Callan

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Mendocino County Employees' Retirement Association

MCERA Board Education

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MCERA Board Education Calendar

FY 2026 – 2027

✓ June
Asset Allocation by Function

July
Closed End and Direct Investing Considerations

August
Quarterly Investment Update

September
Liquidity Management & Active Risk Budgeting

October
Risk Mitigation & Private Equity Education

November
Actuarial Valuation Presentation

Quarterly Investment Update

December
Private Credit Education

January
Capital Market Expectations

California Retirement System Investment Experience Review

February
Investment Philosophy Review

Quarterly Investment Update

March
Asset Liability Study

April
Mid Cap Value Strategy Update

Performance Measurement Framework

May
Investment Policy Statement Update

Quarterly Investment Update

Closed End and Direct Investing Considerations:
Private Equity and Private Credit

Why Private Equity and Private Credit

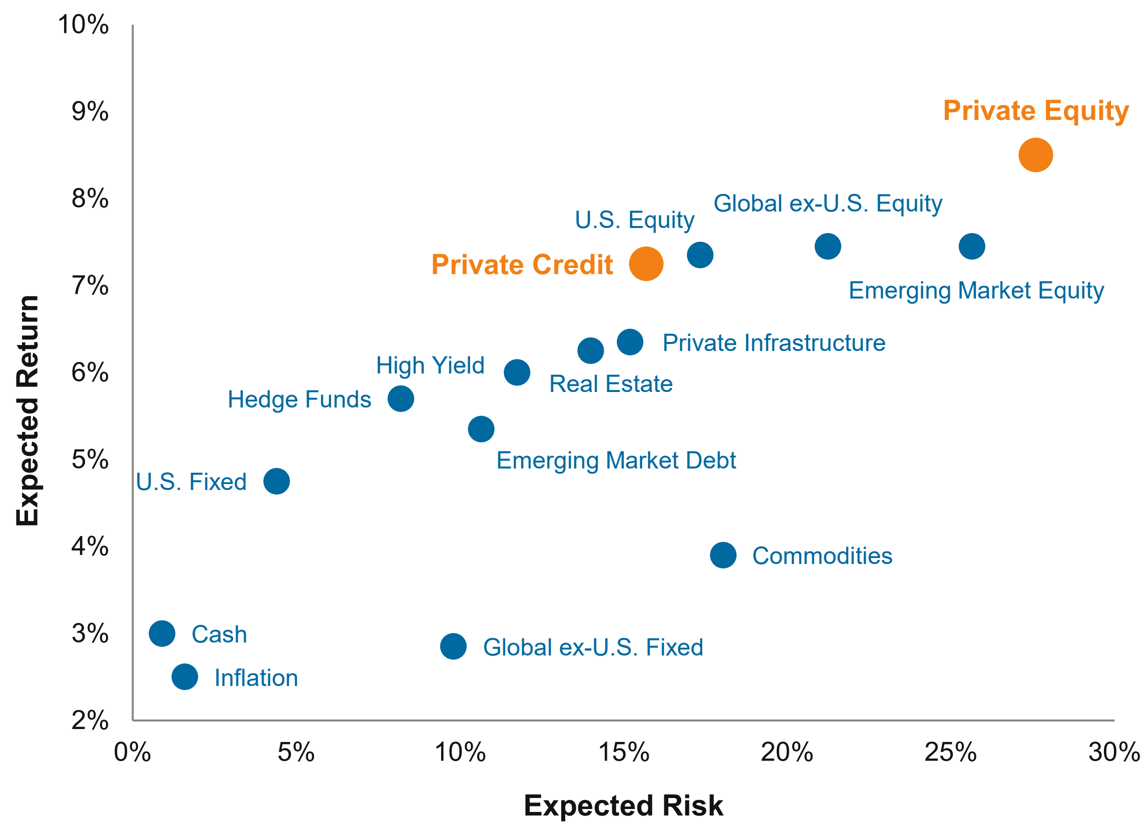
Definition: Private, unlisted investments in the equity or debt of companies, typically accessed through limited partnerships

- Provides a differentiated return stream and diversification in a portfolio with publicly securities
- Addresses a different opportunity set — private companies
- Primary appeal: potential to outperform publicly traded stocks and bonds
- Primary drawbacks: illiquidity, program complexity, high return dispersion

Capital Markets Assumptions:

– Private equity is *(conservatively)* expected to return 115 bps above U.S. Equity

– Private credit is expected to return 125 bps above High Yield at a similar risk level as U.S. Equity



Reflects Callan's 2025 Capital Markets Assumptions

Private Markets Program Development

Four essential building blocks

Program Design

- Governance, staffing, and resources
- Implementation models—buy, build, or both?
- Objectives and risk specifications
- Investment policy statement

Strategic Planning

- Capital budget/commitment pacing
- Strategy selection
- Vehicle structure
- Liquidity management

Monitoring and Evaluation

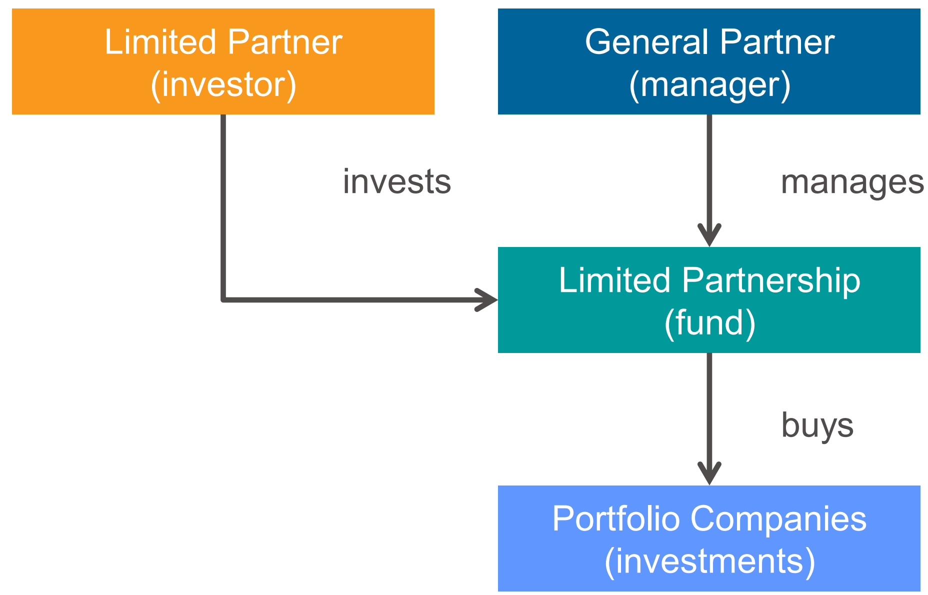
- Qualitative and quantitative monitoring
- Benchmark selection
- Reporting

Manager Selection

- Forward calendar
- Due diligence
- Terms and conditions

How to Invest in Private Equity & Private Credit

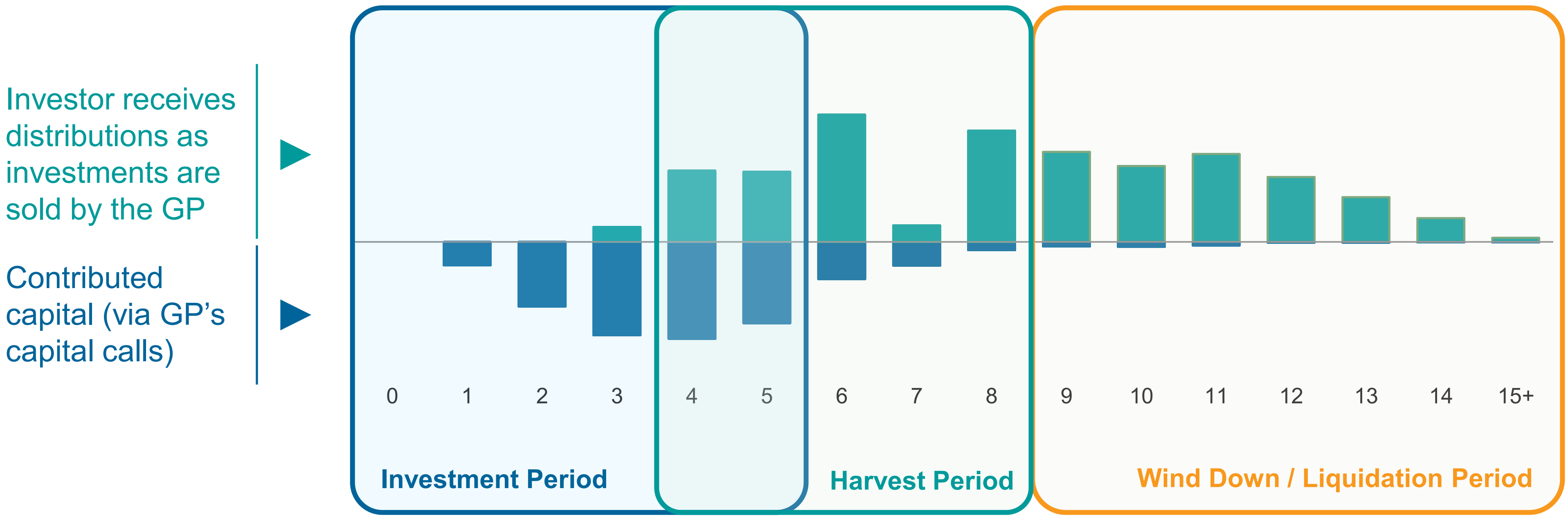
- Private equity and private credit investments are typically accessed through a limited partnership vehicle in which the manager is the general partner (GP) and the investor is the limited partner (LP).
- To provide diversification, asset owners seeking private equity and private credit should invest in a number of limited partnerships in these asset classes.
- **Private equity** can be implemented via direct investments or a fund-of-funds, each of which is “closed-end” in nature.
- **Private credit** can be implemented via an open-end or closed-end structure.



Commitment Pacing

Closed-end fund structure

- Private Markets partnerships typically structured as closed-end investment vehicles
  - Full commitment made at fund closing; legally obligates investor (LP) to fund future capital calls
  - LP receives capital distributions as investments are sold or income collected; PE funds typically do not distribute income during investment period
  - LP cannot exit the fund unless interest is sold or fund is dissolved (extraordinary circumstances)
- Multi-year term (typically 10–15+ years), with investment, harvest, and liquidation periods



Importance of Manager Selection

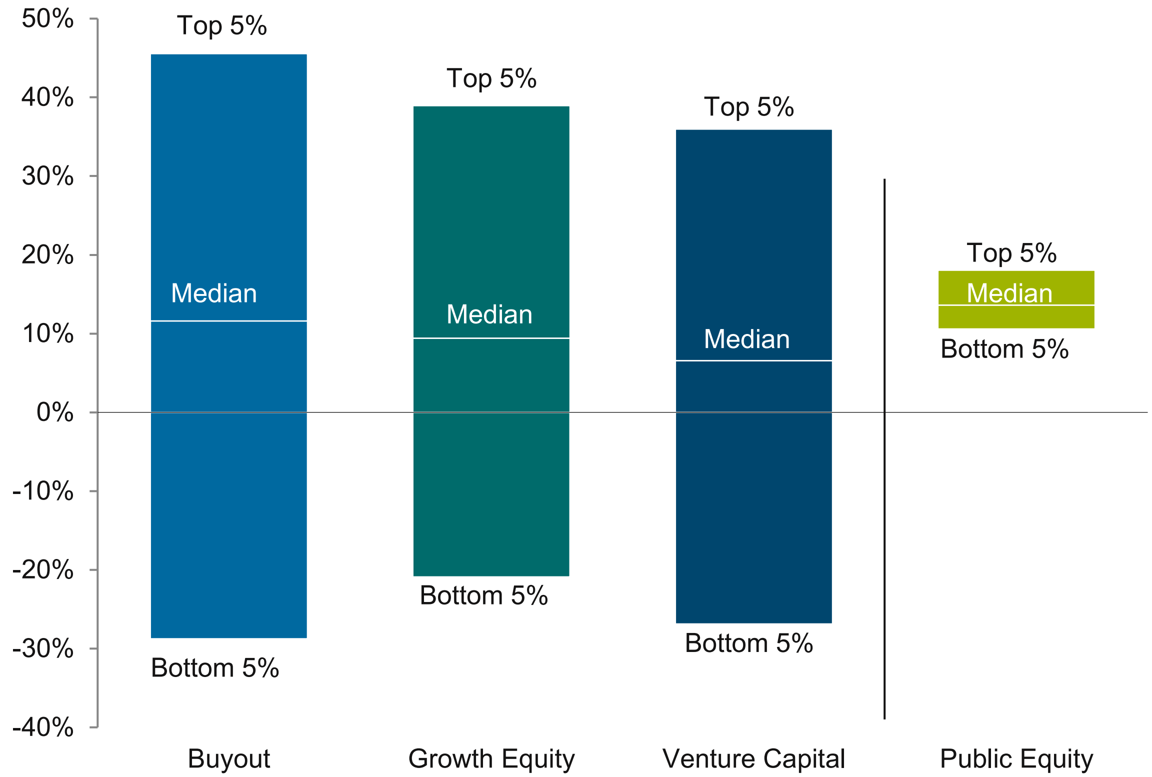
Although aggregate private equity returns have exceeded the public markets, there is a high level of dispersion in individual fund returns.

This dispersion demonstrates the importance of manager selection in the asset class.

67% return dispersion between the top private equity funds and the bottom over the last 10 years

In contrast, the dispersion in public equity returns is only 7%

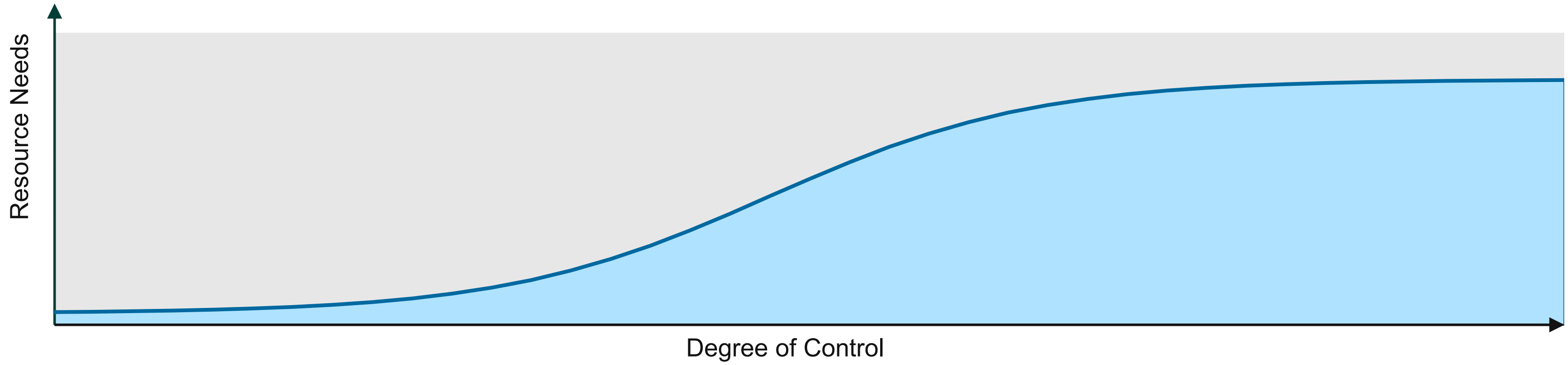
Net IRRs by Strategy Type, Last 10 Years ending 09/30/25



Source: LSEG/Cambridge. Public Equity reflects TWRs of Callan's All Cap Broad Public Equity peer group.

PE Implementation Options

Characteristics of each implementation model

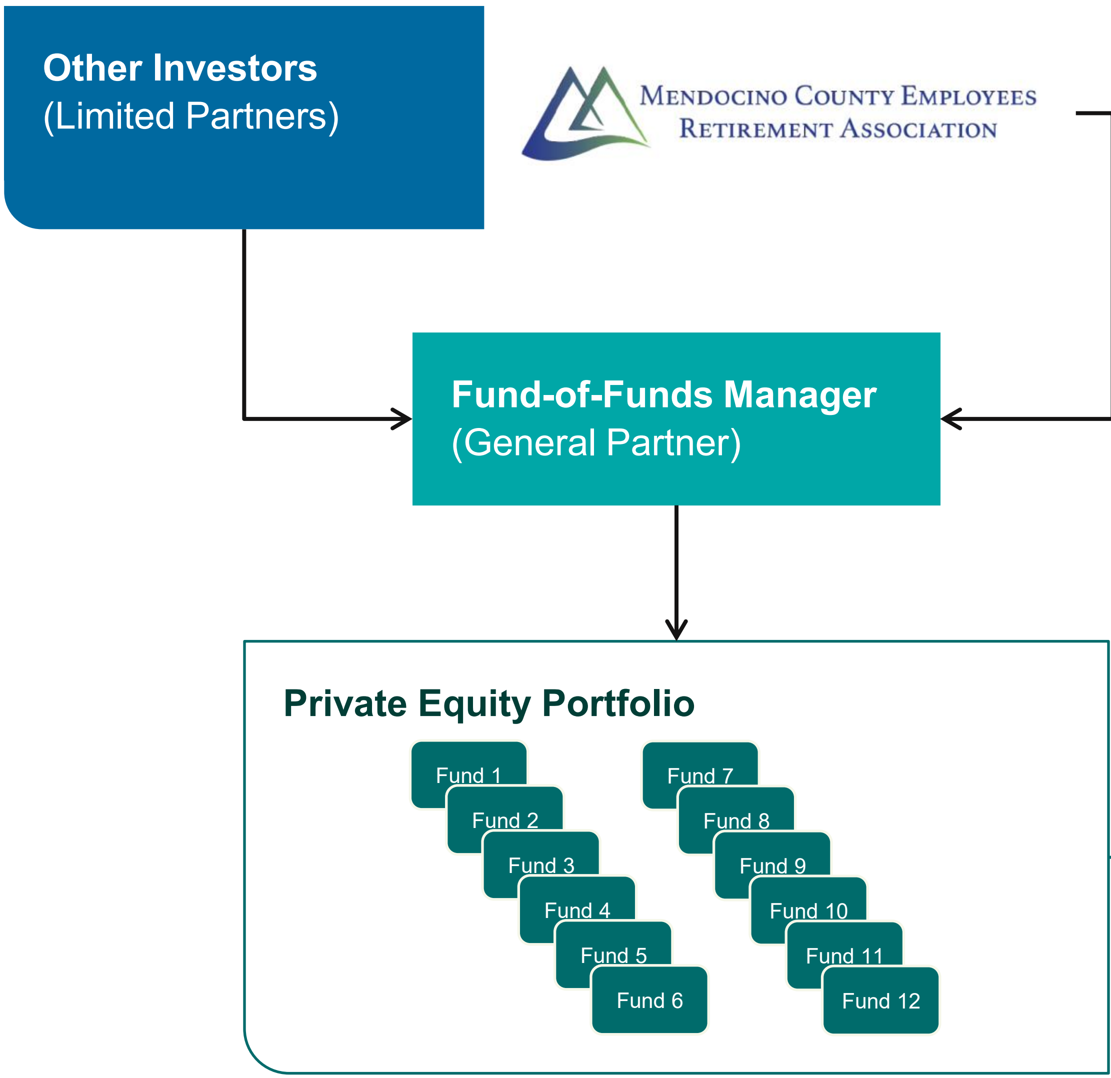


	Fund-of-Funds	Hybrid Program	Direct Program
Implementation Risk »	Lower	Moderate	Higher
Program Complexity »	Lower	Moderate	Custom
Diversification »	High	Moderate	Custom
Total Fee Load »	High estimated 250-400 bps	Moderate ← in between →	Lower estimated 200-250 bps
Net of Fee Returns »	Lower	Lower / Moderate	Higher
Return Dispersion »	Lower	Moderate / Higher	Higher

Typical Commingled FOF Fee = 0.50% to 1.0% (committed) plus 0% to 10% performance fee plus administrative fee

Underlying Fund Level Management Fee = typically 1.5% to 2.5%; Underlying Fund Carried Interest = typically 20%

Investment Structure: Fund-of-Funds (Commingled)



Pros
- All PE functions handled by FOF
- Broad portfolio diversification; one line item
- MCERA can budget annual commitments

Cons
- MCERA has no say over manager selection or portfolio construction
- Same portfolio for all investors
- Additional deployment period
- FOF manager “owns” relationships
- Extra layer of fees

Fund Legal

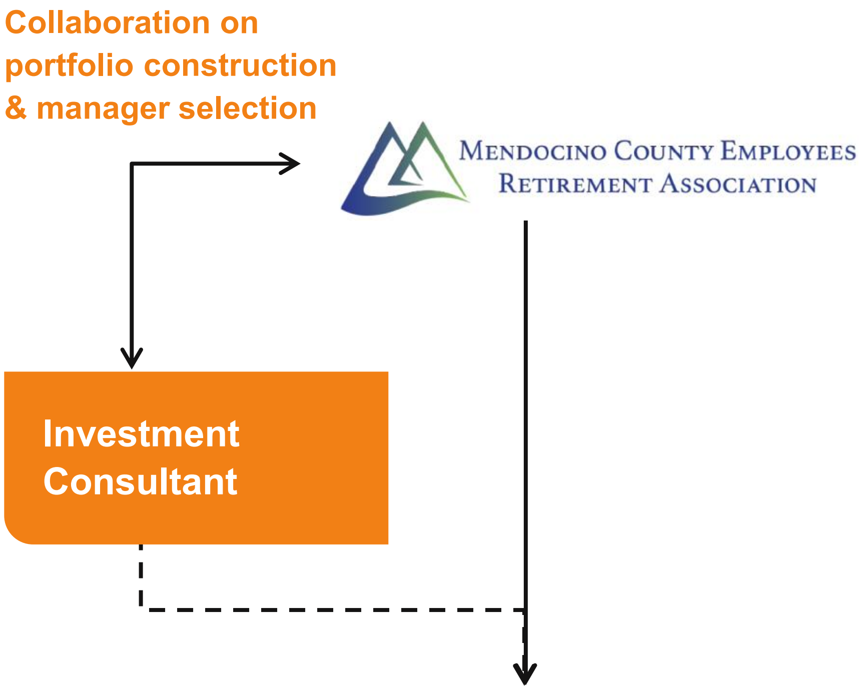
Fund Tax

Fund Audit

Fund Admin

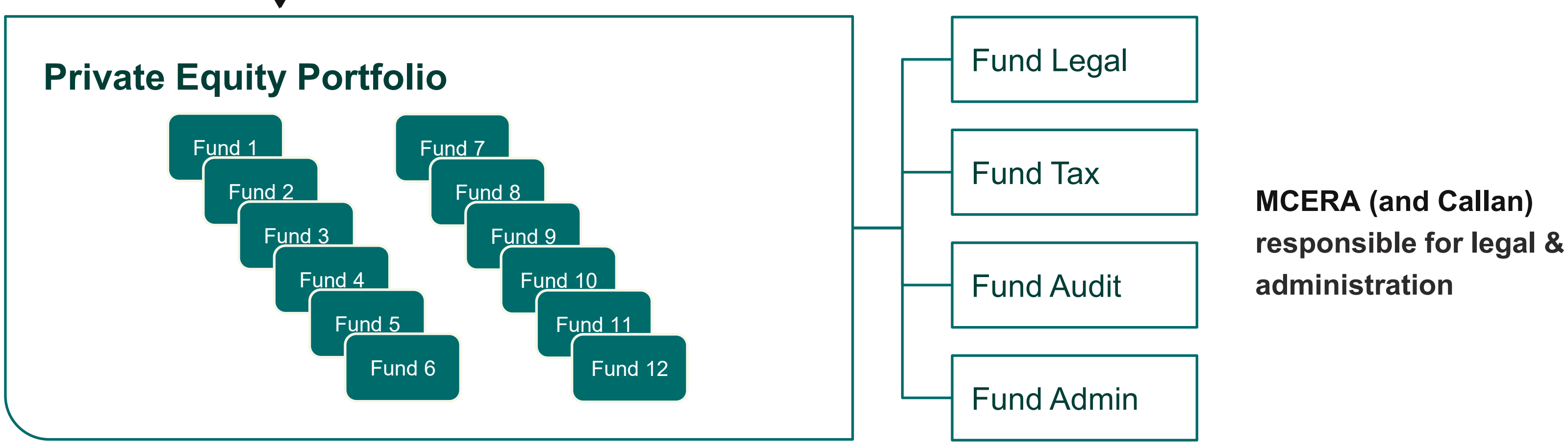
FOF manager responsible for legal & administration

Investment Structure: Direct (Primary Fund) Program



Pros
- MCERA retains input over manager selection and portfolio construction
- Collaboration with consultant to source and diligence fund ideas
- Lower fees vs. FOFs
- Potentially higher expected returns and liquidity

Cons
- Requires regular coordination between consultant and MCERA staff/Investment Committee
- Requires MCERA to perform administration functions for a potentially significant number of line items



Key Decision Dimensions

- Governance and decision-making
- Internal resources and expertise
- Access to top-tier managers
- Portfolio construction, pacing, and diversification
- Co-investment capabilities
- Risk profile
- Cost and fee structures

Private Equity Implementation Options

	Fund-of-Funds (Commingled)	Hybrid Structure	Direct (Primary Fund) Program
Summary	Commingled fund-of-funds	Combination of FoF, direct funds, and/or evergreen (commingled, tender, platform, etc.)	Tailored portfolio of private markets funds with consultant assistance.
Implementation Risk	Lower	Moderate	High
Program Complexity	Lower	Moderate	High
Diversification	High	Moderate	Custom
Fee Structure (mgmt. fee and carried interest est. fee range)*	0.5%-1.0% mgmt fee / 5%-10% carried interest for FOFs plus underlying fund fees*	Weighted average of FOF and direct fund fees, and potentially “access” fees where applicable	Advisory fee + underlying fund fees*
Net Returns	Lower	Lower / Moderate	Higher
Return Dispersion	Lower	Moderate / Higher	High
Degree of Investor (LP) Collaboration	Low	Lower / Moderate	High
Key Benefits	– Lower complexity (“turnkey”) – Broad exposure, including primary funds, secondaries and co-investments – Lower minimum investment (<$5mm) – Outsourced admin and operations – Delegated investment authority	– Potentially more complexity – FoF may serve as entrée to developing relationships with GPs – Liquidity enhancement if utilizing tender, interval and other evergreen vehicles	– Customized portfolio construction and risk profile – Opportunity to collaborate with staff – Lower cost vs. FOFs (lowest cost option) – Flexible degrees of delegation
Key Considerations	– No investor input – Additional fee layer – Potential over-diversification – No consideration of any legacy funds – Potential for return dilution	– Additional fee layer from FOF portion – Multiple “platforms” could lead to complex administration/reporting – Flexibility limited depending on FOF exposure	– Typical annual commitments >$10 million – Need process for fund selection – Investor may retain portfolio administration – More time and resource-intensive

*Underlying fund level management fee typically 1%-2%; carried interest typically 15%-20% (lower for private credit; higher for private equity); typically 0% management fee on co-investments

Private Credit Implementation Options

	Closed-End Funds	Evergreen (Open-End Funds)
Liquidity	Illiquid	Limited liquidity depending on structure
Maturity	5–7 years	3–5 years
Interest rate	Floating	Floating
Investor Entry Points	Every 2–3 years	Every 3–6 months
Investment Period	2–3 years	1–2 years
Redemption Period	No redemptions	Requests can be made quarterly or annually, but the actual time to receive proceeds may be 3-4 years
Harvest Period	3–4 years	3–4 years after redemption
Benefits	Typically used for assets requiring longer timelines (specialty finance, asset-backed finance, etc.)	More flexible entry/exit points

- Private credit closed-end funds are similar to private equity, with the key differences being a shorter term and greater j-curve mitigation.
- Evergreen funds are more flexible, with frequent entry and exit points that allow investors to gain immediate exposure to the asset class.

TAKEAWAYS

1. Direct investing is an organizational commitment, not simply an investment decision.
2. There is no universally "best" implementation model.
3. Scale and internal resources influence implementation choices.
4. Most peers continue to rely on external expertise.
5. Implementation should reflect MCERA's objectives and governance capacity.

Appendix

Governance Requirements

Constituent		Primary Role(s)	Responsibilities
Investment Committee and/or Board	▶	Fiduciary and program oversight	– Approves strategic plan and investment policy statement – Monitors program risk profile and performance relative to investment policy and guidelines – Ensures adequate resources are available for program management; delegates responsibilities
Investment Staff	▶	Program implementation and monitoring	– Manages and monitors program per the board's approved plan and guidelines – May retain external advisers to assist
Administrative Staff	▶	Program administration	– Verifies and processes all economic flows between the partnership and the limited partnership (LP) interest – Responsible for fund accounting, performance measurement, risk monitoring, reconciling fees, and preparing the annual audit
Administrator–Custodian/Trustee	▶	Program administration	– Custodian: Provides custody and recordkeeping services and performance reporting, and processes all capital flows—is not a fiduciary – Trustee: Holds legal title to the program's assets and executes partnership and other legal documents on behalf of the plan—is a fiduciary
Consultant	▶	Program oversight, implementation, monitoring, and administration (varies)	– Assists with the development of the strategic plan based on the sponsor's objectives and resources – Provides manager sourcing, due diligence, monitoring, and day-to-day administration – Advises the investment committee and staff on industry trends and best practices – Assists administrative staff with reviewing cash flows, working with the custodian, and annual audit
General Partner	▶	Program implementation	– Executes investment strategy: the sale and purchase of portfolio companies and securities – Each partnership has its own legal/governance structure and works with legal, tax, audit, and administration service providers
Legal Counsel	▶	Program implementation and monitoring	Reviews and negotiates partnership agreements, side letters, and amendments; may be internal or external

Peer Group

We compiled a peer group of California public pension plans with $1–10 billion in assets to examine how similarly sized systems have implemented their private equity programs. Given their comparable regulatory environment, governance structure, and scale, these plans provide a useful benchmark for evaluating implementation models, staffing approaches, and use of external partners.

CERL Plans ('37 Act County Systems)

Official Plan Name	AUM ($)	PE Allocation (%)
Imperial County Employees' Retirement System	1,380,440,548	5%
Merced County Employees' Retirement Association	1,442,293,376	15%
Tulare County Employees' Retirement Association	2,347,140,411	9%
Stanislaus County Employees' Retirement Association	3,315,231,858	5%
Marin County Employees' Retirement Association	3,654,589,979	8%
Sonoma County Employees' Retirement Association	4,274,326,000	0%
San Joaquin County Employees' Retirement Association	5,244,428,788	16%^
Santa Barbara County Employees' Retirement System	5,002,423,218	10%
Kern County Employees' Retirement Association	6,891,788,108	5%
San Mateo County Employees' Retirement Association	7,141,375,017	7%
Fresno County Employees' Retirement Association	7,852,637,940	8%
Ventura County Employees' Retirement Association	9,915,882,466	18%

^ Aggressive Growth Allocation includes Opportunistic Real Estate

Fund of Fund Use

The table below maps each peer plan's current private equity implementation model across three broad categories: fund of funds, hybrid, and direct. These categories reflect how each plan accesses private equity managers — whether through a pooled vehicle managed by an intermediary, through a combination of approaches, or through general partners.

Official Plan Name	Implementation Model	FoF Usage
Imperial County Employees' Retirement System	Fund of Funds	Y
Merced County Employees' Retirement Association	Primary	Y
Tulare County Employees' Retirement Association	Hybrid	Y
Stanislaus County Employees' Retirement Association	Primary	N
Marin County Employees' Retirement Association	Fund of Funds	Y
Sonoma County Employees' Retirement Association	N/A	N/A
San Joaquin County Employees' Retirement Association	Hybrid	Y
Santa Barbara County Employees' Retirement System	Primary	N
Kern County Employees' Retirement Association	Primary	N
San Mateo County Employees' Retirement Association	Primary	N
Fresno County Employees' Retirement Association	Primary	Y
Ventura County Employees' Retirement Association	Primary	Y

**Implementation model classifications reflect the predominant approach to private equity manager access at each plan.*
Source: Pitchbook

Resources

The table below surveys a cross-section of California public retirement plans and maps each plan's current approach to private equity investment infrastructure across three dimensions: (1) whether the plan maintains dedicated internal staff*, (2) whether the plan has an internal Chief Investment Officer^, and (3) whether the plan has engaged a specialist PE consultant to support manager selection and portfolio monitoring.

Official Plan Name	Dedicated Staff	Internal CIO	Second Consultant
Imperial County Employees' Retirement System	N	N	N
Merced County Employees' Retirement Association	Y	N	Y
Tulare County Employees' Retirement Association	N	N	N
Stanislaus County Employees' Retirement Association	Y	N	Y
Marin County Employees' Retirement Association	N	N	N
Sonoma County Employees' Retirement Association	Y	Y	Y
San Joaquin County Employees' Retirement Association	Y	N	N
Santa Barbara County Employees' Retirement System	Y	N	Y
Kern County Employees' Retirement Association	Y	Y	Y
San Mateo County Employees' Retirement Association	Y	Y	N
Fresno County Employees' Retirement Association	Y	Y	Y
Ventura County Employees' Retirement Association	Y	Y	N
	75%	42%	50%

*Staff classifications are based on publicly available job titles and may not fully reflect the scope of responsibilities, reporting structures, or internal resource allocation at each plan.
^Internal CIO data from https://sacrs.org/ and publicly available job titles
Source: Pitchbook

Program Design

Governance and oversight: investment policy statement

An investment policy statement (IPS) should be incorporated in the strategic planning process to provide guidelines, policies, and procedures

Guidelines

- The role of private markets in the context of total portfolio
- Total return objectives for the private markets portfolio
- Composition of the total return (proportion of income vs. appreciation)
- Level of discretion assigned to each participant and their corresponding fiduciary role
- Roles and responsibilities of each participant (managers, staff, board, consultant, legal counsel)
- Appropriate vehicles for accessing investments

Policies

- The management of risk: seniority, quality, diversification, ownership structure, and leverage
- Portfolio composition
- Security types: securitized equity/debt, private placements
- Any statutory requirements

Procedures

- Investment funding and documentation
- Investment control and monitoring, including performance measurement and monitoring and manager reviews

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