INVESTMENT POLICY MANAGEMENT PLAN – ASSET ALLOCATION– FIRST READING

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

ITEM PURPOSE

The purpose of this item is to request the Investment Committee approve the:

1. Adoption of the long-term strategic asset allocation approved in May 2023 into policy and an implementation plan to adjust the asset class weightings to move toward the long-term strategic asset allocation weights.
2. Illiquidity threshold of the total fund to be at 55% (currently 50%) to align with the new strategic asset allocation ranges.
3. Allocation of all investment asset classes for the Cash Balance Benefit Program.

The Investment Committee conducts an Asset Liability Management (ALM) study every four years. The 2023 study was completed at the May meeting when the Investment Committee selected the new long-term strategic asset allocation targets. This new strategic asset allocation and its implementation plan is reflected in Attachment 2 – the redline version of the Investment Policy and Management Plan (IPMP). This item is also requesting to shift the Asset Allocation Targets and Policy Benchmark to the first step of the implementation plan effective July 1, 2023.

RECOMMENDATION

1. Staff and the consultant, Meketa, recommend the Investment Committee adopt the revised Asset Allocation targets, the implementation plan in table 1 and the shift to the first step effective as of July 1, 2023. The specific changes in the first step are:
   - Increasing the Private Equity target weight by 1%.
   - Decreasing the Public Equity target weight by 1%.

2. Staff and Meketa, also recommend the Investment Committee approve the new illiquidity threshold of 55%.

3. Additionally, staff and Meketa recommend the Investment Committee approve the allocation of all investment asset classes to the Cash Balance Benefit Program.

BACKGROUND

Asset Allocation and Implementation Plan

The Committee approved the new long-term asset allocation targets at the May 2023 meeting. Staff is now also presenting the course to start shifting the current portfolio towards 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.

Today staff is recommending the Committee shift to its first step towards the new long-term strategic allocation targets. Any move to the subsequent steps will be brought forward to the committee for approval at the appropriate time.

The specific changes are increasing Private Equity target weight from 13% to 14% while decreasing Public Equity by 1% to fund this increase.

The Table 1 below shows the recommended Implementation Plan and the first step in the process.

Table 1: The Implementation Plan

Strategic Class	Asset Class/Strategy	Current Target	Effective Date 7/1/2023 Step 1	Effective Date 7/1/2024 Step 2	Effective Date 7/1/2025 Step 3	Effective Date 7/1/2026 Step 4	Long-Term Target
Economic Growth	Public Equity	42%	41%	40%	39%	38%	38%
	Private Equity	13%	14%	14%	14%	14%	14%
Real Assets	Real Estate	15%	15%	15%	15%	15%	15%
	Inflation Sensitive	6%	6%	6%	6%	7%	7%
Diversifying	Innovative Strategies	0%	0%	0%	0%	0%	0%
	Risk Mitigating Strategies	10%	10%	10%	10%	10%	10%
	Fixed Income	12%	12%	13%	14%	14%	14%
	Cash / Liquidity	2%	2%	2%	2%	2%	2%
	Total Asset Allocation	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**

Illiquidity Threshold

With the adoption of the new asset allocation, the illiquidity threshold of the total fund needs to be revised for proper alignment with the implementation plan. The current asset allocation allows for a 50% illiquidity threshold and with the adoption of the new asset allocation, a 55% illiquidity threshold is more aligned with the long-term targets.

Cash Balance Benefit Program

The Teachers' Retirement Fund, which is the primary trust fund through which CalSTRS operates, is comprised of the Defined Benefit Program, the Supplemental Benefit Maintenance Account, the Defined Benefit Supplement Program and the Cash Balance Benefit Program. All programs are invested together, except the Cash Balance Benefit Program has not been invested in the private equity and real estate asset classes since the 1990s when the program was initially created. The CalSTRS Board made that decision over concerns related to cash flows and a desire to avoid investing in less liquid assets. Staff from Investments, Financial Services and Actuarial Resources recommended including the Cash Balance Benefit Program into the 2023 ALM Study and adopting this new the long-term asset allocation mix, including private equity and real estate asset classes, for the Cash Balance Benefit Program. A board action is required to make this change and apply all asset classes for investing the Cash Balance Benefit Program.

Per the 6/30/2022 audited financial statements, the total value of assets reported under for the Cash Balance Benefit Program was $437M.

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

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

May 4, 2023 Investment Committee: 2023 ALM; 2023 ALM Study Discussion

July 7, 2022 Investment Committee: Investment Policy and Management Plan Revision - Asset Allocation - First Reading