



CASH PORTFOLIO STRUCTURE REVIEW

EMPLOYEES' RETIREMENT SYSTEM
OF RHODE ISLAND

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STRATEGIC CASH OVERVIEW

- **The ERSRI Pension Plan has a strategic cash asset allocation target of 2.0%**
 - The allocation resides within the Volatility Protection category (15% target) which is part of the broader Stability sleeve (33% target)
- **The strategic cash portfolio is actively managed by Payden & Rygel**
- **Since inception (2017) the strategy has outperformed the benchmark by ~25 basis points, net of fees**
 - Despite the long-term outperformance, there have been periods of meaningful underperformance such as March 2020 when the strategy underperformed the benchmark by more than 1.5%
- **At times, the process for withdrawing assets from the account has been more challenging than expected**
- **Finally, fees for the current strategy are above the market rate for a mandate of this size**
- **Given these factors, we believe a review of the cash manager is appropriate**

PORTFOLIO SUMMARY

Total Portfolio Assets (\$million)	\$11,614
Total Strategic Cash Assets (\$million)	\$192
Number of Cash Managers	1
% Actively Managed	100%
Benchmark	ICE BofA 0-1 Yr. U.S. Treasury
Expected Return (10-Year)*	4.1%
Expected Risk (Standard Deviation)*	0.6%

Stated IPS Portfolio Objectives

- **The Strategic Cash portfolio seeks to obtain a level of current income while prioritizing the preservation of principal and liquidity via investments in high quality U.S. dollar-denominated money market and fixed income securities of domestic and foreign issuers, U.S. Government securities, and repurchase agreements.**

		Current Target	Actual – 2/28/25
Growth	Global Equity	40.0%	37.6%
	Private Equity	12.5%	16.8%
	Non-Core Real Estate	2.5%	2.3%
	Private Growth	15.0%	19.2%
	TOTAL GROWTH	55.0%	56.7%

Income	Equity Options	2.0%	1.8%
	Liquid Credit	5.0%	4.3%
	CLO Mezz/Equity	2.0%	2.4%
	Private Credit	3.0%	3.1%
	TOTAL INCOME	12.0%	11.6%

Stability	Long Treasuries	5.0%	4.8%
	Systematic Trend	5.0%	4.5%
	CPC	10.0%	9.2%
	Core Real Estate	4.0%	3.2%
	Private Real Assets (ex-RE)	4.0%	4.2%
	Inflation Protection	8.0%	7.4%
	Inv. Grade Fixed (ex-Treas.)	6.5%	5.7%
	Absolute Return	6.5%	6.6%
	Strategic Cash	2.0%	1.7%
	Volatility Protection	15.0%	14.0%
	TOTAL STABILITY	33.0%	30.6%

STRATEGIC CASH GUIDELINE ADJUSTMENTS

- **The current strategic cash guidelines with Payden & Rygel are reasonable and generally appropriate**
- **However, we believe there are adjustments that can be made to increase safety and liquidity and reduce the risk of mark-to-market volatility**
 - The trade off is a slightly lower expected return relative to the benchmark.
- **Most notably, the guidelines should contain language that up to 50% of the portfolio should be readily available for withdrawals with 1 day notice with the next 25% available in a week and the full account value available with 1 month**
- **Other areas for potential adjustment include:**
 - Credit Quality: Move to A3/A- and A1/P1 or better
 - Duration: Reduce to a target of 0.75 years or less
 - Corporate Securities: Limit to 50% of portfolio
 - Structured Product: Maintain 10% limit, but add the following:
 - Prohibit CLO/CBO
 - Prohibit mortgage derivatives such as IO/PO/Inverse
 - Require all holdings be AAA by one of the “big three” NRSRO
 - Include a specific Weighted Avg Life restriction
 - Foreign Issuers
 - Prohibit foreign securities, non-dollar securities, Yankees
 - Illiquid Securities: Not allowed

COMPARISON OF GUIDELINES

	Current Guidelines	Adjusted Guidelines
Investment Objective	The Cash Portfolio seeks to obtain a high level of current income	The Cash Portfolio seeks to obtain a moderate level of current income in excess of Treasury bills
Liquidity Expectations	N/A	50% within one day 75% within one week Fully available within one month
Minimum Quality	At time of purchase: Investment Grade Short-Term Issues: A2/P2	At time of purchase: A3/A- Short-Term Issues: A1/P1
BBB-Rated Securities	Max 15%	Not Allowed
Non-Agency Securitized	Based on minimum quality guidelines	Must be rated AAA/Aaa by any major NRSRO
Government Holdings	U.S. and Foreign Governments	U.S. Only
Duration	1 year or less	0.75 years or less
Corporate Securities	No limit	Max 50%
MBS and ABS Wtd. Avg. Life	No limit	Max 2.08 years
Derivatives/Other	See footnote on existing restrictions*	Expanded to include CBOs, CMOs, and non-derivatives such as Foreign Issuers/Securities, Non-Dollar and Yankees
Illiquid Securities	Max 5%	Not Allowed

*Current guidelines exclude: futures, swaps, options, IO/PO MBS, inverse floaters, CMT floaters, leveraged floaters, dual index floaters, COFI floaters, and range floaters, Structural Investment Vehicles (SIV's), Collateralized Debt Obligations (CDO's), Auction Rate Securities

MANAGER REPLACEMENT OPTIONS

- NEPC maintains a recommended list of active short duration strategies
- Payden & Rygel is on our recommended list as a 2-rated manager for short duration and we included two other candidates (Garcia Hamilton and IR+M) for consideration which are 1-rated*
- Another potential solution is to move to a low-cost, 2a-7 money market strategy
- Given the portfolio has a strategic target to cash and there is an expectation that portfolio assets will generally be close to that target, we continue to recommend the use active management
 - We recommend a conservative approach that focuses on downside protection
 - Expectations on contributions and withdrawals should be established with the manager up front
 - The portfolio should be managed conservatively and with enough liquidity such that large cashflows (in or out) do not cause the portfolio to breach guidelines

*NEPC does not rate active cash/money market strategies; short duration is our proxy for purposes of this search
Baird was also considered for this search, but declined to participate

FEES AND LIQUIDITY TERMS

	Payden & Rygel (Current Manager)	Garcia Hamilton	Income Research + Management
Fee Schedule	First \$150mm: 12 bps Next \$100mm: 10 bps Balance: 8 bps	First \$100mm: 6 bps Balance: 4 bps	First \$100mm: 10 bps Balance: 8 bps
Total Fee for \$200mm investment	11.5 basis points	5.0 basis points	9.0 basis points

SUMMARY AND RECOMMENDATION

- NEPC is supportive of active management for the strategic cash allocation
- Guidelines for the strategy should be adjusted to fit the needs of the ERSRI Pension Plan
- We believe Payden & Rygel should be replaced with a more conservative, lower cost approach

Recommendation: Replace Payden & Rygel as the active manager of the ERSRI's Strategic Cash portfolio with Garcia Hamilton & Associates. The recommendation is based on GH&A's attractive fee proposal and history of managing high quality, conservative short duration portfolios.

APPENDIX



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