CALSTRS

Investment Committee

Item Number 3 – Open Session

Subject: Investment Policy & Management Plan Revision – Asset Allocation – First Reading

Presenter(s): Geraldine Jimenez

Item Type: Action

Date & Time: July 7, 2022 – 20 minutes

Attachment(s): Attachment 1 – Meketa Investment Group Concurrence Memo
Attachment 2 – Investment Policy and Management Plan – Redline Version
Attachment 3 – Investment Policy and Management Plan – Clean Version

PowerPoint(s): None

POLICY

The Trust Fund's asset allocation is governed by the CalSTRS Investment Policy and Management Plan (IPMP)**.** As the overarching policy document for the Investment Branch, the IPMP begins with CalSTRS Investments Beliefs then presents the framework for meeting CalSTRS' objectives including the current Strategic Asset Allocation Long Term Policy Targets.

PURPOSE AND HISTORY

The purpose of this policy change is to adjust the liquidity requirement and the asset class weightings to continue moving toward the long-term strategic asset allocation weights.

The Investment Committee conducts an Asset Liability Management (ALM) study every four years. The 2019 study was completed at the November meeting when the Investment Committee selected new long-term asset allocation targets. Those new long-term targets and the Implementation Plan with Step shifts to the portfolio were adopted into the Board's Investment Policy and Management Plan at the January 2020 meeting. This item is being presented to shift the liquidity requirement and the Asset Allocation Targets and Policy Benchmark to a modified Fourth Step of the implementation plan.

If approved the changes would be effective as of July 1, 2022.

BACKGROUND & DISCUSSION

After the Committee approved the new long-term asset allocation targets at the January 2020 meeting, it included a course to shift from the January allocation to the new long-term targets over a series of Steps. CalSTRS has learned from experience that setting a rigid timeline is inefficient as investment opportunities ebb and flow and do not follow a calendar time frame. Therefore, the implementation plan is expressed in "Steps" toward the long-term target. With the COVID-19 global pandemic, we have seen significant volatility on the global financial markets and volatility in market valuations across the portfolio. The portfolio continues its path toward its long-term targets away from the public markets towards private markets with less liquidity.

As a result, staff is recommending the Committee shift to a modified Step 4 in the Implementation Plan. The specific changes are:

- Increase Real Estate target weight by 1% to 15%. This step will put it at its long-term target.
- Increase Inflation Sensitive target weight by 1% to 5% as it paces to its long-term target of 6%. Staff expect to meet this 6% target by December 2022, in advance of the start of the next ALM study.
- Decrease Public Equity by 2% to fund these increases.

For today's recommended Step, The Total Fund benchmark will automatically adjust with the new asset allocation for performance measurement purposes since it comprises each of the respective asset classes' benchmarks weighted by that period's policy target asset allocation.

The Table 2 below shows the recommended Implementation Plan and the final Step in the process.

Table 2: The Implementation Plan

Strategic Class	Asset Class/Strategy	Effective Date 7/1/2020 Step 1	Current Target 7/1/2021 Step 2	Effective Date 1/1/2022 Step 3	Effective Date 7/1/2022 Step 4	Long-Term Target
Economic Growth	Public Equity	49%	47%	45%	43%	42%
	Private Equity	10%	11%	13%	13%	13%
Real Assets	Real Estate	14%	14%	14%	15%	15%
	Inflation Sensitive	3%	4%	4%	5%	6%
Diversifying	Innovative Strategies	0%	0%	0%	0%	0%
	Risk Mitigating Strategies	9%	10%	10%	10%	10%
	Fixed Income	13%	12%	12%	12%	12%
	Cash / Liquidity	2%	2%	2%	2%	2%
	Total Asset Allocation	**100%**	**100%**	**100%**	**100%**	**100%**

Liquidity Limit Update

Additionally, the IPMP includes an update to the liquidity risk limit. The proposed increase from 40% to 50% maximum illiquid assets is in line with the shift to more illiquid assets in the strategic asset allocation. During the next ALM study, staff will incorporate more discussion and analysis of liquidity management and limits in the strategic asset allocation.

Policy Modernization Update

In an effort to modernize, synthesize, and restructure investment policies to best in class, staff began a peer review of Investment Policy Statements and will be bringing a revised IPMP to the Investment Committee for discussion and consideration. Since much of the IPMP is dedicated to the ALM study and the resulting strategic asset allocation, integrating an IPMP modernization project into the ALM timeline is ideal. Table 3 shows the ALM study schedule, including the IPMP review.

Table 3: Tentative Policy Review and ALM study timeline

Meeting	Topic
November 2022	Annual Review of Funding Levels & Risks (Actuaries)
	Review mapping of IPMP to proposed IPS Policy
January 2023	Introduction to the Asset Allocation Project
	Review proposed IPS Policy (formerly IPMP)
March 2023	Discussion of Investment Categories: Portfolio Role (growth, liquidity, diversification, etc.)
	Review IPS (formerly IPMP)
May 2023	Adopt Capital Markets Assumptions
	Review Annual Actuarial Valuations (Actuaries)
	IPS (formerly IPMP) Final Reading
July 2023	Approve Portfolio Constraints
September 2023	Consider Strategic Policy Portfolio with Funding Risks
November 2023	Approve Strategic Policy Portfolio
	Annual Review of Funding Levels and Risks (Actuaries)
January 2024	Present updated IPS with New Asset Allocation Incorporated
	Adopt Experience Study, Actuarial Assumptions (Actuaries)
May 2024	Review Annual Actuarial Valuations (Actuaries)

RECOMMENDATION

Staff and the consultant, Meketa, recommend the Investment Committee adopt the revised IPMP with the new Steps in the asset allocation targets, the liquidity constraint change and implement these changes effective as of July 1, 2022. The specific changes are:

- Increase the Real Estate target weight by 1%.
- Increase the Inflation Sensitive target weight by 1%.
- Decrease the Public Equity target weight by 2%.
- Increase the maximum policy limit for illiquid assets to 50%.