

**Kerrie Vanden Bosch**  
MERS Chief Executive Officer

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# An Investment Update from MERS



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**An Investment Update from MERS**  
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# MERS Investment Portfolio Insights and Updates in the Wake of COVID-19

*Jeb Burns, Chief Investment Officer*  
*Michael Schrauben, Director of Asset Allocation*  
*Michael Charette, Managing Director of Investments*



# Agenda

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- MERS Portfolio Characteristics
- Managing Through a Crisis
- Current Market Environment
- Liquidity Considerations
- Portfolio Rebalancing

# MERS Portfolio Characteristics

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- Disciplined investment process
- Globally diversified
- Valuation focused investors
- May lag in periods of extended bull markets
- Focus on risk-adjusted returns

# Managing Through a Crisis

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## **Discipline**

- Critical to follow the model; eliminate emotion
- Rebalancing when an asset's return provides adequate compensation for the risk; you will never know the bottom

## **Patience**

- Volatility tends to persist and opportunities will continue to present themselves
- Rebalancing is a process

## **Communication**

- Team communication
  - Weekly PRC and daily portfolio positioning meetings/calls
- Discussions with brokers and custodial bank
- Conversations and webinars with managers and research providers
- Engagement with industry peers

## **Focus on the long-term**

- What opportunities will emerge?
- What lessons can we learn?

# Market Environment

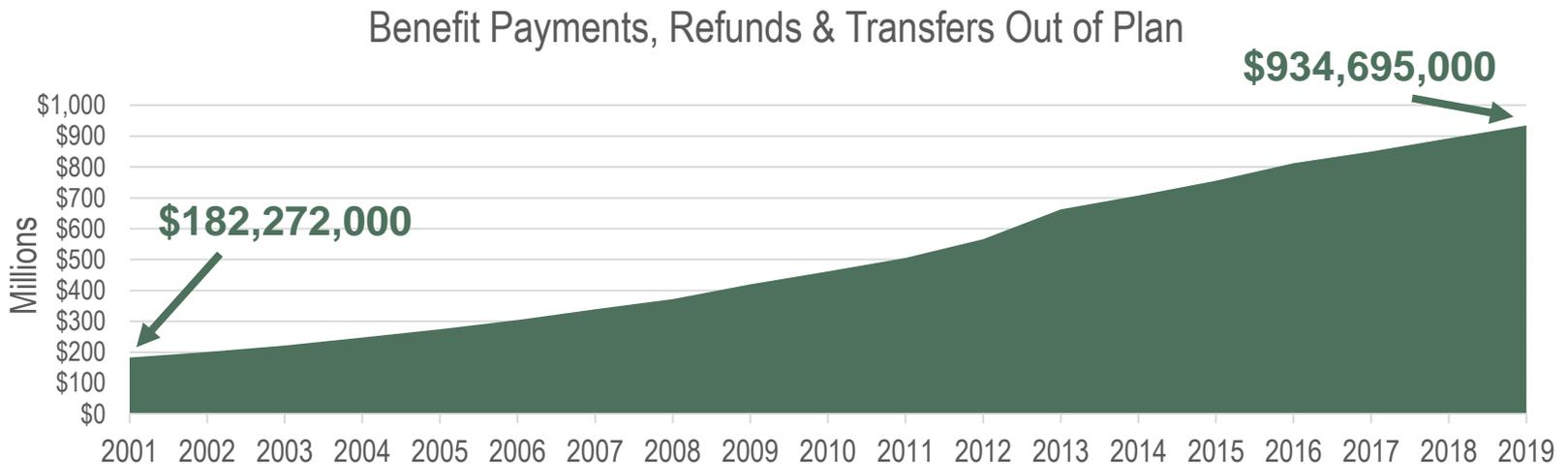
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- The last two months have seen unprecedented volatility (upside and downside)
  - Dramatic risk off then dramatic risk on
- Unprecedented economic decline
  - Materially worse than 2008/2009
- Unprecedented policy response
  - Both in the US and abroad
- How long to flatten the curve and reopen the economy?
  - What does a return to “normal” look like?
- What is the shape of the recovery?
  - L-shaped, U-shaped, or V-shaped

# Liquidity Considerations

It's important to proactively manage liquidity **before and during** a crisis to ensure the following:

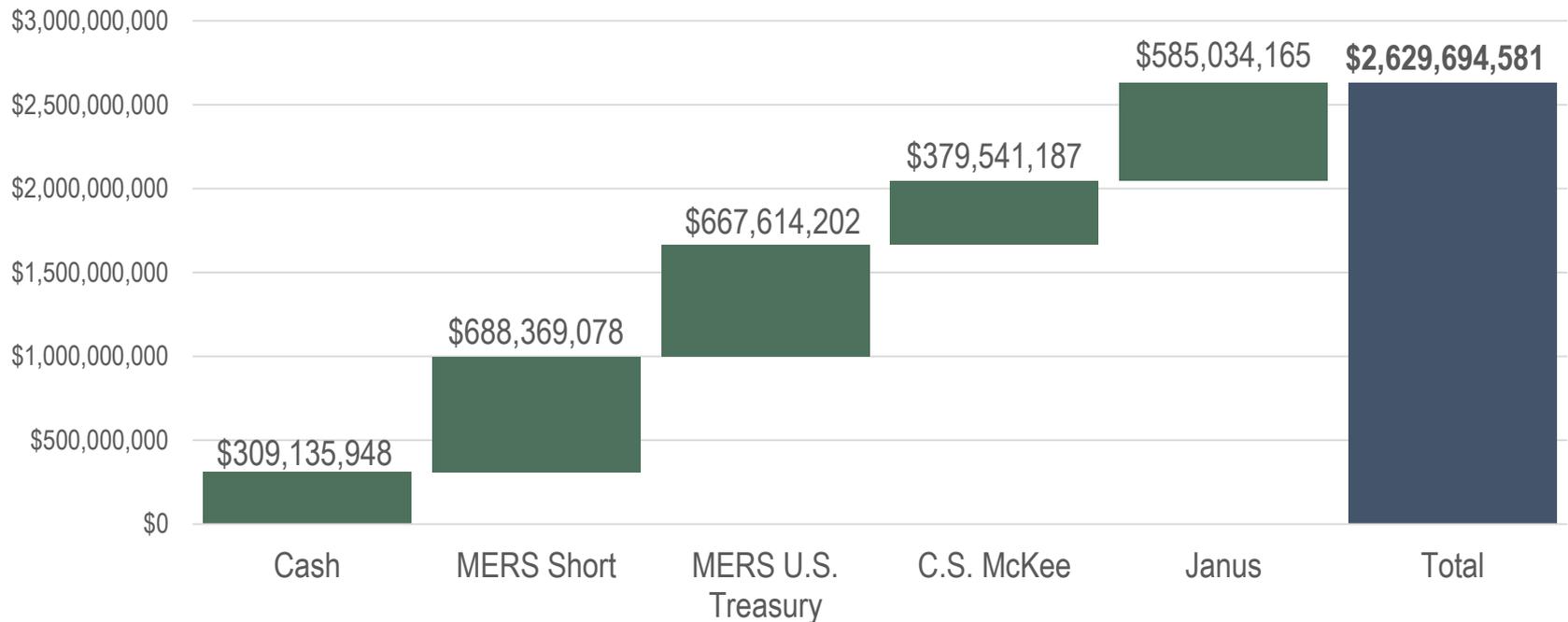
1. **Monthly pension obligations are paid**
2. Don't forget #1
3. Contractual private market capital calls are met
4. Adequate liquidity to rebalance the portfolio and take advantage of market opportunities



# MERS' Pre-Crisis Liquidity

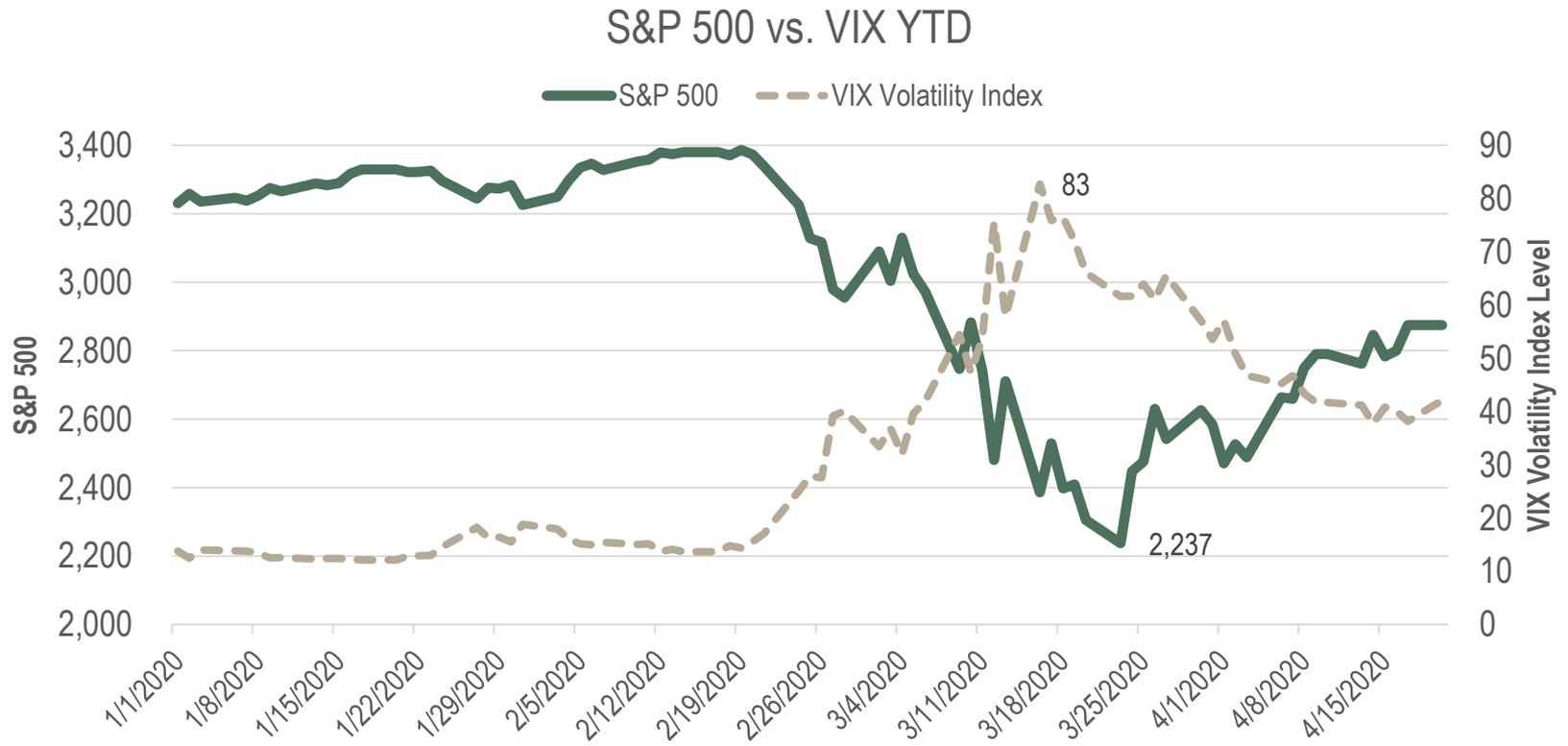
- MERS was well positioned heading into crisis
- 25% of portfolio was in cash and core fixed income

MERS Liquidity Waterfall as of January 31, 2020



# Market Volatility

- S&P 500 was down over 30% from all time high
- VIX volatility reached 2008 levels



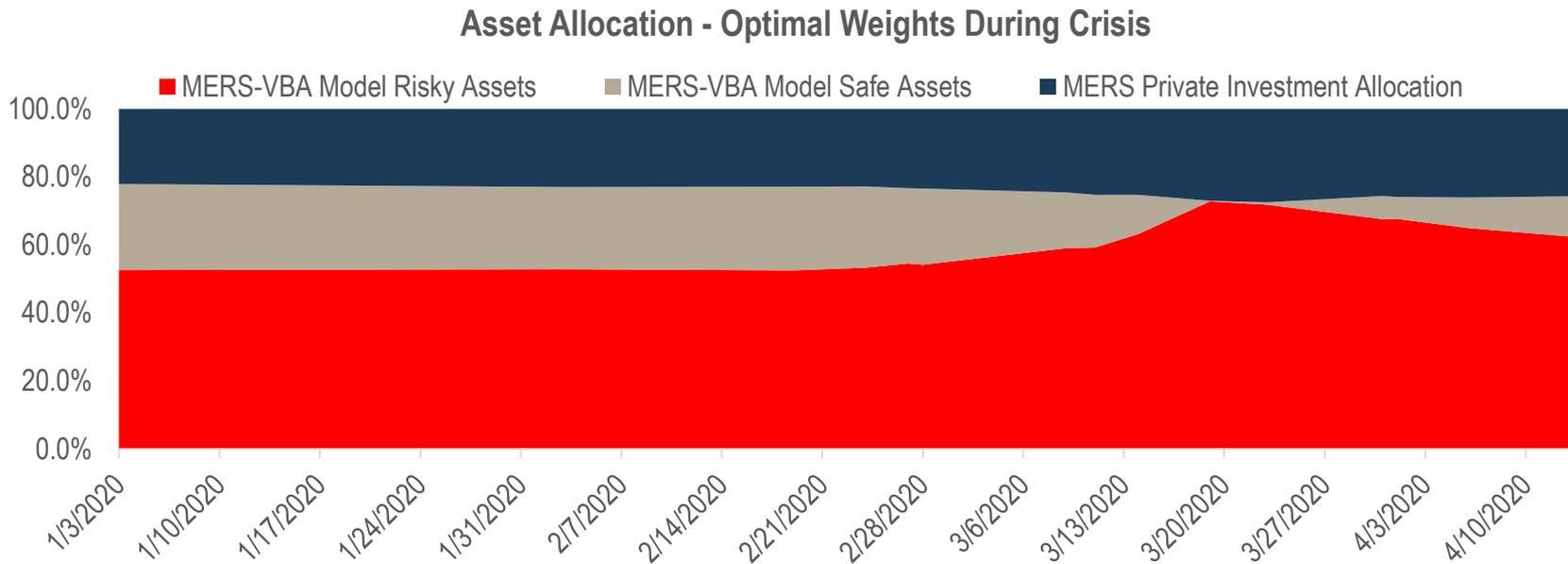
# Liquidity Management

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- **Pay monthly pension obligations**
  - Monthly pension obligation shortfall analysis
    - Roughly \$25M but assumed to be \$40M
  - Segregated cash (\$300M)
  - Aggressively raised cash from internal fixed income portfolios
- **Contractual private market capital calls**
  - Private markets team conducted an analysis to forecast capital calls/distributions for 2020
  - Roughly \$200M in estimated net contributions
- **Adequate liquidity to rebalance the portfolio**
  - Efficient and liquid instruments – ETFs
  - Best use of available liquidity
  - Portfolio stress tests (OMEGA)

# Crisis Rebalancing

- Attractiveness of higher risk assets increased dramatically during crisis
  - Valuations on equities, EM debt and credit (HY and IG) cheapened substantially
  - Asset allocation model required “safe” assets (cash and U.S. Treasuries) to be sold to fund increased allocation to risky assets



# Performance Summary

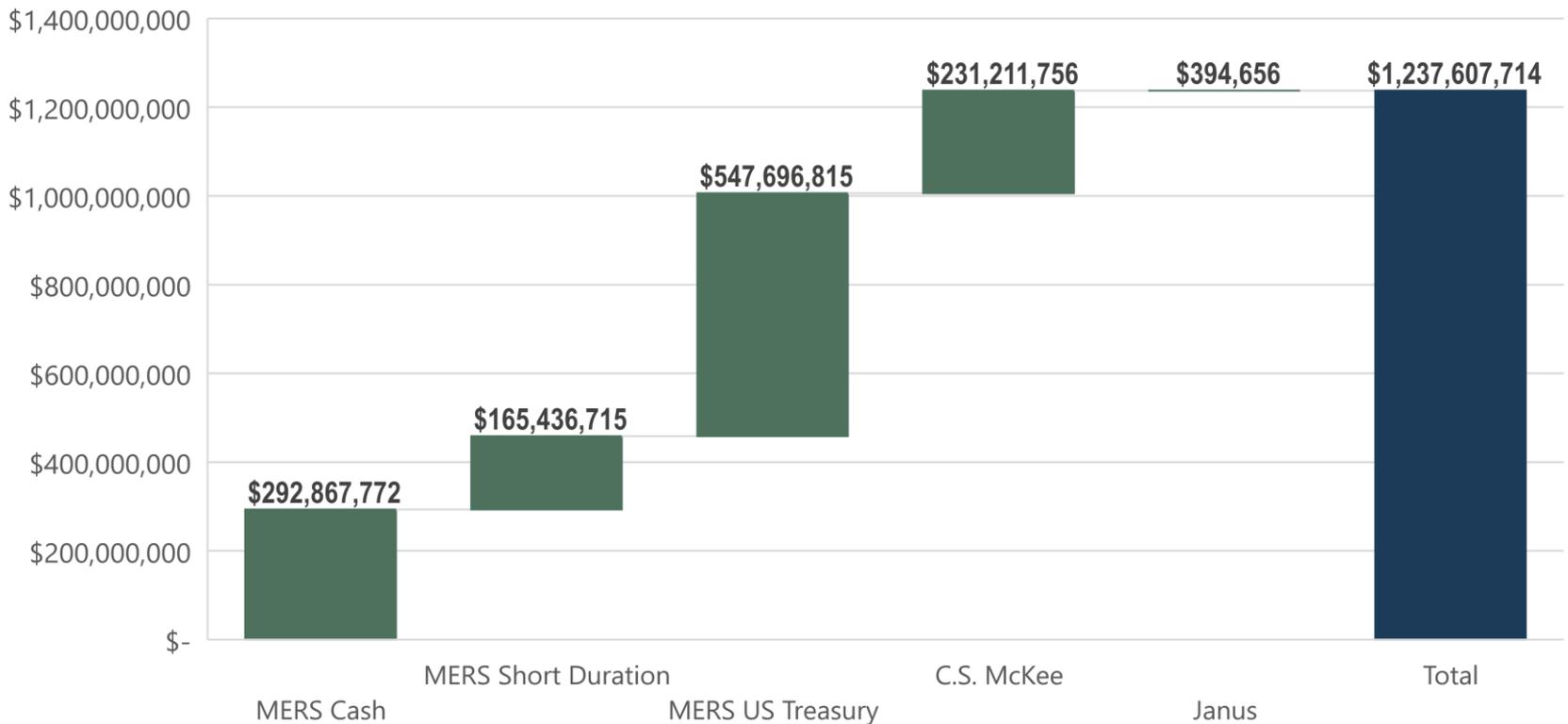
	January	February	March	Q1
MERS' Portfolio (net)	-0.76%	-3.96%	-8.17%	-12.47%
Policy Benchmark	-0.04%	-4.87%	-9.68%	-14.11%
Excess	-0.72%	0.91%	1.51%	1.64%

- From peak to trough (February 19 to March 23) the portfolio outperformed the benchmark by over 500 bps
- The portfolio returned 14.14% in 2019 and is outperforming the benchmark for both the seven and ten-year time periods

# Current Liquidity

- MERS still has over \$1B (12% of fund) in liquidity available for rebalancing and pension payments

MERS Liquidity Waterfall as of May 12, 2020



# Portfolio Diversification

Table of Investment Returns Including MERS Defined Benefit with Asset Classes (2000-2019)

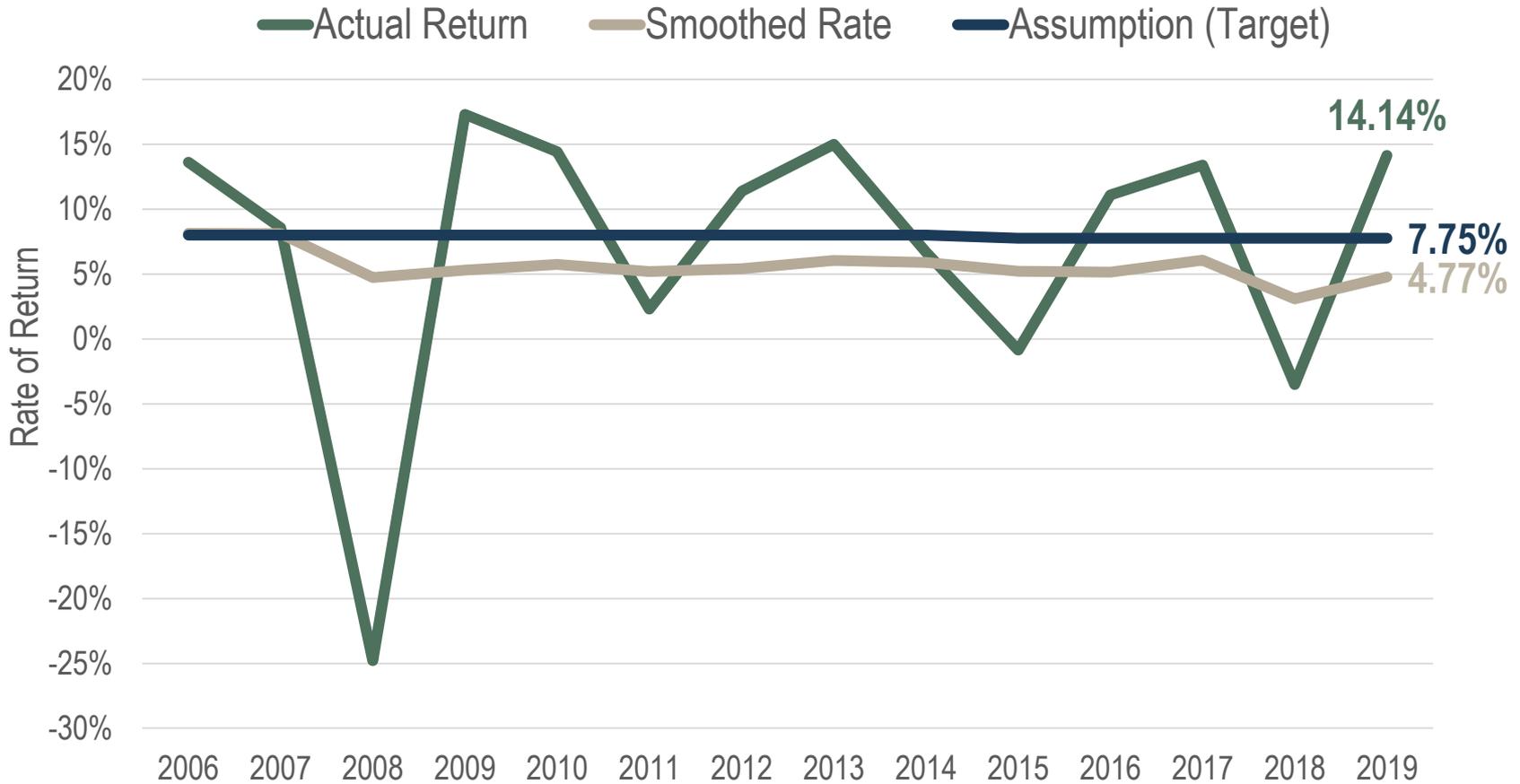
2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Real Estate 13.84%	U.S. Fixed Income 8.43%	Gbl ex-U.S. Fixed 22.37%	Emerging Market Equity 55.82%	Real Estate 37.96%	Emerging Market Equity 34.00%	Real Estate 42.12%	Emerging Market Equity 39.38%	U.S. Fixed Income 5.24%	Emerging Market Equity 78.51%	Small Cap Equity 26.85%	U.S. Fixed Income 7.84%	Real Estate 27.73%	Small Cap Equity 38.82%	Real Estate 15.02%	Large Cap Equity 1.38%	Small Cap Equity 21.31%	Emerging Market Equity 37.28%	Cash Equivalent 1.87%	Large Cap Equity 31.49%
U.S. Fixed Income 11.63%	High Yield 5.28%	U.S. Fixed Income 10.26%	Small Cap Equity 47.25%	Emerging Market Equity 25.55%	Real Estate 15.35%	Emerging Market Equity 32.17%	Dev ex-U.S. Equity 12.44%	Gbl ex-U.S. Fixed 4.39%	High Yield 58.21%	Real Estate 19.63%	High Yield 4.98%	Emerging Market Equity 18.23%	Large Cap Equity 32.39%	Large Cap Equity 13.69%	U.S. Fixed Income 0.55%	High Yield 17.13%	Dev ex-U.S. Equity 24.21%	U.S. Fixed Income 0.01%	Small Cap Equity 25.52%
Cash Equivalent 6.18%	Cash Equivalent 4.42%	Real Estate 2.82%	Real Estate 40.69%	Dev ex-U.S. Equity 20.38%	Dev ex-U.S. Equity 14.47%	Dev ex-U.S. Equity 25.71%	Gbl ex-U.S. Fixed 11.03%	Cash Equivalent 2.06%	Real Estate 37.13%	Emerging Market Equity 18.88%	Gbl ex-U.S. Fixed 4.36%	Dev ex-U.S. Equity 16.41%	Dev ex-U.S. Equity 21.02%	MERS Defined Benefit 6.68%	Cash Equivalent 0.05%	Large Cap Equity 11.96%	Large Cap Equity 21.83%	High Yield -2.08%	Dev ex-U.S. Equity 22.49%
MERS Defined Benefit -2.76%	Small Cap Equity 2.49%	Cash Equivalent 1.78%	Dev ex-U.S. Equity 39.42%	Small Cap Equity 18.33%	MERS Defined Benefit 6.78%	Small Cap Equity 18.37%	MERS Defined Benefit 8.56%	MERS Defined Benefit -24.79%	Dev ex-U.S. Equity 33.67%	High Yield 15.12%	MERS Defined Benefit 2.30%	Small Cap Equity 16.35%	MERS Defined Benefit 15.00%	U.S. Fixed Income 5.97%	Real Estate -0.79%	Emerging Market Equity 11.19%	Small Cap Equity 14.65%	Gbl ex-U.S. Fixed -2.15%	Real Estate 21.91%
Small Cap Equity -3.02%	MERS Defined Benefit -1.01%	High Yield -1.37%	High Yield 28.97%	MERS Defined Benefit 14.90%	Large Cap Equity 4.91%	Large Cap Equity 15.73%	U.S. Fixed Income 6.97%	High Yield -26.16%	Small Cap Equity 27.17%	Large Cap Equity 15.06%	Large Cap Equity 2.11%	Large Cap Equity 16.00%	High Yield 7.44%	Small Cap Equity 4.89%	MERS Defined Benefit -0.85%	MERS Defined Benefit 11.10%	MERS Defined Benefit 13.40%	MERS Defined Benefit -3.51%	Emerging Market Equity 18.44%
Gbl ex-U.S. Fixed -3.91%	Emerging Market Equity -2.61%	Emerging Market Equity -6.16%	Large Cap Equity 28.68%	Gbl ex-U.S. Fixed 12.54%	Small Cap Equity 4.55%	MERS Defined Benefit 13.61%	Large Cap Equity 5.49%	Small Cap Equity -33.79%	Large Cap Equity 26.47%	MERS Defined Benefit 14.43%	Cash Equivalent 0.10%	High Yield 15.81%	Real Estate 3.67%	High Yield 2.45%	Dev ex-U.S. Equity -3.04%	Real Estate 4.06%	Gbl ex-U.S. Fixed 10.51%	Large Cap Equity -4.38%	High Yield 14.32%
High Yield -5.86%	Gbl ex-U.S. Fixed -3.75%	MERS Defined Benefit -8.34%	MERS Defined Benefit 24.72%	High Yield 11.13%	Cash Equivalent 3.07%	High Yield 11.85%	Cash Equivalent 5.00%	Large Cap Equity -37.00%	MERS Defined Benefit 17.31%	Dev ex-U.S. Equity 8.95%	Small Cap Equity -4.18%	MERS Defined Benefit 11.39%	Cash Equivalent 0.07%	Cash Equivalent 0.03%	Small Cap Equity -4.41%	Dev ex-U.S. Equity 2.75%	Real Estate 10.36%	Real Estate -5.63%	MERS Defined Benefit 14.14%
Large Cap Equity -9.11%	Real Estate -3.81%	Dev ex-U.S. Equity -15.80%	Gbl ex-U.S. Fixed 19.36%	Large Cap Equity 10.88%	High Yield 2.74%	Gbl ex-U.S. Fixed 8.16%	High Yield 1.87%	Dev ex-U.S. Equity -43.56%	Gbl ex-U.S. Fixed 7.53%	U.S. Fixed Income 6.54%	Real Estate -6.46%	U.S. Fixed Income 4.21%	U.S. Fixed Income -2.02%	Emerging Market Equity -2.19%	High Yield -4.47%	U.S. Fixed Income 2.65%	High Yield 7.50%	Small Cap Equity -11.01%	U.S. Fixed Income 8.72%
Dev ex-U.S. Equity -13.37%	Large Cap Equity -11.89%	Small Cap Equity -20.48%	U.S. Fixed Income 4.10%	U.S. Fixed Income 4.34%	U.S. Fixed Income 2.43%	Cash Equivalent 4.85%	Small Cap Equity -1.57%	Real Estate -48.21%	U.S. Fixed Income 5.93%	Gbl ex-U.S. Fixed 4.95%	Dev ex-U.S. Equity -12.21%	Gbl ex-U.S. Fixed 4.09%	Emerging Market Equity -2.60%	Gbl ex-U.S. Fixed -3.09%	Gbl ex-U.S. Fixed -6.02%	Gbl ex-U.S. Fixed 1.49%	U.S. Fixed Income 3.54%	Dev ex-U.S. Equity -14.09%	Gbl ex-U.S. Fixed 5.09%
	Dev ex-U.S. Equity -21.40%	Large Cap Equity -22.10%	Cash Equivalent 1.15%	Cash Equivalent 1.33%	Gbl ex-U.S. Fixed -8.65%	U.S. Fixed Income 4.33%	Real Estate -7.33%	Emerging Market Equity -53.33%	Cash Equivalent 0.21%	Cash Equivalent 0.13%	Emerging Market Equity -18.42%	Cash Equivalent 0.11%	Gbl ex-U.S. Fixed -3.08%	Dev ex-U.S. Equity -4.32%	Emerging Market Equity -14.92%	Cash Equivalent 0.33%	Cash Equivalent 0.86%	Emerging Market Equity -14.57%	Cash Equivalent 2.28%

# Market Rebounds



# Effect of Smoothing

*Smoothing is a buffer against extreme fluctuations in the market*



*\*Investment rate of return is gross of fees*

# Conclusion

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- MERS carefully balances risk and liquidity to **ensure that monthly pension obligations are paid**
- MERS had prepared for market volatility and thus **outperformed our market benchmarks**
- Our governance model allows MERS to **respond to market changes quickly within a prudent structure**



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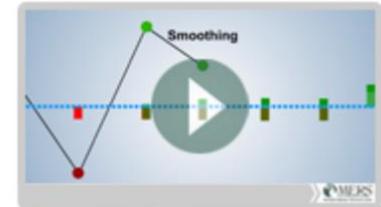


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# Employer Resources

- Asset smoothing helps avoid dramatic spikes and dips in annual contribution requirements due to short term fluctuations in asset markets
- MERS is here to partner with you to help you proactively explore plan design and funding options
- Other resources
  - 2019 Annual Actuarial Valuations will be available mid-year
  - Employer COVID-19 Updates on [mersofmich.com](https://mersofmich.com)
- Employers with questions about the impact of volatility on plan costs should contact their Regional Manager

## How Smoothing Works



*Smoothing video available  
on [mersofmich.com](https://mersofmich.com)*

# Contacting MERS of Michigan

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