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Pension Fund Officer's Position Is in Peril

FINANCE: County Considers Trying Path With Less Risks
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San Diego County's employee pension fund would be better off adopting a safer, more traditional investing model rather than the higher-risk one now in place, said several investment professionals.

Earlier this month, the county's retirement board that oversees the $10 billion pension fund voted 7-2 to consider terminating its contracted chief investment officer Lee Partridge and his firm Salient Partners and appointing an interim consultant at its next meeting, Oct. 2.

The motion was prompted by some board members having misgivings about Partridge's compensation, which exceeds $10 million annually. They also criticized his pay in light of returns that lag those of other public pension funds.

County Supervisor Dianne Jacob, a board member since 2004, said when the county fund's performance is compared with the city of San Diego employee pension fund, the latter had 2 percent higher returns over four years and did so at about half of cost of the county fund.

"Clearly, we are not getting the benefit for the high cost that has been paid out over the last four years," Jacob said.

Several professional money managers said it appears the fund, called the San Diego County Employees Retirement Association, is using unnecessarily higher risk investment strategies that aren't delivering higher returns.

"It seems to me that the risk to the county of a complete loss is something that taxpayers should be worried about," said Stephen Nielander, a partner in HPM Partners, an Orange County firm that manages about $5 billion in assets.

"To me, they're making a major bet with other people's money," said Nielander, who also teaches finance at San Diego State University.

Brent Wilsey, president of San Diego-based Wilsey Asset Management, which manages some $160 million in assets, said SDCERA's use of leverage or borrowing against its assets to boost returns could backfire especially in a severely declining market.

"That's why so many hedge funds went broke — because they were so highly leveraged," Wilsey said. "Leverage is a dirty word."

At earlier SDCERA meetings, Partridge said the leverage strategy was aimed at limiting losses in a down market and that losing all of the fund's money was highly unlikely. However, when pressed, he said the $10 billion fund was totally leveraged to $22 billion.

The county fund's return for the year ended June 30 was 13.43 percent net of fees. That beat the fund's targeted return of 7.75 percent. In contrast, SDCERS, the city employee pension fund, reported an annual return net of fees of 17.3 percent. It has an annual target of 7.25 percent.

Wilsey called the county fund's annual performance "pretty darn good." But he was surprised the fund was leveraged so highly.

While hedge funds have attracted a tremendous amount of institutional money in recent years, those funds' returns have trailed the returns generated by plain-vanilla, low-cost index equity funds have achieved, noted Nielander.

Christina Dileva, spokeswoman for SDCERS, the city pension fund, said the city's fund is not invested in any hedge funds, but one of its holdings does use derivatives. "The fixed income portfolio that is managed by PIMCO does use derivatives to gain market exposure but cannot use leverage," she said.

In addition to considering firing Partridge at its upcoming meeting, another SDCERA board member, Samantha Begovich, said it should also consider terminating its top manager, CEO Brian White, but that idea wasn't included in the agenda item that was approved.

At press time, White hadn't responded to a request for an interview, but through a spokesman said he doesn't comment on personnel matters.

Should the SDCERA board decide to terminate Partridge, it would reverse a path that board has been traveling for the past five years in outsourcing its investment decisions to an outside consultant.

The change followed the resignation of former CIO David Deutsch in 2009 following the stock market meltdown, resulting in the $8 billion fund bleeding by about $2 billion.

In response, the board decided to contract for an investment manager at a Houston firm headed by Partridge, who was then helping to manage the $83 billion Teachers Retirement System of Texas.

In his first year managing SDCERA's investment Partridge's compensation was about $1 million, with the fund's return at 13 percent. The next four years the fund's returns were 20.7 percent, 6.5 percent, 7.73 percent, and 13.4 percent last year.

In June, apparently pleased with how the fund was performing, the board voted to extend the Salient contract to 2019, and increased the management fee by 2 basis points or 0.002 percent to 0.01 percent. When applied to the $10 billion fund, that increased the firm's annual fee from $8 million to $10 million.

In contrast, the four members of the city's pension fund investment team were paid a collective $984,000 in salaries and benefits for the 2013 fiscal year, Dileva said.