



# Investment Committee

## Item Number 4b – Open Session

**Subject:** Collaborative Model Savings Report

**Presenter(s):** April Wilcox, Shifat Hasan, Mike Dunigan

**Item Type:** Information

**Date & Time:** November 3, 2022 – 15 minutes

---

**Attachment(s):** Attachment 1 – Scope and Methodology

Attachment 2 – Savings per Asset Class

**PowerPoint(s):** Collaborative Model Savings Report

---

### **Item Purpose**

To enhance the annual cost reporting by providing defined metrics around savings from the CalSTRS “Collaborative Model.”

### **Executive Summary**

The Collaborative Model is an internally led approach to how CalSTRS engages in the investment marketplace. It is an investment strategy to manage more assets internally - to reduce costs, control risks and increase expected returns - and leverage our external partnerships to achieve similar benefits. CalSTRS embraces partnership and collaboration with world-class investment institutions, along with building internal (or ‘direct’) investing capabilities to achieve the benefits of internally managed assets. The Collaborative Model covers a spectrum of different types of investment strategies and investment ownership structures from simple to very complex. This report aims to quantify the savings achieved from the implementation of this strategy.

### **Background**

This report includes 266 collaborative private investment structures, 56 internally managed funds, and 2 rebate agreements that contributed to collaborative savings results as of 2021 and identifies the savings to the Total Fund on a per year basis going back to 2017. Though internal management and investment types like co-investments were around prior to this date, it is used as the starting point for tracking as it correlates to the 2017 workplan project around direct

investing and an allocation shift toward increased private investing, both in committed capital and the number of deals.

**Chart 1 – Collaborative Assets Under Management with Savings<sup>1</sup>**

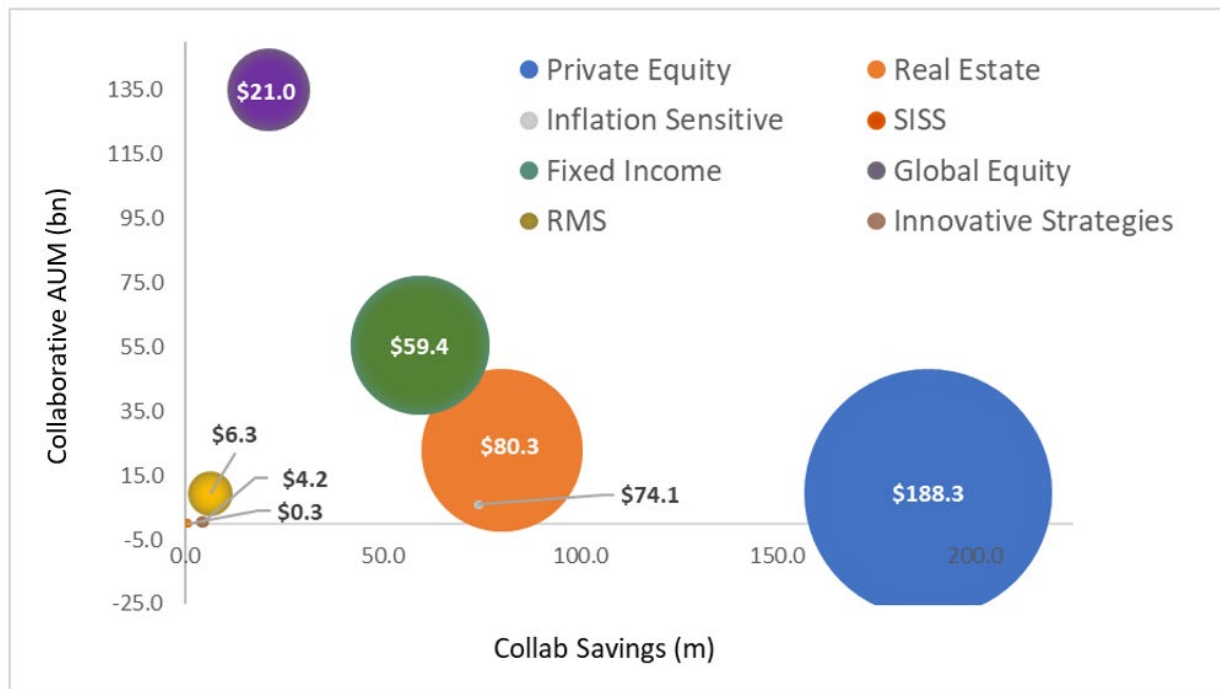


Chart 1 above shows the amount of collaborative assets under management relative to their collaborative savings for each asset class as of the end of the 2021 calendar year. The higher on the chart, the more assets under management. The larger the size of the bubble, or the further to the right of the chart, the more savings.

Of the collaborative components, Private Equity has the highest collaborative savings with one of the lowest collaborative assets under management at roughly \$188 million saved for calendar year 2021. A similar savings to assets under management (AUM) ratio extends to the other private assets like Real Estate and the private portion of Inflation Sensitive. Private assets in general will have the greatest opportunity for savings given their fees are higher, but the potential carried interest savings is where the largest impact of the Collaborative Model will be seen.

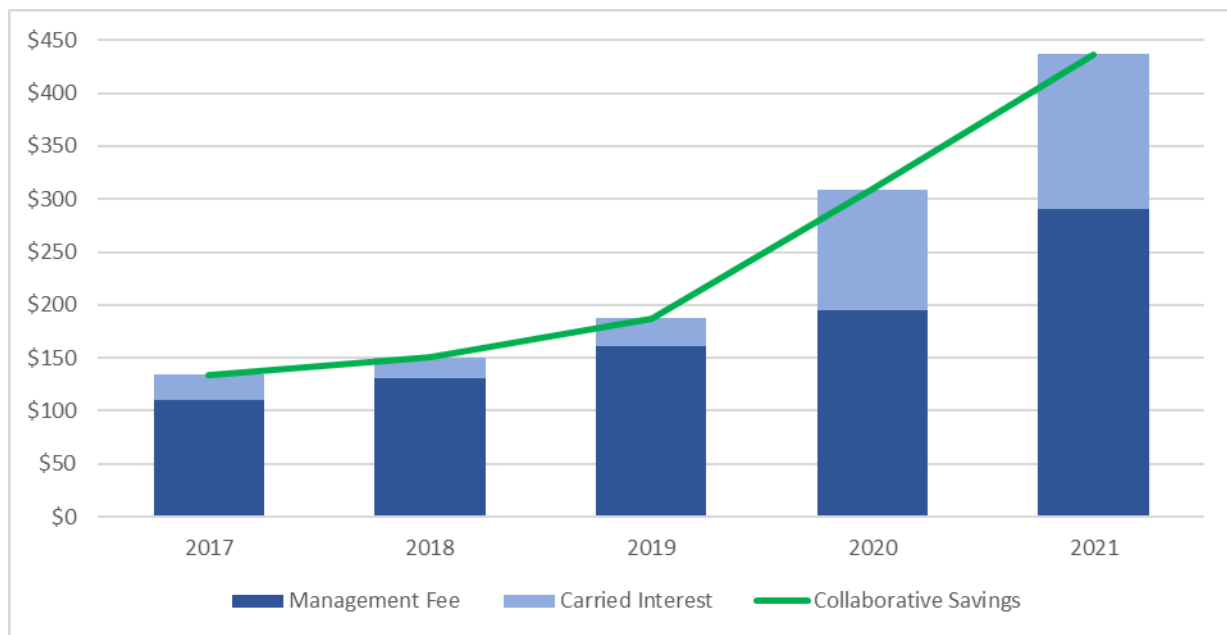
The number of private investment structures increased by 110 from the initial year of the model. The majority of this came from new 2021 vintage year investments or previous vintage year investments that had not been funded – including 53 new co-investments. The remaining includes structures that fit the criteria but were not captured previously due to missing terms or zero impact on savings. The scope and methodology for the collaborative savings calculation is provided in attachment 1.

<sup>1</sup> Fixed Income includes \$25.8 billion in assets managed for the liquidity and securities lending programs

### Collaborative Savings Results

As shown in Chart 2 below, CalSTRS has saved over \$1.2 billion since 2017, with an average annual savings of \$243.6 million. The savings in management fees and carried interest has increased each year as the number of collaborative components has increased. This annual savings number will increase or decrease variably over time based on the amount of carried interest paid out in a given year and the number of collaborative components.

**Chart 2 – Overall Savings per Year (\$ Millions, since 2017)**



(\$ millions)	2017	2018	2019	2020	2021	Total 5 Yr Savings
<b>Collaborative Savings</b>	<b>134.4</b>	<b>150.6</b>	<b>187.2</b>	<b>308.9</b>	<b>437.0</b>	<b>\$1,218.0</b>
<b>Management Fee</b>	<b>110.8</b>	<b>130.2</b>	<b>161.4</b>	<b>195.3</b>	<b>290.5</b>	
<b>Carried Interest</b>	<b>23.6</b>	<b>20.3</b>	<b>25.8</b>	<b>113.5</b>	<b>146.4</b>	
<b>Component Count</b>	106	140	167	200	324	

The collaborative components (investment types) were outlined in the model’s scope (see attachment 1). Their savings are generated from different combinations of management fees and carried interest. Joint Ventures, Separate Accounts and Managed Accounts often have reduced fee and carried interest expenses. Internally managed public funds generate their savings from the elimination of management fees. Co-investments predominantly have zero management fees and carried interest. Chart 3 below outlines the savings results broken down by investment type.

**Chart 3 – Savings per Investment Type (\$ Millions)**



As shown in the chart above, internally managed funds and co-investments have provided the greatest amount of savings over this time. Internally managed funds are compared against public managers with low fee structures, so the savings is derived significantly from the AUM. Private investments tend to have higher fee structures, so even with less invested, there can be significant savings in management fees. Co-investments, with their aggressively reduced fee structures (often zero fees and carry), will often reflect the greatest amount of savings in periods after bull markets when profits are realized without having to share profits with a General Partner (carried interest savings). This was evident the past two years, after multiple years of positive market returns, where co-investment savings accounted for over half of the Total Fund’s savings. In 2021, co-investments across the private asset classes saved \$221.7 million, with \$94 million of that coming from carried interest.

**Chart 4 – Savings per Asset Class (\$ Millions, since 2017)**

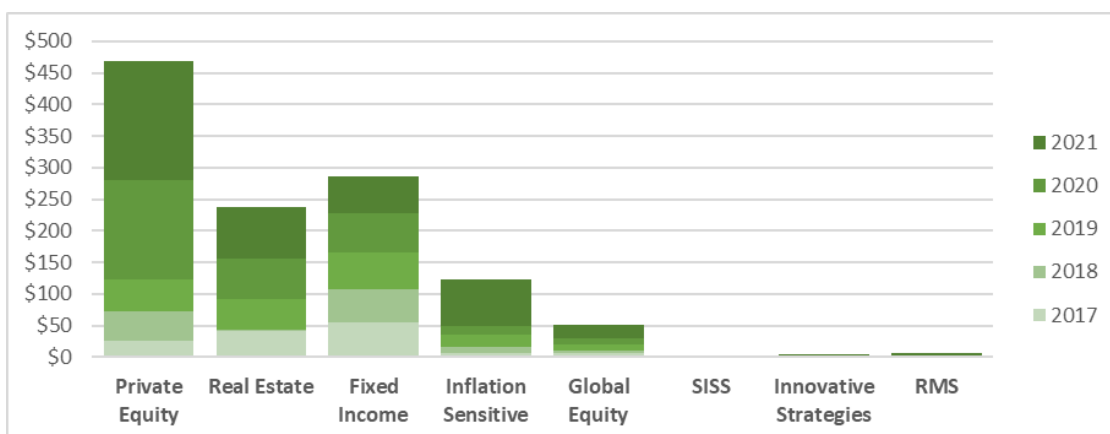


Chart 4 reflects the contributed savings per each asset class over the last five years. A complete breakdown of the dollars saved per asset class and investment type, broken out by management fees, and carried interest, is available in Attachment 2. An excerpt for 2021 is shown here.

Over the 5-year period (Chart 4), Private Equity has contributed the most savings, with Fixed Income internally managed funds having contributed the second most savings over this time. Private assets in general, though, have begun to outpace the public savings over the last two years because of carried interest savings.

Table 1 below estimates the impact the Collaborative Model had on each of the asset classes listed. The savings earned by reducing costs had a direct impact to the dollars earned (dollar return) over 2021. Removing this savings from the dollar return reduced each asset class return as shown in the table below.

(\$ Millions) Asset Class	2021	
	Management Fee	Carried Interest
<b>Private Equity</b>	<b>\$97.8</b>	<b>\$90.5</b>
Co-Investments	\$97.8	\$90.5
<b>Real Estate</b>	<b>\$62.3</b>	<b>\$17.9</b>
Co-Investments	\$9.9	\$3.4
Joint Ventures	\$28.9	\$11.6
Separate Accounts	\$23.5	\$2.9
<b>Inflation Sensitive</b>	<b>\$36.6</b>	<b>\$37.5</b>
Co-Investments	\$15.6	\$0.0
Internally Managed	\$1.3	\$0.0
Managed Accounts	\$19.8	\$37.5
<b>SISS</b>	<b>\$0.3</b>	<b>\$0.0</b>
Co-Investments	\$0.3	\$0.0
<b>Fixed Income</b>	<b>\$59.4</b>	<b>\$0.0</b>
Internally Managed	\$59.4	\$0.0
<b>Global Equity</b>	<b>\$21.0</b>	<b>\$0.0</b>
Internally Managed	\$21.0	\$0.0
<b>Innovative Strategies</b>	<b>\$4.2</b>	<b>\$0.0</b>
Co-Investments	\$4.2	\$0.0
<b>RMS</b>	<b>\$6.3</b>	<b>\$0.0</b>
Internally Managed	\$6.3	\$0.0
<b>Rebate Agreements</b>	<b>\$2.7</b>	<b>\$0.5</b>
<b>Total Savings</b>	<b>\$290.5</b>	<b>\$146.4</b>

**Table 1 - Collaborative Savings Impact on 2021 Returns (\$ Millions)**

Asset Class	Net Dollars Earned	Collaborative Dollars Saved	2021 Return	Return with Savings Removed	Excess Return Added	
<b>Total Portfolio</b>	<b>\$47,553.1</b>	<b>\$437.0</b>	<b>16.93%</b>	<b>16.78%</b>	<b>0.16%</b>	
<b>Growth</b>	Global Equity	23,249.4	21.0	18.07%	18.06%	0.02%
	Private Equity	14,216.2	188.3	47.78%	47.14%	0.63%
	SISS	1,754.9	0.3	18.39%	18.39%	0.00%
<b>Real Assets</b>	Real Estate	5,404.2	80.3	14.82%	14.59%	0.22%
	Inflation Sensitive	2,197.9	74.1	19.94%	19.27%	0.67%
<b>Diversifying</b>	Fixed Income	-321.8	59.4	-0.95%	-1.13%	0.18%
	RMS	1,277.3	6.3	4.82%	4.80%	0.02%
	Innovative Strategies	231.9	4.2	15.34%	15.06%	0.28%

In 2021, the Collaborative Model saved the Total Fund roughly \$437 million, adding an estimated 0.16% (16 basis points) to the 2021 net return.

---

Strategic Plan Linkage: [Goal 1 of the strategic plan](#). Trusted stewards – Ensuring a well-governed, financially sound trust fund.

Board Policy Linkage: [CalSTRS Investment Policy and Management Plan](#)

---

**Optional Reference Material:** *(e.g., prior board items, supplemental educational materials, etc.)*