The Health Care Foundation of Greater Kansas City
Finance and Investment Committee
Minutes of Meeting Held Thursday, August 10, 2017 at 8:00 a.m.

Location: Health Care Foundation of Greater Kansas City (HCF)
Two Pershing Square, 2300 Main Street, Suite 304, Jonas Board Room
Kansas City, Missouri 64108

Attendance

Finance & Investment Committee Members Present: Peg VanWagoner, Chair; Tom Carignan; Tom Cranshaw; Jim Dockins, Ed.D.; Chuck Foudree; Spence Heddens; Roy Robinson; and Julia Simmons, MD

Committee Members Unable to Attend: None

HCF Board Members and Associates Present: Christena Diven; Paula Cornwell; Bridget McCandless; Nancy Pfromm (Contractor); Rick Zimmer; and Victoria McNack (telephone)

Guests in Attendance: David Keil, Brandon Patterson, and Suzanne Bernard, AON

Call to Order

Peg VanWagoner, Chair, called the meeting to order at 8:00 a.m.

Interviews of Investment Advisor Candidate Firms

The ad hoc committee of Finance & Investment has completed its work on the Investment Advisor RFP process. Over the past five months the committee has crafted the selection criteria for the RFP, reviewed proposals received from 20 firms, narrowed firms down by analyzing responses against selection criteria, and nominated a slate of three investment firms to interview at today's meeting. The selected firms include Fund Evaluation Group (FEG), NEPC, and AON. Each firm was allotted 45 minutes to provide a presentation and answer questions of the committee; said interview questions can be found in Appendix A. The committee held a brief discussion following each interview to clarify additional information and their final recommendation was determined after the conclusion of the regular business meeting.

Review and Accept Second Quarter Financial Statements

Rick Zimmer reviewed the operations dashboard and financial statements for the period ended June 30, 2017. The Foundation is operating within budget for the first six months of the year and Mr. Zimmer highlighted points of interest within the provided reports.

Operations Dashboard

- Budgeted grants and operating expenses year-to-date is $8.8 million compared to the actual expenses totaling $8.6 million.
- Current expenditures are $200,000 favorable to budget due to the Communications budget; however, Mr. Zimmer anticipates that the entirety of that budget will be utilized by year-end.
- A positive variance is expected for the year in the payroll and benefits related accounts due to the four new previously approved staff positions. These positions were budgeted for beginning in July, however, each position is in a different stage of the hiring process with expected start dates pushed out to later this year.
- The net asset analysis shows $724 million in current net assets and $660 million in contributed capital.

- One goal has been to recoup the loss of purchasing power; a significant decrease in loss of purchasing power now shows $69 million, the lowest it has been since 2013.

Schedule of Investments

- $735 million of all asset classes are within the respective target ranges assigned.
- The Foundation received approximately $40 million last week from the Aetos and Maverick investment liquidations. These funds are invested for the short term in the Fidelity Money Market Fund until they can be deployed in the new investments as approved in the previous meeting.

Statement of Financial Position

- Grants payable is at $14.5 million which is typical at this time of year.

Sources and Uses of Cash

- The Foundation has had $22 million in cash requirements for capital calls, grants and operations expenses, and pay down on the line of credit. Sources of cash came from the lawsuit ($12 million of cash used) and from cash distributions.
- Current cash distributions are about 10 to 1 compared with capital calls; there have been $11.5 million in cash distributions and $1.8 million in capital calls.

Statement of Changes in Net Assets

- After fees, the investments totaled $43 million in revenue, $37 million of which are unrealized gains which could be lost in a market downturn.
- The annual revenue budget is $31 million, so the Foundation is performing well compared to that target.
- Net asset size increased by $197 million within the first six months of the year, $162 million being from the lawsuit proceeds. This is by far the largest increase in net assets that the Foundation has had since inception.

Medium Term View (MTV) Update *(see AON Materials, Section 2)*

Mr. Keil directed the committee's attention to page 4 and provided a high-level overview of the report (the report can be found in Appendix B of this document):

- Within the equity section, AON is tracking a few additional areas, such as fundamental indexation, low volatility, and quality-focused investments.
- Within equities, the only changes occurred in the international space.
- The overall recommendation is to be overweight in the international investments due to the increased valuation that has not yet been realized in the U.S.
- MTV's are still slightly negative for U.S. government bonds.
- If the dollar is oversold, hedging will be recommended because the portfolio is favorably disposed to the dollar. They will continue to watch this in the coming months.

In response to a question from Jim Dockins, Mr. Keil noted that the Private Equity ratios are within one standard deviation of where the market should be.

Brandon Patterson commented on two of the managers in the Foundation's portfolio (AON materials, Section 3). Templeton announced a change in leadership to take place at year-end when they will appoint a new director of portfolio management. Due to the deep, three-pronged team, AON will still maintain a buy rating. Secondly, it was recently announced that Reams has reached an agreement to be purchased by Carillon Tower Advisors. The transaction is expected to close before the end of the year. There will be no change in the day to day management of Reams and the investment team remains in-tact. As with Templeton, AON will maintain a buy rating.

Quarterly Investment Review *(see AON Materials, Section 4)*

Mr. Keil outlined key highlights from the Asset Allocation & Performance section of the AON materials.

- Total fund performance for the period was 2.8% versus the benchmark of 2.4%.
- Fixed income investment performance for the period was 1.4% versus the benchmark of 1.7%
- While the global equity markets had previously diminished portfolio value, these areas are now performing quite well.
- Real estate performance in the portfolio was a little lower than the benchmark during the quarter earning 1.2%. Five-year performance is positive to benchmark at 10.4% versus 10.3%.

Mr. Zimmer inquired as to why the private equity section tends to remain blank and is there is a way to gain perspective of the specific values. In response, Mr. Keil noted that the return of these investments would be quite small in a quarterly view; however, over the long-term, the composite performance of these areas will be close to the IRR (page 13) and show a more realistic value of the investments. It was decided to include the IRR numbers in an earlier portion of the report and show the short-term performance of private equity.

Mr. Patterson provided additional comments regarding 2nd Quarter activity in the portfolio:

- The new investment in Artisan was funded with $30 million;
- Shankman and Oaktree were terminated;
- The new investment in Guggenheim was funded with $30 million;
- Proceeds of $36 million were received from the Aetos and Maverick liquidations which will be used to invest in direct hedge funds.

Manager Fee Review *(see AON Materials, Section 5)*

Mr. Patterson reviewed the overall fee schedule for investments in the Foundations portfolio. Overall total portfolio fees are .61% compared to peer fees of .82% (according to the 2014 Council on Foundations Commonfund Study of Foundations) and .96% (according to the 2016 Greenwich study on U.S. Institutional Market Trends) Mr. Patterson also went over individual manager's fees as compared to their corresponding peer universe. As noted in the AON materials, the Health Care Foundation's manager fees are lower due to passive management and relatively low fees in the opportunistic strategies portfolio. See Appendix C for AON's summary of manager fee review.

Determine Recommendation to Board for selection of Investment Advisor

After interviewing the three firms, the Finance & Investment Committee recommended that AON continue to serve as the investment advisory firm for the Health Care Foundation. This firm was selected for service level, investment performance, attention to management fees, and cost of the contract.

Tom Carignan motioned to enter into contract and/or renegotiate the current contract with Aon for investment advisor services, pending approval from the HCF Board of Directors. Roy Robinson seconded and the motion was approved by unanimous voice vote.

Adjourn

The meeting was adjourned at 12:29 p.m.

APPENDIX A

Investment Advisor Interview Questions

INVESTMENT CONSULTANT INTERVIEW QUESTIONS
(Question rationales listed in red)

1. **CURRENT PORTFOLIO ASSESSMENT (PRE-WORK FOR LEAD CONSULTANT)**
   a. Each Lead Consultant was asked to provide in advance of the meeting (in summary bulleted format) answers to the following questions: **(Peg)**
      i. **What changes would you make to our current portfolio and why?**
      ii. **When and How would you do it?**
      iii. **At what cost?**
      iv. **Explain the administrative support role that NEPC/FEG would provide in making the recommended changes (e.g. Letters of Instructions, etc.).**

   Purpose of Pre-Work Questions: Having the Consultant assess our current portfolio has these objectives:
   1. Gives the consultant an opportunity to get their best ideas out on the table (and for us to assess those ideas).
   2. Demonstrates the Lead Consultants ability to communicate clearly with the Committee in explaining Investment changes, fit within the portfolio and the role any recommended investment changes would play in the overall portfolio. We will see how well the Lead Consultant expresses complex investment vehicles, philosophies and rationale that everyone can understand, regardless of their investment experience on our Committee.
   3. Could provide interesting questions to inquire of Aon Hewitt as they did not get this assignment.
   4. Making significant changes to existing portfolio is time-consuming and costly (especially in the alternative asset classes). Net, I am interested in this assignment.

2. **ASSET ALLOCATION, INVESTMENT PHILOSOPHY, AND RISK ASSESSMENT QUESTIONS**

a. **Explain how they take a client through the Asset Allocation Process and how often do they recommend that we do it? (Chuck)**

   Purpose of Question: Asset Allocation is the single largest factor in portfolio performance (significantly higher than manager selection). From asking this question we should be able to get a better understanding of the depth of the firm's market research bench and the analytical data/tools they use to make asset allocation recommendations in terms of: (1) current market trends (2) intermediate capital market outlooks, (3) ability to capitalize on inefficient markets and temporary pricing anomalies (i.e. how proactive are they in providing tactical asset allocation recommendations (4) their attention to lowering correlation to other asset classes, and (4) knowledge of the tools they use model expected returns in supporting their asset allocation recommendations.

b. **How do they determine the Risk Tolerance of the Finance & Investment Committee? (Tom Carignan)**

   Purpose of Question: Every Investment Committee member has a different level of tolerance towards risks and temporary losses in the portfolio (i.e. volatility in the portfolio). What we should be listening for is the process they use, **and other factors they consider** in determining the Committee's risk tolerance. Other factors I would like to hear mentioned are in Risk

Tolerance would be consideration of our spending policies and liquidity needs within the portfolio.

3. **INVESTMENT MANAGER SELECTION AND TERMINATION QUESTIONS**

a. **Describe the key factors that would cause you to recommend hiring or terminating an investment manager? (Spence)**

Purpose of Question: We are looking for several things in their manager selection, monitoring and termination process:

(a) their level of investment and maintenance in proprietary database(s) of high conviction investment managers (especially alternative managers).

(b) an understanding how they monitor investment managers on an ongoing basis including: (1) regular due diligence reviews, (2) change in portfolio managers (3) change in investment strategy (e.g. risk monitoring), (4) changes in performance metrics or track record

(c) an understanding of the factors that generally lead to termination of an investment manager in their process of putting managers on their "watch list."

b. **How do you allocate access to investment managers in your database? (Rick)**

Purpose of Question: Access to the best managers are often with smaller boutique managers as opposed to large investment houses (much research has been done in this area). For a foundation our size, the question of how they allocate access to these managers when competing against larger foundation clients could be interesting? For example, if Manager A has $50M in supply for a certain investment strategy, yet NEPC has $150M in demand across all their foundation clients, who gets access to this manager? The answer we would like to hear is that NEPC provides a pro-rata allocation across all their clients who fit this investment strategy. In practice, I suspect the larger, more valuable NEPC clients would get access to this investment manager over their smaller clients, but I would like to hear their answer.

c. **Do you receive any compensation from investment management firms for any reason? (Tom Cranshaw)**

Purpose of Question: To uncover any potential conflicts of interest for receiving compensation from managers that they may recommend.

4. **QUESTIONS FOR THE LEAD CONSULTANT AND FIRM IN GENERAL**

a. **Describe our account size and complexity compared with other accounts that you are managing? (Julia)**

Purpose of Question: To ascertain the lead consultants experience with foundations our size.

b. **Describe why your firm should be selected, specifically what sets your firm apart from other Investment Advisory Firms? (Roy)**

Purpose of Question: Looking for key differentiators in what promises to be a difficult decision.

c. **Please describe related services that your firm can/will provide that would be beneficial to the foundation that are included in your fee? (Jim)**

Purpose of Question: Investment management is what our questions have been focused on to this point. I think it is important to make sure we have access to other support (when needed) that we have become accustomed to with Aon. Examples include:

i. Support with spending policy analysis/modeling.
ii. Opportunities for Committee education

iii. Administrative support to HCF staff in Investment decision execution.

d. **Please describe your firm's philosophy and approach to Mission Related Investing.** **(Bridget)**

Purpose of Question: Mission Related Investing is something the Committee has not considered in the past for a portion of our portfolio. Could be a differentiator based on their philosophy, experience and access to mission related managers for implementation.

APPENDIX B

Summary of Medium Term Views

(taken from AON materials, Section 2, Page 4)

Summary of Medium-Term Views

MTVs are shown against strategic benchmark weights. Fundamental, valuation and near-term columns convey the positives and negatives that build up to the aggregate MTV for an asset class.

	MTV July 2017	MTV June 2017	July 2017 Fundamental	July 2017 Valuation	July 2017 Near Term
Regional Equity / Factor views relative to ACWI Equity					
Global Equity (ACWI)	=	=	=	=	=
US LC Equity	=	=	=	-	=
US SC Equity	=	=	=	-	=
EAFE Equity	+	+	+	+	↓=
EM Equity	+	+	+	+	↓=
Fundamental Indexation (RAFI)	+	N/A	+	+	=
Low Volatility	-	N/A	-	-	=
Quality	=	N/A	=	-	=
High Yield	=	=	=	-	=
Bank Loans	+	+	+	↓=	+
USD EMD	=	=	=	-	=
Local EMD	+	+	+	+	=
Hedge Funds	+	+	N/A	N/A	N/A
Commodities	=	=	=	=	+
Direct Real Estate	=	=	=	=	N/A
IG Credit	-	-	=	-	=
US Government Bonds	--	--	--	-	-
Cash	=	=	=	--	=
USD	=	=	=	-	↑↑++

Key:
"+++++/- - - - -" = max over / underweight, "=" = neutral. Currency "+" scores indicate a stronger USD and "-" scores indicate a weaker USD.
↑ / ↓ = positive /negative change in view or component of view from last update.

APPENDIX C

Summary of Manager Fee Review

(taken from AON materials, Section 5, Page 8)

Manager Fee Review

- The Health Care Foundation of Greater Kansas City requested that AHIC assess the reasonableness of the managers' fees in the program.
- In the following slides, we evaluate the fees of the managers in the Foundation's portfolio.
- We compare each manager's fee to the fees of its respective peer universe:
  - Peer universe will include manager products with similar asset class/style (e.g., Passive U.S. All Cap Equity or Active U.S. Core Plus Fixed Income) and mandate size (based on the 6/30/2017 market value) to the manager product being evaluated
  - Universes are compiled by eVestment, HFR, and NCREIF databases:
    - Utilize eVestment for U.S. equity, international equity, global equity, and fixed income products; HFR for hedge fund products; and NCREIF for real estate manager products
  - We footnote on each slide a description of the peer universe
- For the equity, fixed income, and real estate managers, we rank each manager's fee relative to a peer universe.
  - For example, a percentile rank of 25% indicates that the manager's fee is lower than 75% of the fees in its peer universe.
- For the hedge fund managers, we compare the management and incentive fees separately relative to the industry norms.
- For the private equity managers, we utilize the Preqin survey for the comparative management fee analysis.