To: Members of the FLPS Executive Committee
From: Mike Tavlin, Chair of the FLPS Investment Committee
Date: March 3, 2025
Subject: Recommendation of the FLPS Investment Committee to engage Mercer as Investment Advisor for FLPS and substitute Mercer for D. A. Davidson in that role

Ladies and Gentlemen:

Accompanying this memo are minutes of the January 10, 2025, meeting of the FLPS Investment Committee where that committee recommended the engagement of Mercer as the OCIO investment advisor for FLPS as a substitute for D. A. Davidson in the role of investment advisor. You will note, at the conclusion of those minutes, the bases stated for that recommendation. The purpose of this memo is to provide some additional color, context and perspective to that recommendation.

The principal elements of that recommendation are investment management fees, broad access to more investment resources and opportunities and the investment management team.

<u>Investment Management Expenses</u>

One does not need to read very far or deep into the literature regarding investment management to appreciate the significance of investment management fees and the relationship of investment management fees to portfolio returns. Simply stated, minimizing investment management fees is crucial for maximizing long-term returns. Even seemingly small fees can compound over time, significantly eroding returns and wealth. Warren Buffett has consistently emphasized the importance of minimizing investment management fees. He believes that high fees can significantly erode investor returns over time.

Comparing the proposed investment management fees between D. A. Davidson, Fiducient and Mercer is not something that need be left to speculation. Those fees can be precisely calculated because those firms have precisely disclosed how they would charge for their services.

- D. A. Davidson annual investment management fees a $12 million investment portfolio (the approximate current size/value of the FLPS investment portfolio) are calculated to be $79,200.
- Fiducient annual investment management fees for a $12 million investment portfolio are calculated to comparable to D. A. Davidson.
- Mercer annual investment manage fees for a $12 million investment portfolio are calculated to be $24,000 per year assuming services provided are identical to what D. A. Davidson currently provides and $43,200 per year assuming enhanced OCIO services.
- <u>Annual investment management fee expense savings</u> with Mercer, when compared to D. A. Davidson, would be at least $36,000 (and $55,000 if an OCIO relationship is not selected).
- This amount is a Permanent Annual Difference.

- It would not be surprising for someone to be curious as to whether D. A. Davidson could earn this difference back through investment performance. The likelihood of that happening is possible, but not probable. This is because both Mercer and D. A. Davidson (1) would be using the same Investment Policy Statement as the "playbook" and (2) the asset allocation mix developed in collaboration with the investment manager and the FLPS investment committee would likely take the same or similar risk and reward portfolio construction characteristics into account. Whether asset allocation could be tweaked to reliably or consistently make up this difference is speculation, at best.

Broad Access to More Investment Resources

We seek to preserve the inflation adjusted purchasing power of the assets of the fund over time after giving effect to operating expenses, investment management expenses, programmatic expenses and inflation.

Never confuse brains with a bull market.

Interest rates. Earnings. Inflation. Recession. Politics. War. Climate change. Etc. Etc. Etc. The equity returns of the past two years are unlikely to be soon repeated. Respected forecasts currently predict an investment return for U.S. large cap stocks as a class over the next decade (this category includes companies such as Apple, Meta and Nvidia) in the mid-single digits. Forecast returns for U.S. fixed income for the same period are slightly lower. Forecast 10 year returns for private equity and private debt are higher but with higher volatility. Non-U.S. equity returns are forecast to be slightly higher than for U. S. equities.

The investment world is going to get more, not less, challenging. In order for FLPS to be positioned to consistently achieve its investment goals over time it will be necessary, in the opinion of investment committee members, for FLPS to have ready access to the broadest, deepest possible set of global investment resources and opportunities. The members of the investment committee think that Mercer is best positioned and best qualified to provide ready access to those resources and opportunities for the reasons stated in its proposal.

The Investment Management Team

Committee members were impressed with the members of the Mercer team that would be assigned to FLPS – their backgrounds, qualifications, experiences and commitment to high quality, responsive service. Mercer has a low client to consultant/staff ratio (in the range of 15 to 20 clients per team) compared to D. A. Davidson with more than 40 clients per consultant and Fiducient (with a ratio between Mercer and D. A. Davidson) and a deeper bench. This is important not only in an ongoing sense, but also in the on boarding process. Mercer also has ongoing relationships with other non-profit clients in Lincoln which are expected to facilitate regular communications between FLPS and the Mercer investment team.