asset-level consulting services. The breadth of services is an asset to their alternative asset consulting services bringing a total plan view when making investments, something not directly seen by the other finalist clients. Aon's team approach encourages staff to develop relationships with the asset teams rather than directing all communication through a single point of contact. Given the size of Aon's platform and the potential of other Aon clients seeking assets with GPs, building direct communication and relationships with managers is paramount.

The firm is a large global investment consultant that offers a platform with a broad range of institutional funds across all asset categories. Aon's investment research teams draw from their professionals' well-developed networks. Some of their professionals are 15-25+ year veterans in their respective fields, with extensive access to managers, industry contacts, events, and other professionals. The firm's broad client base provides an expansive universe of a diverse set of underlying managers, leading to better knowledge when making manager selections. However, many of the tools used to build portfolios are not readily available to clients.

Albourne

With a staff of 417, including 275 analysts and offices in 11 locations worldwide, Albourne is one of the largest dedicated alternative asset consultants. They have over 280 clients, ranging across public pension plans, corporate pensions, sovereign wealth funds, endowments, foundations, family offices, and financial institutions. Albourne clients have over \$550 billion invested in alternative asset classes. The clients are based in 27 countries and 36 U.S. states. Albourne advises six California pension funds.

The firm is 100% owned by 28 full-time employee shareholders, the Albourne Employee Benefit Trust, and a trust created for the founder's family. Albourne follows a deliberate policy of distributing share options to selected employees to broaden the shareholder base, contributing to Albourne's stability as a firm. Albourne's diverse and extensive client base affords them a large pool of data for which Albourne has built the infrastructure and tools to maximize its use.

Albourne has the largest research team of all the managers in the RFP, and size affords them the ability to have significant breadth across the asset classes they cover. Albourne offers sophisticated analytical tools through its data system, which can serve as a valuable resource to its clients. The database tracks robust fund and holding level data, giving clients a detailed understanding of the portfolio and associated risks. Scenario analysis and hypothetical portfolio construction are also valuable tools made available to clients.

Albourne is a large global organization offering clients local access to a wide range of investment opportunities across private markets and absolute return. The platform provides a wide range of services such as a middle office offering, including help with legal negotiations, fee reduction opportunities, maintaining legal documents, and a host of other important non-investment related items. Albourne has a very flexible system for interacting with clients, allowing them to be as hands-on with the technology and team as clients want. While Albourne does not have, nor do they desire to have proprietary capital, they have a large client base, which could impact allocations if there is limited access to a manager. Albourne is a global organization with staff in

the U.S. and Europe administering the portfolio, allowing staff to tap into a worldwide network to improve delivery times and increase detail in the underlying portfolio.

A consideration with Albourne is the firm's scale and the amount of data and information available, and whether SCERS' smaller staff would get full use of it.

Aksia

Aksia employs 177 professionals globally, including 96 research and risk professionals, and is 100% employee-owned by its 11 partners. On January 8, 2020, Aksia announced that it has agreed to acquire TorreyCove, a boutique private markets consulting specialist. The transaction closed in April 2020. The two firms submitted a bid as part of SCERS' RFP process before the transaction closed. The combined firms advise on over \$160 billion in alternative assets with more than 240 professionals globally, including over 150 professionals focused on research and risk management.

Aksia seeks to act as an extension of a client's staff. The firm treats all portfolios as bespoke and dependent on clients' specific needs and objectives. SCERS would have full access to research analysts and portfolio risk professionals during all parts of the diligence process. SCERS' dedicated advisory team would support the day-to-day needs and coordination of resources; however, clients have direct access to Aksia staff and generally develop close contacts with senior members of the research teams. Aksia works directly with a client's unique portfolio needs and does not operate from a typically narrow or limited 'recommended' or 'buy list' of funds.

Aksia has one of the more robust technology platforms seen during the RFP process, through Aksia's analytics platform, which is used by Aksia as well as its clients. Private market data is tracked down to the holding level, giving clients a detailed understanding of the portfolio and associated risks. Scenario analysis and hypothetical portfolio construction are just two of the tools made available to clients across private markets and hedge funds.

A consideration with Aksia is the pace of integration and synergies between Aksia and Torrey Cover, which could take time to play out.

Cliffwater

Cliffwater has been SCERS' alternative assets consultant since 2011. They have worked closely with the Board and Staff to build a diversified alternative assets portfolio, across direct private market and absolute return investments. They have also worked well with SCERS' other plan consultants within SCERS' broader strategic asset allocation to deliver consistent performance across economic and market cycles.

Cliffwater was founded in 2004 by a group of experienced investment professionals from Wilshire Associates with the belief that alternative investments (private debt, private equity, hedge funds, real estate, and real assets), in combination with traditional asset classes, provide investors the best opportunity for long-term returns and diversification. Cliffwater advises on approximately \$73 billion in assets, and the firm's 47 clients are well diversified by number, with high net worth clients representing 30% of total clients. Public pension plans account for 88% of total assets, with one public plan representing 44% of assets under advisement. Over the last

few years, Cliffwater's client base has been stable by number, with client departures offset by new clients. Cliffwater has a smaller client base by design, allowing for a low client-to-consultant ratio. Of the finalist group of firms reviewed, as part of the RFP, only Cliffwater and Aksia do not have third-party shareholders.

Cliffwater employs 46 professionals across two offices in Los Angeles and New York, including 5 consultants and 23 research professionals. Cliffwater's investment team is arranged by asset class and sub-asset class. Clients are encouraged to work with Cliffwater's industry specialists. These experienced professionals are responsible for investment due diligence, monitoring investments, evaluating co-investments, and advising on secondary investments. Cliffwater also has a separate and dedicated team to work on operational due diligence. The average investment experience of Cliffwater's consulting team is approximately 31 years, with the average tenure at the firm being about 15 years.

Cliffwater understands SCERS' investment philosophies and objectives, and its approach to strategic asset allocation, which translates well into constructing and implementing alternative assets portfolios. Cliffwater's due diligence reports find a nice balance between being thorough and succinct in the information and considerations they provide, and are a critical component of SCERS' investment process. In speaking with managers/GPs, Cliffwater has a strong reputation as it relates to the thoroughness and depth of their due diligence.

Cliffwater's analytical tools are intuitive and are geared towards manager research, portfolio monitoring, and asset class analytics. There is a broad range of deliverables accessible via the client relationship team, but not as much that clients can access directly. Cliffwater allows for some scenario and portfolio customization modeling for the absolute return portfolio; however, the system does not provide more granular views on the entire alternative assets portfolio, including dynamic views on factor and industry exposures, or portfolio company level data within the private markets like some of the other consultants.

CONCLUSION

SCERS' alternative assets portfolio has evolved and matured significantly over the 10 years since Cliffwater was hired. SCERS' alternative assets consulting needs are based less on designing and implementing an alternative assets portfolio from scratch, but rather on completing the build out of some asset classes, fine-tuning and maintaining exposures across other asset classes, opportunistically adding new investment managers and strategies, and providing proper Staff tools to oversee and analyze a multitude of existing exposures and risks within the current portfolio.

All of the candidates in the selection process bring a varying suite of manager relationships, expertise, tools, skills, and resources the Board and Staff would find useful. With track records somewhat balanced across the consultant pool, Staff looked at additional factors, such as organizational structure, team sizing/dynamics, resumes of key staff, firm experience, investment and operational due diligence reports, scalability, and analytical tools and technology.

When comparing the finalist firms, Cliffwater has helped SCERS develop a strong-performing alternative assets portfolio on an absolute and relative basis, with a diverse set of investments

across a range of alternative asset classes. Some considerations in evaluating Cliffwater against the other candidates is that with fewer firm resources, Cliffwater takes a more narrowed focus approach across the alternative assets manager universe, while the other firms offer a broader approach, covering a greater number of managers and funds both within assets classes and across geographies. The other finalist firms are strong competitors to Cliffwater and have several differentiated offerings, including greater firm resources, broader manager and fund coverage, and in some cases more robust analytical tools. These offerings do translate to higher proposed fees compared to that proposed by Cliffwater, and in some cases, double the price.

As part of the recommendation, Staff will seek to update the language, scope of services, and terms within the Cliffwater contract as needed. While the recommended contract term is three years, the contract will have language that gives either party the ability to terminate the engagement upon notice, which is similar to language within SCERS' other investment consulting contracts. With this flexibility, SCERS will have the ability to evaluate Cliffwater on an ongoing basis.

Cliffwater currently charges SCERS a flat annual fee of \$450,000. Cliffwater has proposed keeping the existing annual fee for a renewed contract with SCERS. The current primary consulting relationship for SCERS will remain Jamie Feidler, and Cliffwater's CEO/CIO Stephen Nesbitt will remain as a co-consultant, in the renewed contract.

Prepared by:

/S/

Jim Donohue
Deputy Chief Investment Officer

Reviewed by:

/S/

Steve Davis
Chief Investment Officer

/S/

Eric Stern
Chief Executive Officer