Board Report 21-12

Date: March 16, 2021

To: Board of Deferred Compensation Administration

From: Staff

Subject: Stable Value Fund

Recommendation:
That the Board of Deferred Compensation Administration (Board) approve a five-year contract term with Galliard Capital Management to provide Stable Value Fund management services for the Deferred Compensation Plan (DCP) effective January 1, 2022 to December 31, 2027.

Discussion:

A. Stable Value Fund Contract Update

At its meeting on **February 16, 2021**, the Board selected Galliard Capital Management (Galliard) to provide Stable Value Fund management services for the DCP and instructed staff to negotiate and draft a contract in consultation with Board counsel and authorize the Board Chairperson to execute said contract on behalf of the Board, subject to agreement between the City and the provider as to all applicable terms and conditions and all necessary approvals.

Notwithstanding the fact that the Request for Proposal (RFP) specified a contract term for five years, while the Board approved a new contract with Galliard, staff neglected to formally specify the contract term as part of its recommendation. Under Los Angeles Administrative Code (LAAC) Division 10, Chapter 1, Section 10.5, the Board is authorized to enter into contracts with service providers for the DCP for terms of up to five years without City Council approval. A contract term beyond five years requires the approval of the City Council in accordance with LAAC Division 10, Chapter 1, Section 10.5.

Given that the Board historically has entered into five-year contracts for its investment providers, and in the interest of providing for the most efficient use of the Board's and staff's resources, staff recommends that the Board approve a five-year contract term with Galliard to provide

Stable Value Fund management services for the DCP effective January 1, 2022 to December 31, 2027.

B. Galliard Ownership Change

On February 23, 2021, staff received notice of an announcement from Galliard regarding Wells Fargo's sale of their asset management business (**Attachment A**). Staff reviewed this change with the Board's investment consultant, Mercer, which has prepared a review/analysis of the sale (**Attachment B**). A summary of the information provided by Galliard and additional analysis from Mercer is provided below:

- On February 23, 2021, Wells Fargo announced that GTCR LLC and Reverence Capital Partners, L.P., both private equity firms, have agreed to acquire Wells Fargo Asset Management (WFAM) for $2.1 billion. The transaction includes Galliard Capital Management (subsidiary of WFAM) which is expected to remain as a semi-independent operating unit within the broader asset management division. Wells Fargo will continue to own a 9.9% equity interest. The sale transaction is expected to close during the second half of 2021. Upon the close of the transaction, WFAM will be rebranded.
- Nico Marais will continue as Chief Executive Officer (CEO) of WFAM. Mr. Marais will also be a member of an eleven-member board, which will consist of Executive Chairman Joseph Sullivan (former chairman and CEO of Legg Mason), three members from each of GTCR and Reverence, and three independent members. The current Galliard investment and management team is expected to remain fully intact.
- Mercer's research view is that this change in ownership presents both opportunities along with uncertainties. On the positive side, Galliard appears to be maintaining its independence and personnel while perhaps improving its branding and resources for growing its business and positioning itself to lower fees. The uncertainties lie in integration with the new owners and their long-term commitment to the acquisition, personnel, and investments in growing the business.

Mercer and Galliard representatives will be present at the Board meeting to provide further details and address any questions from the Board.

Submitted by: ____
Steven Montagna, Chief Personnel Analyst

GALLIARD
Capital Management, Inc.

ARCHITECTS OF INVESTMENT SOLUTIONS

WELLS FARGO ASSET MANAGEMENT TO BE ACQUIRED BY GTCR AND REVERENCE CAPITAL PARTNERS

February 23, 2021

Earlier today, Wells Fargo announced it had reached a definitive agreement for GTCR LLC and Reverence Capital Partners, L.P. to acquire Wells Fargo Asset Management (WFAM). This transaction includes Galliard Capital Management as well as Wells Fargo Funds Management, LLC; Wells Capital Management Inc.; Wells Fargo Asset Management (International) Ltd.; Wells Fargo Asset Management Luxembourg S.A.; and Wells Fargo Funds Distributor, LLC. In addition, Wells Fargo Bank N.A.'s collective investment trust (CIT) trustee business is also part of the transaction.

The strategic partnership between GTCR and Reverence Capital, both well-respected private equity firms with deep experience investing in asset managers, will allow WFAM to operate as an independent firm dedicated solely to the asset management service of institutional, retirement, and wealth management clients around the world. This acquisition will provide WFAM the capital, resources, and autonomy to better serve clients and to expand and deepen thought leadership across the organization, while keeping a singular focus on delivering consistent and repeatable investment performance.

As you may be aware, Galliard reports to Nico Marais, chief executive officer of WFAM. Nico stated, "We are excited about this transaction and believe it will allow us to accelerate our ability to execute on our strategy and commitment to provide our clients with innovative products and solutions to help them reach their investment goals. GTCR and Reverence Capital have a track record of growing businesses for the long term, and they are committed to investing in our business with the resources necessary to better serve our clients and optimize their investment outcomes."

All of us here at Galliard, as well as the leadership team at WFAM, are tremendously motivated by the announcement, recognizing that this combined partnership represents the following:

- A commitment to providing resources and expertise that will further enhance Galliard's and WFAM's other investment teams' ability to be agile, independent, and innovative partners to seek to meet the diverse needs of clients today and in the future

- The ability to more effectively transition to our operational and technology “platform of the future,” enabling WFAM (and Galliard) to be at the forefront of digital innovation

The transaction is expected to close in the second half of 2021, subject to customary closing conditions. Under the terms of the agreement, the purchase price is $2.1 billion. As part of the transaction, Wells Fargo will own a 9.9% equity interest and will continue to serve as an important client and distribution partner.

In addition, with this change of ownership, it was announced that Joseph A. Sullivan, former chairman and CEO of Legg Mason, will be elected Executive Chairman of the Board of the new company, effective following the closing of the transaction. He will bring a strong leadership background and more than 40 years of industry experience to help drive the company’s strategy forward.

ABOUT GTCR
Founded in 1980, GTCR LLC is a leading private equity firm focused on investing in growth companies in the health care, financial services & technology, technology, media & telecommunications, and growth business services industries. The Chicago-based firm pioneered The Leaders Strategy? ? finding and partnering with management leaders in core domains to identify, acquire, and build market-leading companies through transformational acquisitions and organic growth. Since its inception, GTCR has invested more than $20 billion in over 250 companies. For more information, please visit www.gtcr.com

ABOUT REVERENCE CAPITAL PARTNERS
Reverence Capital Partners, L.P. is a private investment firm focused on thematic investing in leading global, middle-market financial services businesses through control and influence-oriented investments in five sectors: 1. depositories and finance companies, 2. asset and wealth management, 3. insurance, 4. capital markets, and 5. financial technology/payments. The firm was founded in 2013 by Milton Berlinski, Peter Aberg, and Alex Chulack, who collectively bring over 90 years of advisory and investing experience across a wide range of financial services sectors. For more information, please visit www.reverencecapital.com.

We do not anticipate changes to the Galliard brand, our investment process and team, or your client experience as a result of this sale. Your relationship managers will be reaching out in the coming days to provide additional details on this exciting news.

In the meantime, please know it is business as usual here at Galliard and we continue to navigate the financial markets. We are excited for what the future has to offer and we’re looking forward to sharing the updates with you as this deal works towards closing.

Ajay Mirza, Mike Norman, Andrew Owen
Senior Managing Principals

MERCER

On the whole, the recently announced news of Wells Fargo Asset Management's sale to two private equity firms appears promising though there are several areas we will continue to examine as the transaction moves towards and beyond closing. This announcement does not come as a major surprise, as broader organizational challenges faced by Wells Fargo in recent years have made the potential sale of WFAM a likely outcome. While the ownership change does create some uncertainty for Galliard, it creates a fresh path forward for the business. The new owners can focus solely on growth of all WFAM boutiques including Galliard, without needing to also worry about the extensive regulatory and management ramifications attached to a global systemically important bank, such as Wells Fargo.

Importantly, Galliard is expected to remain as a semi-independent operating unit within the broader asset management division. Galliard expects to remain in control of its investment team, process, client service, and distribution efforts. The revenue sharing agreement between the WFAM level and Galliard is expected to remain in place. Additionally, Mercer was happy to hear that Galliard management was involved in discussions with GTCR and Reverence during the due diligence phase of the acquisition. Galliard management walked away from those discussions with the view that their new owners are not intent on cutting expenses and trimming operational excess, but rather, are approaching their new investment with a growth-focused mindset, while recognizing the importance of the people within the businesses that was acquired. They expect a major focus to be placed on further developing marketing/distribution/sales at the Galliard level. An emphasis has also been placed on operational and technology enhancements. Further, and perhaps more importantly for the City, the transaction provides an opportunity for Galliard to have more control over the evaluation of certain services and costs previously provided by the Bank such as trust and custody services for their collective funds. If these themes play out over time, we believe the ownership change will be a positive development for Galliard and its clients longer-term.

Regardless of our optimism, in circumstances like this, Mercer assigns a Watch (W) designation to all affected strategies of a firm (in this case all WFAM and Galliard strategies). We intend to maintain the Watch status at least through the transition period. Mercer will continue to meet with Galliard throughout the transition and subsequent integration, and will provide additional updates as needed. In our meetings, we will examine what we envision the obvious pros/cons associated with WFAM's announcement detailed in the following table. We will keep the Board apprised of material findings along the way.

Pros	Cons
• The Galliard senior leadership team has been in touch with the management of the new parent company. Galliard has been given every indication that it will be left alone to manage its stable value and fixed income businesses independent from the legacy WFAM unit.	• As with any acquisition, there is uncertainty with cultural and operational integration. It is possible that GTCR and Reverence stop collaborating in the future, and/or change plans, which can add to uncertainty around Galliard's strategic direction.

• The Wells Fargo Stable Return Fund, which accounted for almost a third of Galliard managed stable value assets as of 3Q20, will be renamed (possibly as Galliard Stable Return Fund), which should improve Galliard's brand visibility. • Galliard will distance itself from the negative headlines surrounding its current parent company, which has caused angst among current and prospective clients. • It is possible that Galliard will be able to lower fees for some of its collective trust strategies by eliminating the fee portion currently being paid to Wells Fargo. • Galliard mentioned that the new parent is focused on growth. Galliard is likely to get financial support for growing its fixed income and stable value business and have more resources for distribution channels.	• A number of questions and uncertainties exist going forward: ○ Given their new owners are private equity investors, what is the time horizon for GTCR and Reverence? Another potential ownership event will likely be an ongoing question mark in the next five to ten years. ○ Will Galliard maintain its current level of independence, as expected at the time of the deal? Or, will the new owners change course and seek greater expense savings if initial growth aspirations do not go as planned? ○ Will the Galliard teams and investment processes be asked to integrate with legacy WFAM teams/processes in pursuit of scalability? ○ Will Galliard be able to retain its key employees, despite the elevated uncertainty and potential for changes? ○ Will the ownership change cause a distraction to the Galliard team and impact the quality of investment results and/or service that clients have come to expect?

Important Notices

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Risk warnings

- The value of stocks and shares, including unit trusts, can go down as well as up and you may not get back the amount you have invested.
- The value of Gilts, bonds, and other fixed income investments including unit trusts can go down as well as up and you may not get back the amount you have invested.
- Investments denominated in a foreign currency will fluctuate with the value of the currency.
- The value of investments in real estate can go down as well as up, and you may not get back the amount you have invested. Valuation is generally a matter of a valuer's opinion, rather than fact. It may be difficult or impossible to realise an investment because the property concerned may not be readily saleable.
- Certain investments, such as illiquid, leveraged or high-yield instruments or funds and securities issued by small capitalization and emerging market issuers, carry additional risks that should be considered before choosing an investment manager or making an investment decision.
- For higher volatility investments, losses on realisation may be high because their value may fall suddenly and substantially.

Where investments are not domiciled and regulated locally, the nature and extent of investor protection will be different to that available in respect of investments domiciled and regulated locally. In particular, the regulatory regimes in some domiciles are considerably lighter than others, and offer substantially less investor protection. Where an investor is considering whether to make a commitment in respect of an investment which is not domiciled and regulated locally, we recommend that legal advice is sought prior to the commitment being made