CalSTRS Investment Beliefs

Legal Framework

Under California Constitution, Article 16, Section 17, and the California Education Code, Part 13 Teachers Retirement Law, Chapter 4, Section 22250:

The board has plenary authority and fiduciary responsibility for investment of moneys of the retirement system, and the sole and exclusive fiduciary responsibility over the assets of the retirement system. The board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the members and their beneficiaries.

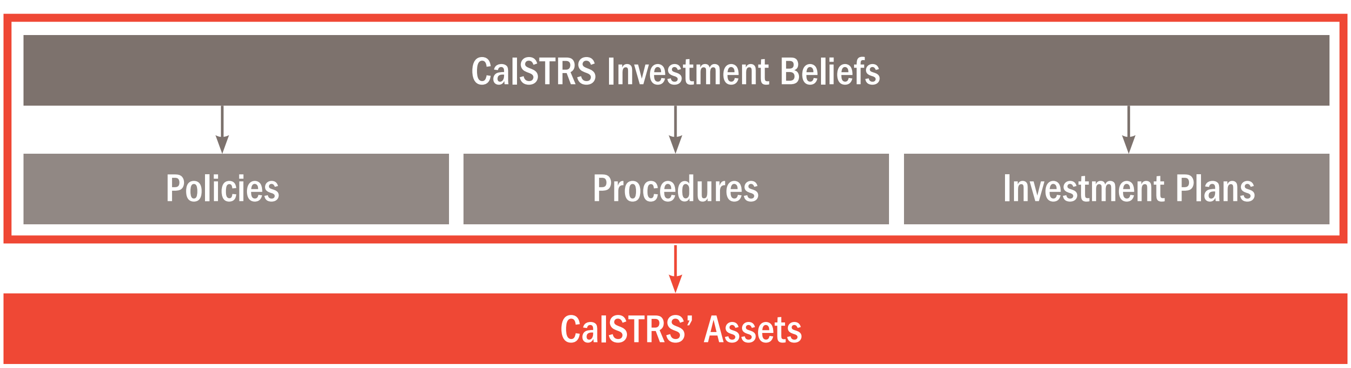
The assets of the retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries, minimizing employer contributions, and defraying reasonable expenses of administering the system.

The board shall discharge its duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims. The board shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

The board's duty to its members and their beneficiaries shall take precedence over any other duty.

Preamble

Consistent with these Constitutional and statutory prescriptions, CalSTRS has broad discretion over the investment of the assets of the fund. These Investment Beliefs provide a foundational framework for all of CalSTRS' investment decision-makers to invest in a manner that reflects CalSTRS' unique view of the global investment markets and its vision for participating in these markets to accomplish its fiduciary goal. In this respect, these Investment Beliefs should help guide CalSTRS' policy leaders and other decision makers to develop appropriate policies, procedures, and investment plans for CalSTRS' assets.



Belief Statements

CALSTRS

Belief 1 **Diversification strengthens the fund.**	Diversification improves the risk-adjusted profile of an investment portfolio.
Belief 2 **The Global public investment markets are largely, but not completely, efficient.**	Historically, a large percentage of the CalSTRS portfolio has been passively or semi-passively managed, approximately 80% of which are publicly-traded assets. In today's internet era, in the major market segments, information is processed rapidly at very low cost and acted upon quickly by millions of market players, making it very difficult to add value. However, there are certain segments of the markets where information processing is more challenging and costly. In these areas astute and well-resourced investors, such as CalSTRS, can utilize unique investment styles and methods to generate net-of-fee returns in excess of those available to a passive buy-and-hold market exposure.
Belief 3 **Managing investment costs yields long-term benefits.**	Investment costs, if not managed appropriately, can have a significant (rather than frictional) impact upon overall portfolio performance. CalSTRS, as a large-scale investor, should focus on measuring, monitoring, and minimizing all relevant investment costs.
Belief 4 **Internal management is a critical capability.**	In contrast to other investors, CalSTRS commands significant resource flexibility and ability to execute its investment activities internally. Where feasible, CalSTRS should utilize internal management to best harness and direct its resources.
Belief 5 **CalSTRS can potentially capture an illiquidity risk premium.**	Illiquid investments offer investors a return premium due to the inability to quickly buy, sell or convert them to cash as quickly as liquid or freely traded assets. CalSTRS believes it can capture this risk premium by investing in real estate, private equity and other similar assets.
Belief 6 **Managing short-term drawdown risk can positively impact CalSTRS' ability to meet its long-term financial obligations.**	As a system, CalSTRS is in a deficit funding position , experiencing ongoing negative cash outflows as benefits paid out exceed contributions received during a fiscal year. Given this status, the system is particularly sensitive to periods when its investments produce negative returns. In such situations, CalSTRS may be required to sell assets—due to its negative cash outflow status—when asset values are declining. In contrast, plans that exhibit positive cash inflows can purchase at a discount during such periods. As a result of this sensitivity, periods of significant negative asset returns will actually impair CalSTRS' chances of achieving its long-term funding objectives, even assuming investment markets recover in later periods. Therefore, CalSTRS must attentively manage short-term drawdown risk when developing the long-term asset allocation and when shifting or rebalancing the portfolio.
Belief 7 **Responsible corporate governance, including the management of environmental, social and governance (ESG) factors, can benefit long-term investors like CalSTRS.**	CalSTRS believes that, in addition to traditional financial metrics, timely consideration of material environmental, social, and governance (ESG), factors in the investment process for every asset class, has the potential, over the long-term, to positively impact investment returns and help to better manage risks. Proxy rights attached to shareholder interests in public companies are additional "plan assets" of the system. As a largely long-term investor, CalSTRS can enhance the value of its plan assets by taking a leadership role through voting proxies.
Belief 8 **Alignment of financial interests between CalSTRS and its advisors is critical.**	In keeping with existing policies, guidelines, and procedures, CalSTRS is best served when there is contractual alignment and transparency of financial interests with its external investment advisors and managers.
Belief 9 **Investment risks associated with climate change and the related economic transition—physical, policy and technology driven—materially impact the value of CalSTRS' investment portfolio.**	CalSTRS believes that public policies, technologies and physical impacts associated with climate change are driving a transition to a lower carbon economy. As a prudent fiduciary and diversified global investor, CalSTRS needs to understand the transition's impacts on companies, industries and countries and consider actions to mitigate risk and identify investment-related opportunities. CalSTRS recognizes the critical role that carbon pricing frameworks may play in integrating the costs of carbon emissions into the global economy to accelerate an orderly low-carbon transition and avoid exacerbating economic inequality and related geopolitical risks.