

POPULAR ANNUAL FINANCIAL REPORT

For the Fiscal Year Ended June 30, 2017



A MESSAGE FROM THE CEO

Here's to our health!



After two years of weak market returns, SamCERA's fund experienced a healthy 12.6% return net of fees for the 2016-2017 fiscal year. This return, along with strong funding by employers, was enough to increase SamCERA's funded status by over 1.0% to an estimated 84.3%. This marks our highest funded status since 2002 and the eighth straight year of an increase.

Significantly, this 84.3% funding level was reached even with the Board adopting a lower assumed rate of return from 7.0% to 6.75% and generational mortality tables.

(Continued on the back page)

INTRODUCTION

This Popular Annual Financial Report is a condensed version of the San Mateo County Employees' Retirement Association's (SamCERA) Comprehensive Annual Financial Report (CAFR), which is prepared in accordance with generally accepted accounting principles in the United States of America. The CAFR provides in-depth information about the financial, investment, actuarial, statistical, and compliance aspects of SamCERA and is available online at www.samcera.org.

For the 14th consecutive year, the Government Finance Officers Association (GFOA) of the United States and Canada presented an award for Outstanding Achievement in Popular Annual Financial Reporting (PAFR) to SamCERA in recognition of its PAFR for the fiscal year ended June 30, 2016.

ABOUT SAMCERA

SamCERA is a cost-sharing multiple-employer, defined benefit pension plan established to provide pension benefits for predominantly all permanent employees of the County of San Mateo (the County), the Superior Court of the County of San Mateo, and the San Mateo County Mosquito and Vector Control District. As of June 30, 2017, SamCERA had a total of 11,780 members.

The management of SamCERA is vested in the Board of Retirement consisting of nine members: the first member is the County Treasurer; the second and third members are general members of SamCERA elected by their peers; the fourth, fifth, sixth and

ninth members are qualified electors of the County and appointed by the County Board of Supervisors; the seventh member is elected by and a member of SamCERA's safety membership; and the eighth member is a retired member elected from the retired membership. In addition, there is one elected Safety Member Alternate and one elected Retired Member Alternate.

MISSION AND GOALS

SamCERA exists to serve as loyal fiduciary for its members and as prudent administrator of the retirement system. SamCERA will continue to pursue its three major goals:

- Provide caring, fair, accurate, timely and knowledgeable professional services and information to members and other stakeholders.
- Prudently manage the assets in order to appropriately fund the actuarial liabilities of the retirement system to ensure the ability to pay all earned benefits while minimizing the costs to employers.
- Constantly improve the effectiveness of SamCERA's services and the efficiency of its operations.



SUMMARY OF SIGNIFICANT ACTUARIAL STATISTICS AND MEASURES

In July 2017, the Retirement Board adopted the assumptions developed from the latest triennial Investigation of Experience Study for use in the 2017 valuation. These changes include lowering the assumed investment return, modifying the mortality assumptions, and adding a projection scale to reflect gradual year-to-year increase in mortality that is expected to occur in the future.



The assumed investment rate of return was changed from 7.00% to 6.75%, the inflation rate from 2.75% to 2.50%, and the general wage growth from 3.25% to 3.00%. The new mortality assumptions resulted in an increase in assumed life expectancy compared to the prior assumptions.

	June 30, 2017	June 30, 2016	Relative Change
ACTIVE MEMBERS			
Number of Members	5,337	5,187	2.9%
Average Age	44.2	45.4	(2.6)%
Average Credited Service	10.5	10.8	(2.8)%
Total Active Payroll (In Thousands)	\$510,132	\$472,385	8.0%
Average Monthly Salary	\$8,154	\$7,933	2.8%
RETIRED MEMBERS			
Number of Members			
Service Retirement	3,869	3,749	3.2%
Disability Retirement	469	454	3.3%
Beneficiaries	618	545	13.4%
Average Age	71.2	71.0	0.3%
Actual Retiree Benefits Paid (In Thousands)	\$190,364	\$179,497	6.1%
Average Monthly Pension	\$3,347	\$3,268	2.4%
NUMBER OF INACTIVE MEMBERS	1,487	1,486	0.1%
ASSETS			
Market Value of Fund (In Thousands)	\$4,038,702	\$3,541,388	14.0%
Return on Market Value	12.6%	0.7%	
Valuation Assets (In Thousands)	\$3,976,717	\$3,624,726	9.7%
Return on Valuation Assets	7.8%	6.4%	
LIABILITY VALUES (IN THOUSANDS)			
Actuarial Accrued Liability	\$4,719,850	\$4,362,296	8.2%
Unfunded Actuarial Accrued Liability	\$743,133	\$737,570	0.8%
Deferred Asset (Gains) / Losses	(\$21,816)	\$119,951	
FUNDED RATIO			
Based on valuation assets	84.3%	83.1%	1.4%

SAMCERA'S STATEMENT OF FIDUCIARY NET POSITION

As of June 30 (Dollars In Thousands)

	2017	2016	Increase (Decrease)	
			Amount	Percentage
Assets				
Cash and cash equivalents	\$ 192,194	\$ 130,111	\$ 62,083	48%
Cash management overlay	25,208	26,249	(1,041)	-4%
Securities lending cash collateral	-	88,363	(88,363)	-100%
Receivables	25,399	22,636	2,763	12%
Prepaid expense	8	8	-	0%
Investments at fair value	3,802,162	3,368,375	433,787	13%
Capital assets, net	7,629	5,162	2,467	48%
Total assets	4,052,600	3,640,904	411,696	11%
Liabilities				
Investment management fees	1,822	1,808	14	1%
Due to broker for investments purchased	9,417	7,582	1,835	24%
Collateral payable for securities lending	-	88,363	(88,363)	-100%
Other	2,659	1,763	896	51%
Total liabilities	13,898	99,516	(85,618)	-86%
Net position restricted for pensions	\$4,038,702	\$3,541,388	\$497,314	14%

MORE ABOUT THE TABLE ABOVE

The **Statement of Fiduciary Net Position** is a snapshot of account balances at fiscal year-end. The difference between assets and liabilities is “net position,” which represents funds available to pay pension benefits. As of June 30, 2017, SamCERA’s net position increased by \$0.5 billion to \$4.0 billion. The increase was mainly from investment earnings and supplemental contributions from the County of San Mateo (the County).

SamCERA’s investment performance was strong overall as the market conditions continued to gain momentum throughout the fiscal year. The return on investments



was 12.6% net of investment manager fees in fiscal year 2017.

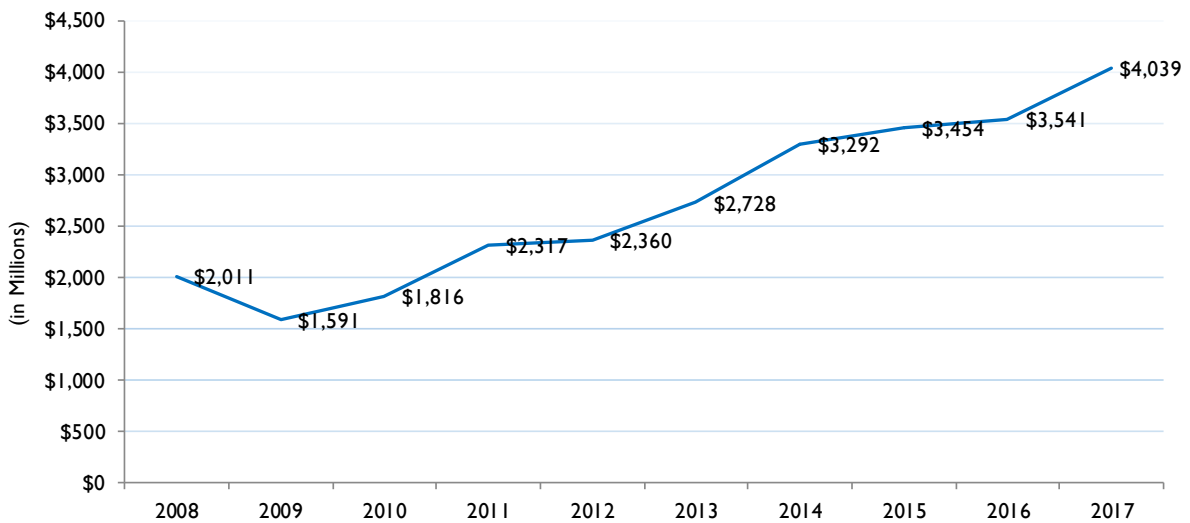
With a strong commitment to accelerate the payoff of its unfunded liability, the County increased its supplemental contributions by \$14 million in fiscal year 2017.

GOOD FINANCIAL STANDING

Increases and decreases in the fiduciary net position over time may serve as a useful indicator of whether the financial health of SamCERA is improving or declining. Because of strong return on investments, the overall financial position of SamCERA has improved. SamCERA remains in a good financial position to meet its obligations to members and beneficiaries.

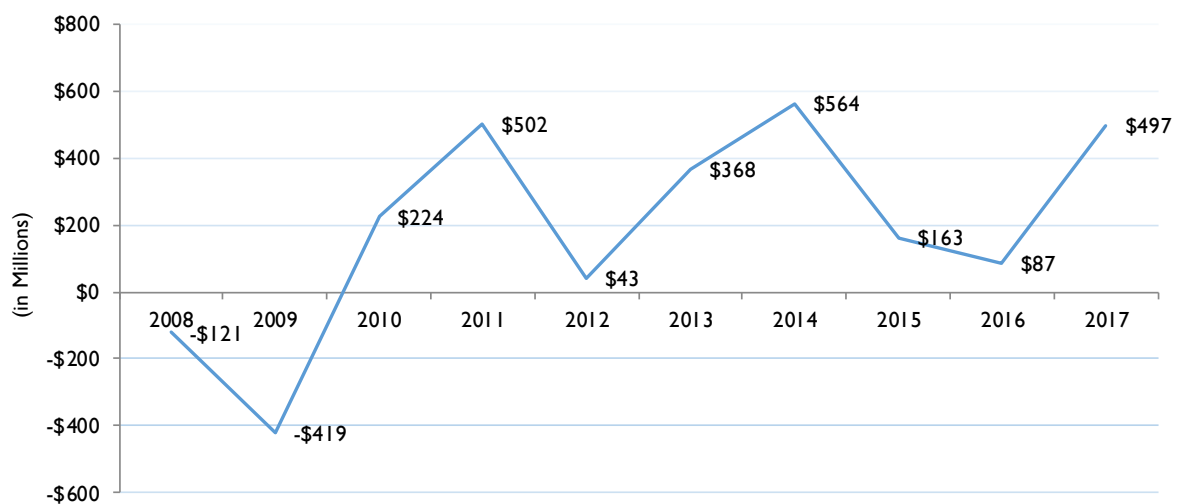
SAMCERA'S NET POSITION

As of the fiscal years ended June 30



CHANGE IN SAMCERA'S NET POSITION

For the fiscal years ended June 30



SAMCERA'S STATEMENT OF CHANGES IN FIDUCIARY NET POSITION

For the Fiscal Years Ended June 30 (Dollars In Thousands)

	2017	2016	Increase (Decrease)	
			Amount	Percentage
Additions				
Employer contributions	\$ 198,727	\$ 191,094	\$ 7,633	4%
Member contributions	62,160	56,069	6,091	11%
Net investment income	436,603	24,112	412,491	1711%
Net securities lending income	46	278	(232)	-83%
Other	27	4,910	(4,883)	-99%
Total additions	697,563	276,463	421,100	152%
Deductions				
Service retirement benefits	166,975	157,513	9,462	6%
Disability retirement benefits	22,690	21,091	1,599	8%
Survivor, death and other benefits	699	894	(195)	-22%
Member refunds	2,876	3,366	(490)	-15%
Administrative expenses	5,983	5,962	21	0%
Information Technology expenses	996	714	282	39%
Other expenses	30	11	19	173%
Total deductions	200,249	189,551	10,698	6%
Changes in Net Position	497,314	86,912	410,402	472%
Net position restricted for pensions				
Beginning of year	3,541,388	3,454,476	86,912	3%
End of year	\$4,038,702	\$3,541,388	\$497,314	14%

The [Statement of Changes in Fiduciary Net Position](#) provides information about SamCERA's financial activities during fiscal year 2017.

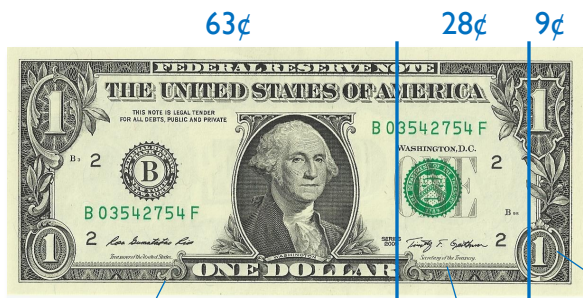
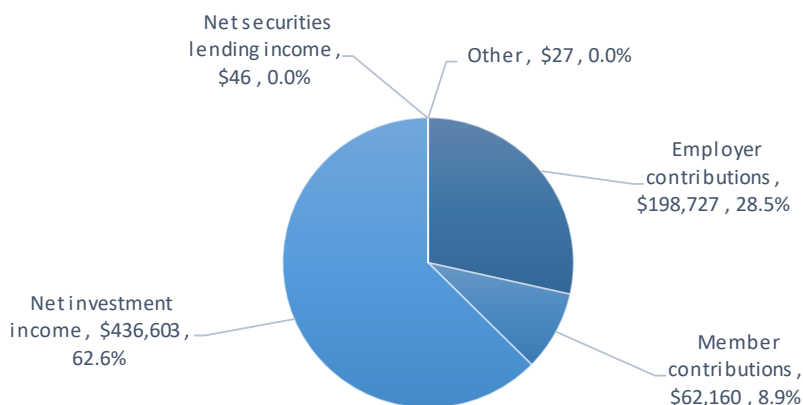
[Total additions to fiduciary net position](#) increased \$421 million, due mainly to the following:

- \$412 million increase in net investment income was primarily due to strong investment performance under favorable market conditions.
- \$14 million increase in contributions, partly from the County's supplemental contributions to payoff the unfunded liability and partly driven by shifting a portion of the cost of living adjustment contributions from the County to its employees.

[Deductions from fiduciary net position](#) increased \$11 million, triggered mainly by an increased number of retirees receiving pension benefits.

WHERE DID SAMCERA'S MONEY COME FROM?

For the Fiscal Year Ended June 30, 2017 (Dollars in Thousands)



This graphic uses the same information in the pie chart above. It shows the breakdown of every dollar SamCERA received this fiscal year.

This is a simplification of SamCERA's additions. Numbers are rounded to the nearest whole penny.

Net Investment Income

This includes earnings from stocks, bonds, alternatives, real estate, and other investments, minus fees.

Employer Contributions

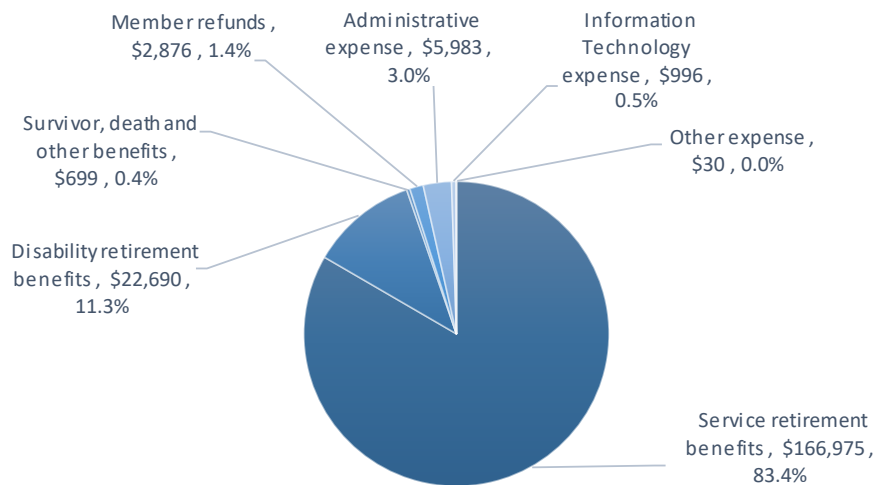
This is the money paid to SamCERA from employers for employees' pension benefits.

Employee Contributions

This is the money active employees pay into the fund for future benefits.

WHERE DID SAMCERA'S MONEY GO?

For the Fiscal Year Ended June 30, 2017 (Dollars in Thousands)



INVESTMENT POLICY

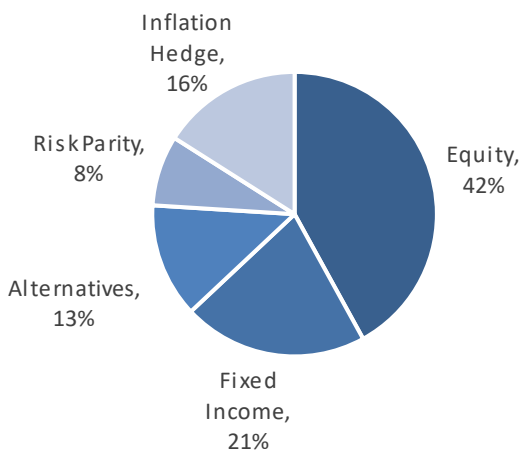
SamCERA’s Investment Policy is aimed at reducing risk through a prudent diversification of the investment portfolio across a broad selection of distinct classes. The Retirement Board conducted an asset-liability study in fiscal year 2017 and subsequently approved a new target asset allocation. The Board undertakes an in-depth asset and liability study every three to five years.



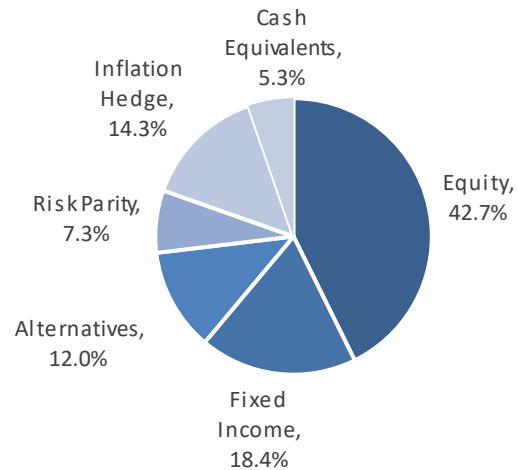
INVESTMENTS

As of June 30, 2017

Target Asset Allocation



Actual Asset Allocation



SamCERA’s asset allocation strategy calls for approximately half of the portfolio to be invested in the stock market.

Items in the charts above labeled with “Equity” are part of this investment, which is divided among domestic and international markets.

ASSET ALLOCATION

Asset allocation divides the investment portfolio among different asset classes including equity, fixed income, alternatives, risk parity, and inflation hedge assets. The target asset allocation consists of 42% in equity, 21% in fixed income, 13% in alternatives, 8% in risk parity, and 16% in inflation hedge assets.

As of June 30, 2017, actual asset allocation was 42.7% in equity, 18.4% in fixed income, 12.0% in alternatives, 7.3% in risk parity, 14.3% in inflation hedge assets, and 5.3% in cash and cash equivalents.

INVESTMENT PORTFOLIO PERFORMANCE

As of June 30, 2017

SamCERA's portfolio returned 12.6% net of investment manager fees for the fiscal year ended June 30, 2017, matching SamCERA's policy benchmark return. This fiscal year's overall performance resulted in median performance relative to SamCERA's peers, as defined by large (greater than \$1 billion in assets) public pension plans.

Global equities and other risk assets (i.e., investment grade credit, high yield fixed income, emerging market equity) provided strong returns during the fiscal year, as easy money policies from the developed world central banks, combined with steady (if unspectacular) global economic growth resulted in higher asset prices for risk assets. This strong performance came in spite of a number of events happening

through the year, including elevated geopolitical risks, the fall-out from the Brexit vote in the United Kingdom, and the impact of the U.S. election.

During the 2017 fiscal year, SamCERA's Board approved an updated asset allocation policy as part of its asset-liability study. Exposures to public equity are reduced in the new policy, with additions to inflation hedge assets (real estate, private real assets, and liquid real assets), fixed income (opportunistic credit and core fixed income), and alternatives (absolute return). SamCERA is reducing its reliance on U.S. equities by allocating more assets to inflation hedge strategies and other diversifying assets. SamCERA will continue

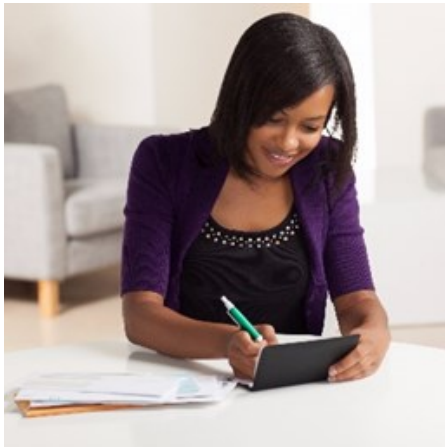
Investment Asset Class	Fair Value (In Millions)	Investment Return		
		One Year	Three Years	Five Years
Equity	\$ 1,718	18.6%	6.1%	12.0%
Equity Benchmark		20.0%	6.0%	12.0%
Fixed Income	738	7.2%	3.5%	4.5%
Fixed Income Benchmark		2.2%	2.7%	2.5%
Alternatives	481	17.1%	7.8%	7.2%
Alternatives Benchmark		13.6%	3.8%	6.7%
Risk Parity	292	4.1%	2.8%	5.8%
Risk Parity Benchmark		10.7%	6.6%	9.6%
Inflation Hedge⁽¹⁾	573	5.9%	*	*
Inflation Hedge Benchmark		4.2%	*	*
Cash Equivalents	237	0.8%	1.0%	0.7%
Cash equivalents Benchmark		0.5%	5.3%	0.2%
Total Investments	\$ 4,039	12.6%	5.5%	9.4%
Policy Benchmark		12.6%	5.3%	9.2%

Equity Leads Earnings
SamCERA's equity portfolio was this year's top performing asset class.

(1) The creation of a dedicated Inflation Hedge asset class was effective April 1, 2016.

* Return information is not available.

Note: return calculations were prepared using a time-weighted rate of return, net of fees, in accordance with the Global Investment Performance Standards.



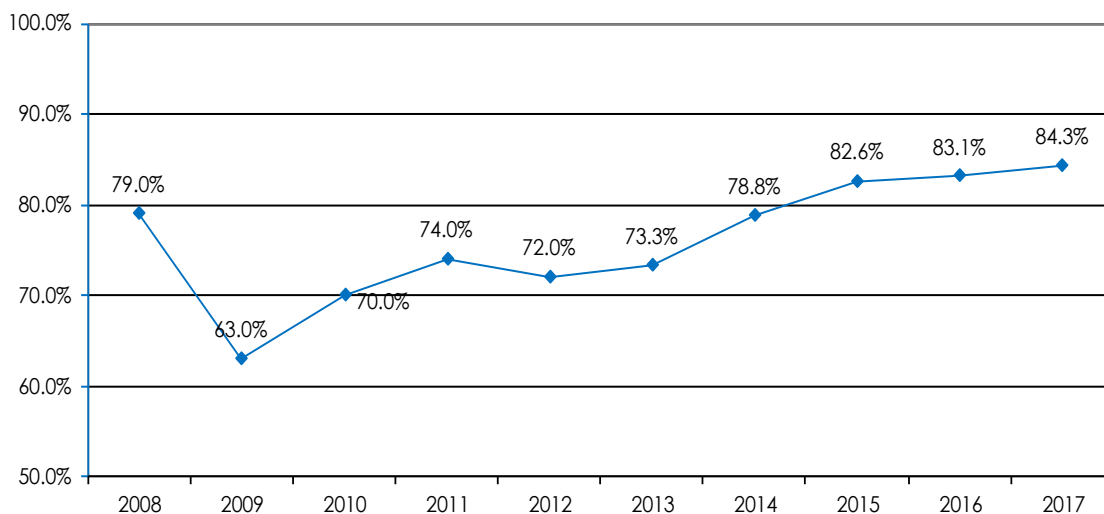
to thoughtfully balance the return potential of equity investments versus the potential risks they bring to the portfolio in order to produce the most efficient risk-adjusted return stream for the portfolio as possible.

Even though the current fiscal year exhibited strong returns, SamCERA continues to be mindful of higher potential future return volatility, and the increased likelihood of this resulting in lower returns in the future. We continue to actively rebalance the portfolio to its long-term policy asset allocation weights in order to keep a balanced risk posture without relying too much on any single asset, strategy, or return stream.

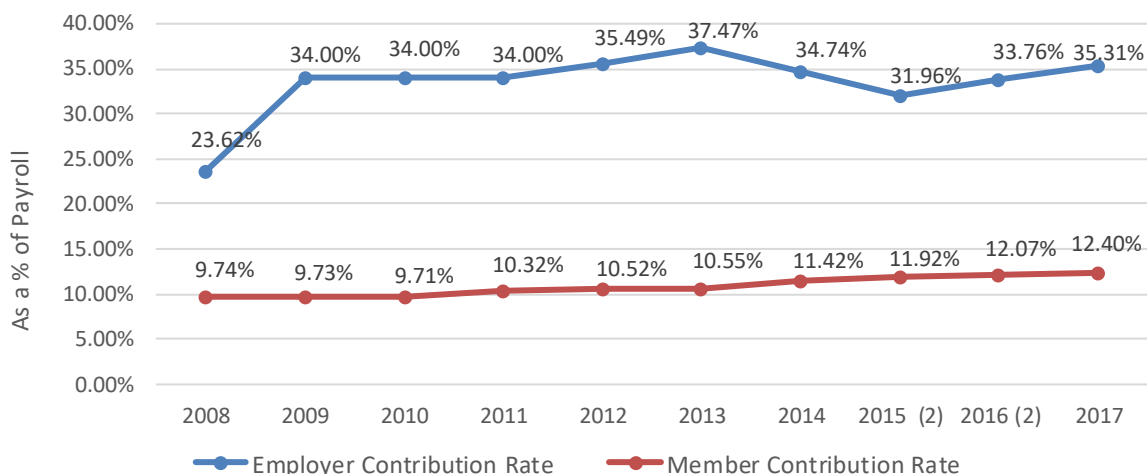
FUNDED RATIO AS OF JUNE 30

According to the latest actuarial valuation as of June 30, 2017, the pension plan was 84.3% funded. The funded status is simply the ratio of plan assets to plan liabilities. The difference between these two amounts represents the unfunded liability, which was \$743 million.

Over the year, the improvement in funded ratio was mainly due to investment gains and employer contributions to pay down the unfunded liability.



EMPLOYER AND MEMBER CONTRIBUTION RATES ⁽¹⁾ (DETERMINED AT JUNE 30)



⁽¹⁾ The contribution rates determined as of the valuation date will become effective a year later. For example, the contribution rates determined as of June 30, 2017, will become effective on July 1, 2018.

⁽²⁾ The Statutory Contribution Rates reflect changes in member rates negotiated subsequent to the 2015 and the 2016 valuations.

SamCERA retains an independent actuary to perform an annual actuarial valuation. The purpose of this valuation is two-fold: (1) to determine required contributions from employers and members to pay the projected future benefits, and (2) to monitor SamCERA’s funded status. Contributions are based on various factors such as market fluctuations, plan amendments, and changes in actuarial assumptions and member demographics. The funded ratio compares SamCERA’s assets and liabilities as a measure of its financial health at a point in time.



The contribution rates determined as of the valuation date will become effective a year later in fiscal year 2018-19. Driven by the recently adopted economic assumptions which include a lower expectation for future investment returns, both the employer and member contribution rates increased slightly when compared to the prior year.

A message from the CEO *(Continued from the front page)*

Any one of these two conservative changes would normally have had an immediate impact of lowering our funded status. However, due to earnings from the strong market performance and the continued strong funding from employers, the Board was able to prudently take both of these actions without negatively impacting our funded status. These conservative funding assumptions will lead to slightly higher contribution rates for employers and most employees, which will serve to keep the fund healthy over the long-term. SamCERA is now better positioned should its investments fall short of its long-term average assumed rate of return.

With respect to the fund's performance, this year's healthy returns were primarily due to our public equity and alternative investments. The 12.6% return matched the fund's policy benchmark and was in-line with our public pension plan peers. Over the most recent five-year period ended June 2017, SamCERA's performance was in the upper quartile of its peers.

In addition to adopting more conservative assumptions, SamCERA's Board also updated its asset allocation policy as part of its asset-liability study. The new policy reduces the reliance on U.S. equity performance as a portfolio growth driver in

favor of more inflation hedging, fixed income and alternatives assets. Inflation hedging assets, such as real estate, private real assets and liquid real assets will receive greater exposure in the new portfolio structure. The increased allocation to fixed income will be split between opportunistic credit and core fixed income, while additional allocations to alternatives will go towards the absolute return asset class. So, much like a balanced diet that helps to maintain or improve a person's overall health, a more diversified portfolio is healthier for our fund and the updated portfolio will be further strengthened to withstand future equity market downturns.

Whatever future ailments might affect the domestic and global markets, SamCERA has the right prescription for the health of its fund: a more diversified portfolio, more conservative economic and demographic assumptions and continued prudent funding by our employers.



Scott Hood
SamCERA
Chief Executive Officer

