San Jose Federated City Employees' Retirement System

Private Markets Pacing Plan

Fiscal Year 2023-24

as of April 2023

Purpose

- Seek approval of target commitment amounts (the "pacing plan") for each private markets asset class in the next fiscal year as required by the IPS.
- The pacing plan uses assumptions on future cash flows and NAVs to estimate commitment amounts to reach and maintain target allocations.
- At the April 2023 meeting, the Investment Committee ("IC") recommended four asset allocation mixes to bring forward to the May 2023 Board meeting. The IC also approved bringing this pacing plan recommendation forward to the Board with output for all private markets targets being considered including both 3% and 4% Venture Capital target allocations.

Valuable context:

- Execution of FY 2022-23 pacing plan and current allocations.
- Impact of changes in financial markets and asset allocation on the plans' long-term private markets program.
- Pacing plan modeling completed by Neuberger Berman (buyout) and Meketa Investment Group (other private asset classes).
- Projections for 10 years shown, but the pacing plan is revisited and approved on an annual basis.

Year in review

FY 2022-23 pacing plan execution

- Staff expects to complete 15 commitments for $133mm of $149mm pacing plan (89%).
- Two-thirds of commitments with existing fund manager relationships.

Current positioning versus target

- Private markets are currently 22.9% of plan assets, 1.9% above the 21% target.
- Denominator effect, acceleration of capital calls, and slowdown of realizations brought the allocation 4% higher than anticipated in the previous pacing plan.

Changes in asset allocation

- The Board is evaluating mixes with a 20% or 21% private markets target.
- Target was 25% in 2018-2019.

Changes in market environment

- Inflation, rising interest rates, geopolitical risk, and banking crisis.
- Valuations have moderated, but remain elevated.
- Capital is no longer a commodity.

FY 2022-23 Pacing Plan Execution

	Style	Date	Executed	Target	
Buyout			**$ 25mm**	**/ $ 25mm**	**100%**
PE Strategic Partnership SJFED	Fund-of-one	7/1/2022	$ 25mm		
Venture Capital			**$ 18mm**	**/ $ 30mm**	**60%**
Transpose Platform SJFED	Fund-of-one	7/1/2022	$ 13mm*		
Crosslink Ventures X	Early stage	1/27/2023	$ 3.5mm		
Expected before 6/30/2023	-	-	*$ 1.5mm*		
Private Debt			**$ 28mm**	**/ $ 30mm**	**93%**
Eagle Point Defensive Income Fund II	Par Credit	8/26/2022	$ 10mm		
HPS Special Situations Opportunity Fund II	Stress	9/7/2022	$ 10mm		
Expected before 6/30/2023	-	-	*$8mm*		
Growth Real Estate			**$ 27mm**	**/ $ 32mm**	**84%**
EQT Exeter Industrial Value Fund VI	Value Added	7/29/2022	$ 8mm		
GCP SecureSpace Property Partners	Value Added	7/29/2022	$ 6mm		
DRA Growth & Income Fund XI	Value Added	11/1/2022	$ 13mm		
Private Real Assets			**$ 35mm**	**/ $ 32mm**	**109%**
Kimmeridge Fund VI	Energy	9/30/2022	$ 9mm		
H.I.G. Infrastructure Partners	Infrastructure	12/22/2022	$ 11mm		
Lime Rock Partners IX	Energy	2/14/2023	$ 5mm		
Paine Schwartz Food Chain Fund VI	Agriculture	3/15/2023	$ 5mm		
Expected before 6/30/2023	-	-	*$ 5mm*		
Total Private Markets			**$ 133mm**	**/ $ 149mm**	**89%**

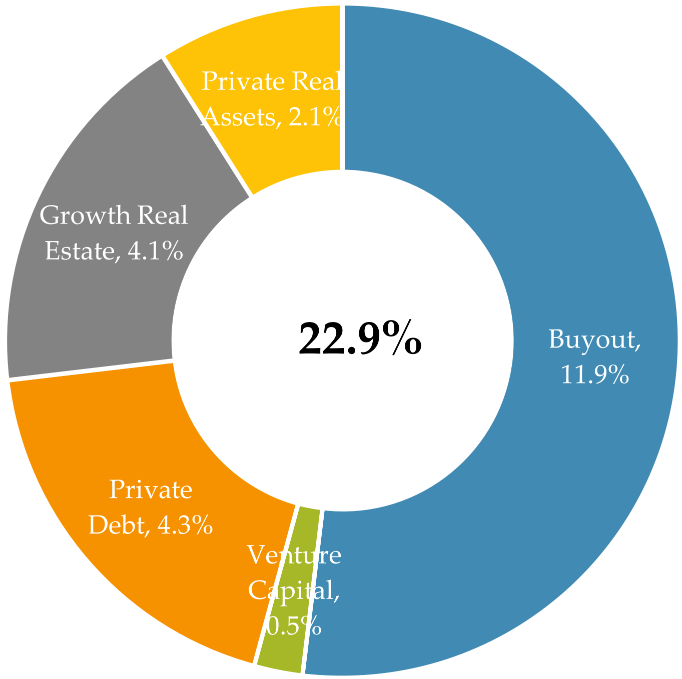
* Expected amount committed to underlying investments during fiscal year 2022-23 out of $30mm commitment.

Private Markets Allocation Snapshot

- The Private Markets allocation is 1.9% above target.
- Venture Capital is the newest private markets asset class and currently 3.5% below target.

	% of Plan	Target	Difference
Buyout	11.9%	8%	3.9%
Venture Capital	0.5%	4%	-3.5%
Private Debt	4.3%	3%	1.3%
Growth Real Estate	4.1%	3%	1.1%
Private Real Assets	2.1%	3%	-0.9%
Total Private Markets	**22.9%**	**21%**	**1.9%**

Pro Forma as of April 7, 2023



Current positioning versus target slightly ahead of plan

- The Private Markets allocation is 4% higher than expected in the prior year pacing plan.
    - Due to a combination of denominator effect, acceleration of capital calls, and slowdown of realizations.

	Expected 6/30/23 % of plan			**Expected 6/30/23 NAV ($mm)**		
	FY 22-23 Pacing	Current Estimates	Forecast Error	FY 22-23 Pacing	Current Estimates	Forecast Error
Buyout	10%	11%	+1%	321	324	+3
Venture Capital	1%	1%	+0%	23	27	+4
Private Debt	3%	4%	+1%	86	120	+34
Growth Real Estate	3%	4%	+1%	88	103	+15
Private Real Assets	2%	2%	+0%	52	60	+8
Total Private Markets	**18%**	**22%**	**+4%**	**570**	**634**	**+65**

Plan-level net asset value forecasts

- Compared to last years pacing plan, the current NAV forecast is:
  - Lower in FY 2023-27 due to a decline in plan assets.
  - Higher in FY 2028-32 due to increased return expectations and updated actuarial data.

	6/30/2023	6/30/2024	6/30/2025	6/30/2026	6/30/2027
Current NAV forecast ($mm)	**2,894**	**3,107**	**3,330**	**3,565**	**3,811**
Prior Year NAV forecast ($mm)	*3,111*	*3,303*	*3,495*	*3,687*	*3,878*
Difference	*-7%*	*-6%*	*-5%*	*-3%*	*-2%*

	6/30/2028	6/30/2029	6/30/2030	6/30/2031	6/30/2032
Current NAV forecast ($mm)	**4,079**	**4,361**	**4,661**	**4,980**	**5,312**
Prior Year NAV forecast ($mm)	*4,077*	*4,284*	*4,499*	*4,723*	*4,951*
Difference	*0%*	*2%*	*4%*	*5%*	*7%*

Pacing Plan Output (3% VC target)

- Below are the target commitment amounts from pacing plan modeling completed by Neuberger Berman (buyout) and Meketa Investment Group (other private asset classes).
- For FY 23-24 compared to the FY 22-23 pacing plan: Venture Capital will be $10mm lower, Private Debt $10mm lower, and Private Real Assets $7mm lower.
- Staff recommends approval of the highlighted commitment amounts for FY 2023-24 if the Board approves an asset allocation with 3% venture capital target.

	FY 22-23		Pacing Plan				
	Pacing Plan	Actual	FY 23-24	FY 24-25	FY 25-26	FY 26-27	FY 27-28
Buyout	25	25	25	25	100	100	100
Venture Capital	30	18	20	20	18	18	16
Private Debt	30	28	20	20	20	24	24
Growth Real Estate	32	27	32	32	36	36	36
Private Real Assets	32	35	25	25	25	25	25
Total Private Markets	**149**	**133**	**122**	**122**	**199**	**203**	**201**

Values in $ millions

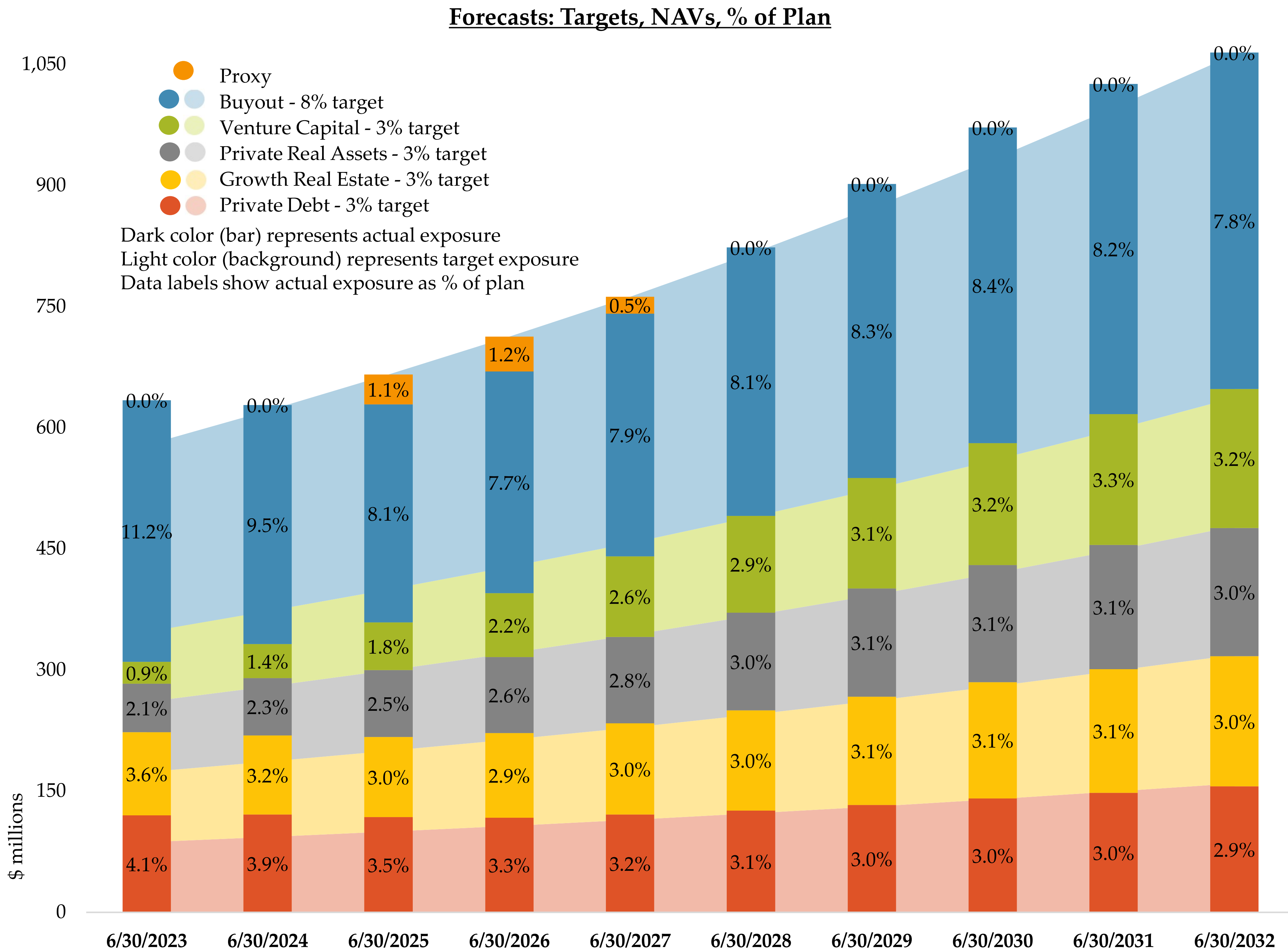
Pacing Plan Output (4% VC target)

- Below are the target commitment amounts from pacing plan modeling completed by Neuberger Berman (buyout) and Meketa Investment Group (other private asset classes).
- For FY 23-24 compared to the FY 22-23 pacing plan: Venture Capital will be $2mm lower, Private Debt $10mm lower, and Private Real Assets $7mm lower.
- Staff recommends approval of the highlighted commitment amounts for FY 2023-24 if the Board approves an asset allocation with 4% venture capital target.

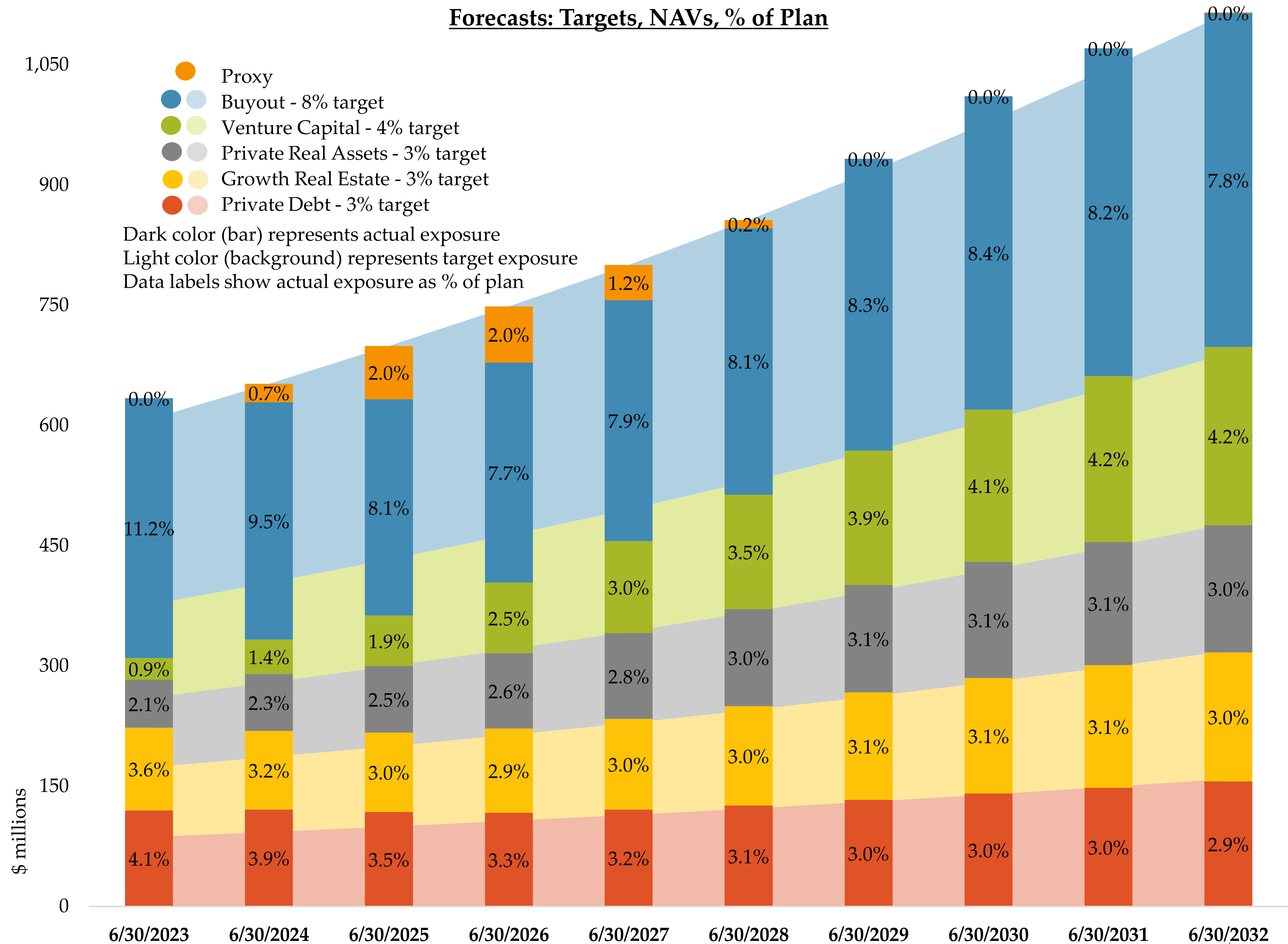
	FY 22-23		Pacing Plan				
	Pacing Plan	Actual	FY 23-24	FY 24-25	FY 25-26	FY 26-27	FY 27-28
Buyout	25	25	25	25	100	100	100
Venture Capital	30	18	28	28	24	24	24
Private Debt	30	28	20	20	20	24	24
Growth Real Estate	32	27	32	32	36	36	36
Private Real Assets	32	35	25	25	25	25	25
Total Private Markets	**149**	**133**	**130**	**130**	**205**	**209**	**209**

Values in $ millions

Forecast private markets net asset values (3% VC target)



Forecast private markets net asset values (4% VC target)

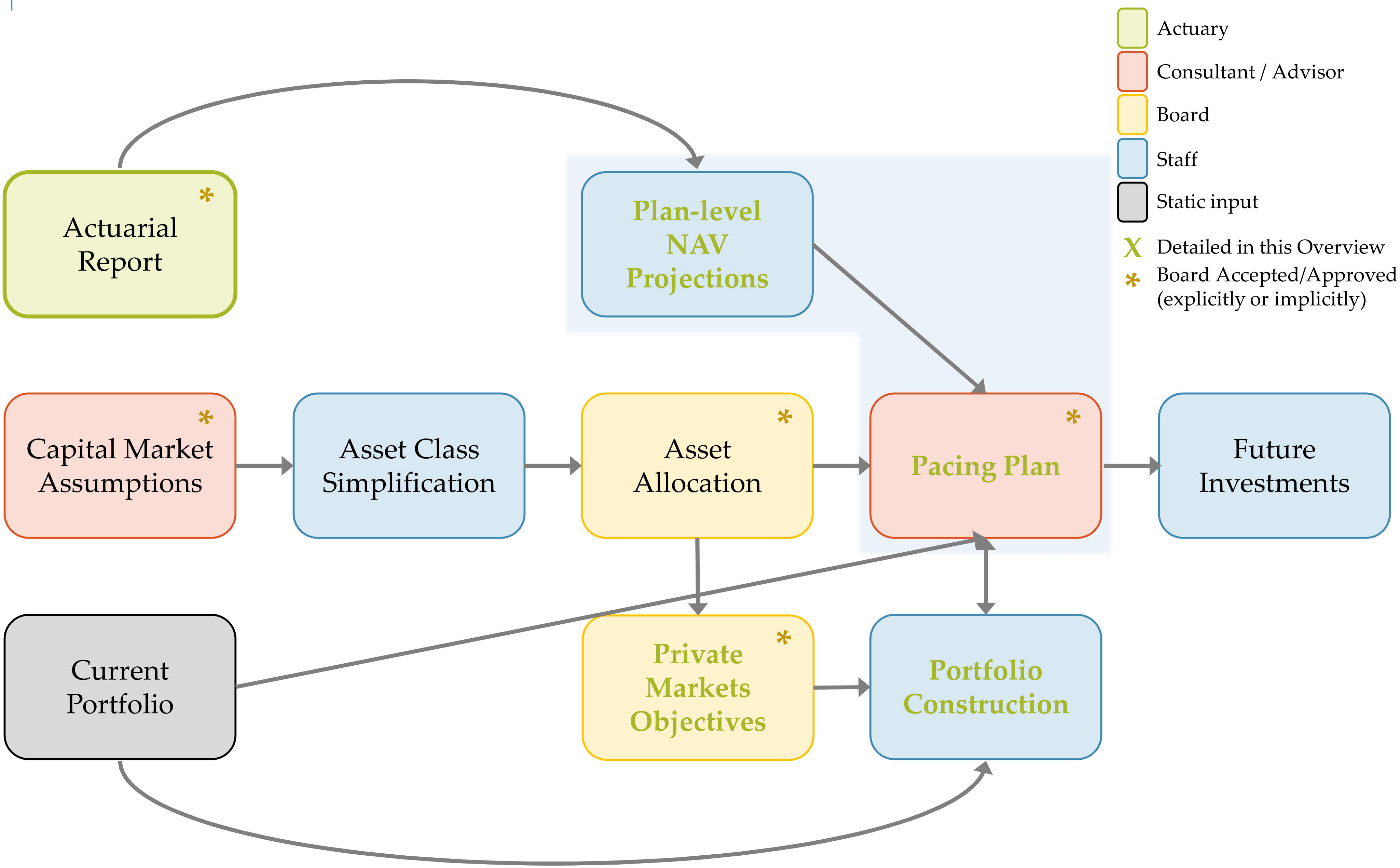


Appendix

Pacing plan basics

- The pacing plan models how the pension plan will reach and maintain target allocation to private markets strategies.
- The key output is a target level of annual commitments to funds in each private market asset class.
- Many assumptions are incorporated into the pacing plan models. Because of the assumptions' high variance (actual vs. forecast), the pacing plan is revisited annually.
- Staff produces plan-level NAV targets for each private markets asset class, which are then provided to Neuberger Berman and Meketa Investment Group for detailed modeling on Buyout, Venture Capital, Private Debt, Growth Real Estate, and Private Real Assets.
- Staff aggregates the output into a single pacing plan document to allow stakeholders to view the private markets program holistically.
- For Buyout, Private Debt, Growth Real Estate, and Private Real Assets, the Boards' approvals of their respective pacing plans sets the guideline for the constraints outlined in the IPS around delegation of manager selection to staff.
- For Venture Capital, individual investments are approved by the Investment Committee and Board.
- When actual private markets exposure is below target, a public markets proxy is used to rebalance to target.

Private markets process / data flow



Investment projection methodology

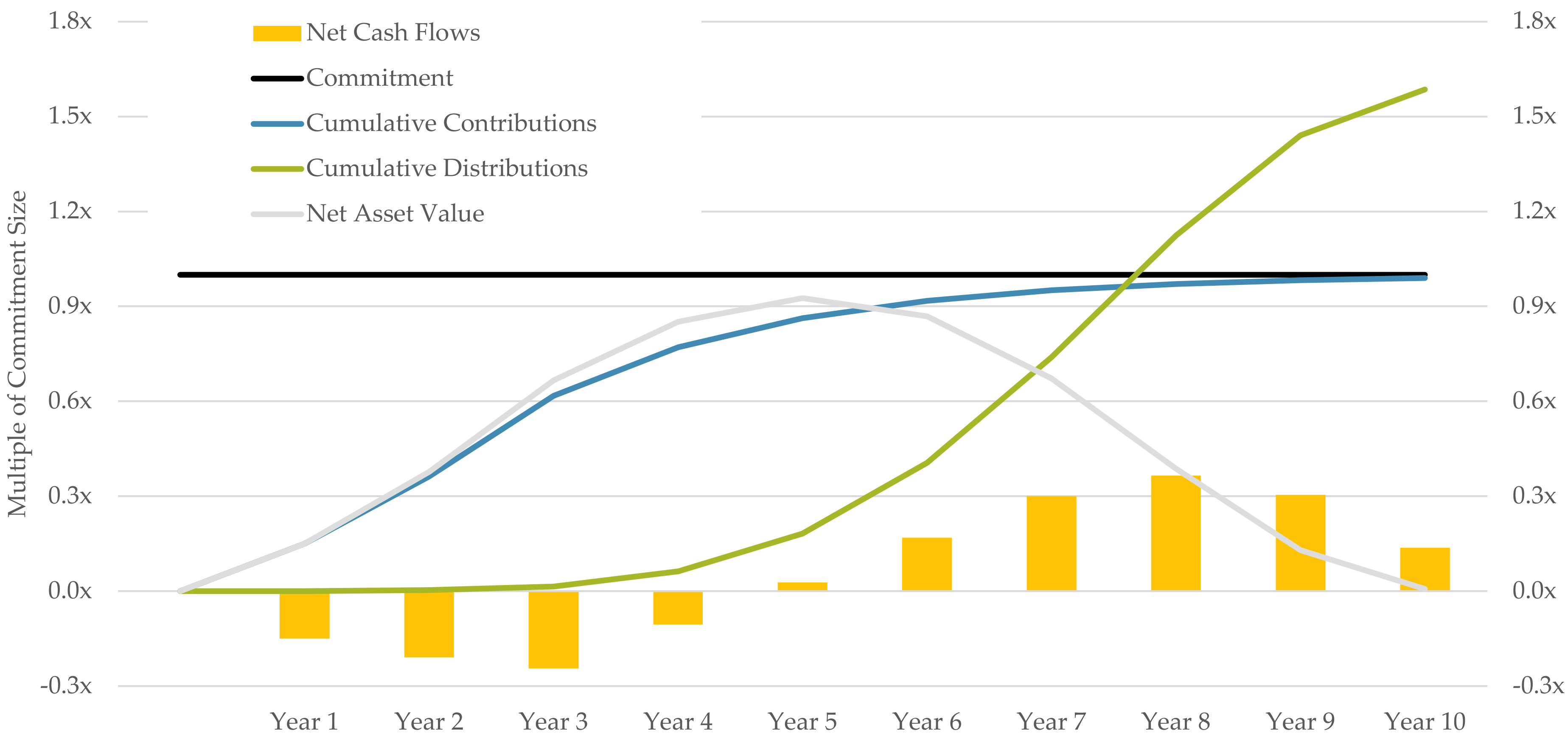
Meketa produced an easy-to-read white paper on commitment pacing that outlines their specific methodology (PDF link).

An example to demonstrate the assumptions and output for a sample investment is shown below using the Takashi-Alexander framework, which is the basis for the Meketa model.

Inputs

Fund type:	Large buyout	**Projected net return:**	12% IRR / 1.6x TVPI
Contribution rates, Year 1 / 2 / 3+:	15% / 25% / 40%	**Projected yield:**	2%
Fund term:	10 years	**Bow factor:**	3.0

Output



Investment Policy Statement

Basis*	Description	Strategy Limit[1]
Vehicle	Separately managed accounts (active)	15%
	Commingled funds and SMAs (public, passive)	No limit[2]
	Commingled funds (public, active)	15%
	Commingled funds (hedge funds)	15%
	Commingled funds (private strategies)	15%[3]
Public Markets[4]	Passive strategies	No limit
	Active strategies	15%
Private Markets		**Transaction Limit[5]**
	Total $ commitment to asset class (e.g. Private Debt)	150% of Board-approved pacing plan (cumulative)[6]
	Primary fund commitment (1st allocation to mgr.)	2%**
	Primary fund commitment (follow-on)	3%**
	Secondary fund investment	1%**

* To be selected, the manager must satisfy the "Vehicle" constraint and the appropriate "Public Markets" or "Private Markets" constraints

** Percentage (%) of total System assets

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1 Percentage (%) of total System assets allowable per investment strategy.
2 Rationale: Fund is constrained by the asset allocation. This is the "default" option for investing, and scale determines pricing.
3 For private strategies, limit applies to the capital invested plus future callable commitments.
4 Some of these limits related to public markets may be "interim", to be replaced by risk-based limits for example.
5 Percentage (%) of total System assets allowable per investment manager.
6 This would allow, for example, a commitment in Year 1 that is 50% above "plan". The "cumulative" provision would allow for a "catch-up" for any slower-than-planned investments in prior years.

Private Markets Asset Classes

Buyout		• Large Buyout • Small-/Mid- Buyout • Special Situations • Other	Equity investments in growing, established, and mature companies, with enterprise values generally ranging from $20mm to $20bn.
Venture		• Fund-of-funds • Direct funds • Co-investments	Primarily equity investments in start-ups and high growth companies.
Debt		• Par Credit • Securitized • Stress/Distress • Other	Debt investments include credit expected to pay back original principal and interest (par credit), loans and bonds that have been packaged into special purpose vehicles (securitized), securities where the obligor is in a stressed or distressed financial situation (stress/distress), and unique strategies that have some or all the characteristics of debt investments.
Real Estate		• Value-Added • Opportunistic • Real Estate Debt • Other	Equity and debt investments in operating companies and physical properties where the economic value is derived primarily through real estate-related activities. Value-added and opportunistic are distinguished by the level of risk associated with an investment.
Real Assets		• Infrastructure • Energy • Natural Resources • Other	Investments in operating companies and physical assets where the economic value is derived primarily from the development, production, transport, or processing of natural resources, and the facilities supporting their downstream progress.