



Investment Committee

Item Number 6 – Open Session

Subject: Approval of Minutes of the July 7, 2022, Investment Committee – Open Session

Presenter(s): Chairperson

Item Type: Consent Action

Date & Time: August 31, 2022 – 0 minutes

Attachment(s): None

PowerPoint(s): None

PROPOSED MINUTES

Teachers' Retirement Board – Investment Committee Meeting

July 7, 2022

OPEN SESSION

LOCATION: Board Room, 100 Waterfront Place, West Sacramento, CA 95605

COMMITTEE MEMBERS PRESENT

William Prezant, Chairperson

Denise Bradford

Michael Gunning

Ken Tang

Jennifer Urdan

Karen Yamamoto

Gayle Miller, Vice Chair, representing the Director of Finance, Keely Bosler

Frank Ruffino, representing the State Treasurer, Fiona Ma

Blake Johnson, representing the State Superintendent of Public Instruction, Tony Thurmond

Betty Yee, State Controller

COMMITTEE MEMBERS ABSENT

Sharon Hendricks

Harry Keiley

STAFF PRESENT

Cassandra Lichnock, Chief Executive Officer
Christopher Ailman, Chief Investment Officer
Brian J. Bartow, General Counsel
Lisa Blatnick, Chief Operating Officer
Ashish Jain, Chief Technology Officer
Melissa Norcia, Chief Administrative Officer
Bill Perez, Chief Benefits Officer
Teresa Schilling, Chief Public Affairs Officer
Julie Underwood, Chief Financial Officer
Scott Chan, Deputy Chief Investment Officer
Mike DiRé, Director, Real Estate
Shifat Hasan, Head of Investment Performance and Compliance
Glenn Hosokawa, Director, Fixed Income
Kirsty Jenkinson, Director, Sustainable Investments and Stewardship Strategies
Geraldine Jimenez, Director, Investment Strategy and Risk
June Kim, Director, Global Equities
Paul Shantic, Director, Inflation Sensitive
Steven Tong, Director, Risk Mitigating Strategies
April Wilcox, Director of Investment Services
Margot Wirth, Director, Private Equity
Kelly Criss, Head of Investment Operations
Charles Fitzpatrick, Portfolio Manager
Alex Holtz, Senior Counsel

OTHER PRESENT

Allan Emkin, Meketa Investment Group
Susan Dixon, CalRTA
Pat Geyer, CalRTA
Jennifer Baker, CalRTA

A quorum being present, Chairperson Prezant called the Open Session meeting of the Investment Committee meeting to order at 9:05 a.m.

I. APPROVAL OF COMMITTEE AGENDA (Item 1)

The Committee Agenda was received, considered, and approved by the consent of the committee.

Members Voting	Aye	Nay	Abstain
Ms. Bradford	X		
Mr. Gunning	X		
Mr. Tang	X		
Ms. Urdan	X		

Ms. Yamamoto	X		
Ms. Miller for the Director of Finance	X		
Mr. Ruffino for the State Treasurer	X		
Mr. Johnson for the Superintendent of Public Instruction	X		
Controller Yee	X		
Chairperson Prezant	X		

II. OPPORTUNITIES FOR STATEMENTS FROM THE PUBLIC (Item 2)

The committee heard from Tabitha Nieman, who applauded CalSTRS’ ESG policies, expressed concerns about investing with companies that do not adequately enforce ESG policies, and urged CalSTRS to not invest in KKR’s Global Impact II Fund.

The committee heard from Anaya, who spoke about fossil fuel divestment, expressed disappointment in SB 1173 failing, and stated that divestment from fossil fuel would not negatively impact CalSTRS.

The committee heard from Magdalena, who spoke about fossil fuel divestment, the climate crisis, and urged more communication.

The committee heard from Raven, who spoke about fossil fuel divestment and expressed that we are in a time of critical climate crisis.

The committee heard from Remari, who acknowledged Mr. Tang and Mr. Gunning as new board members and spoke about fossil fuel divestment, the impacts of climate change, and the disproportionate climate change impacts on minority communities.

The committee heard from Katarina, who spoke about fossil fuel divestment and noted that investing in fossil fuels takes away access to clean water and clean air. She also noted that divestment would not negatively impact the pension fund.

The committee hear from Reyna Meyers-Dahlkamp, who discussed the ongoing violence associated with the oil pipeline and the fossil fuel industry in the Republic of Congo and urged divestment from the East African Pipeline. She also noted that Uganda leaders had requested to meet with CalSTRS and other large pension funds.

The committee heard from Karis Dahlkamp, who discussed the recent Supreme Court EPA ruling, and urged fossil fuel divestment. He also stated that he was a supporter of the recently failed SB 1173.

III. INVESTMENT POLICY AND MANAGEMENT PLAN REVISION – ASSET ALLOCATION – FIRST READING (Item 3)

The committee received the first reading of the Investment Policy & Management Plan Revision – Asset Allocation from Ms. Jimenez. The committee considered the proposed final step in the asset allocation targets and the proposed liquidity constraint change. The committee discussed the proposed increase of 1% to the Real Estate target weight, the increase of 1% to the Inflation Sensitive target weight, and the 2% decrease in the Public Equity target weight to fund the increases.

The committee also considered the proposed update to the liquidity risk limit and discussed the proposed increase from 40% to 50% maximum illiquid assets. It was noted that the proposed policy changes will not affect how cash is managed and the increase to 50% maximum illiquid assets is in line with the shift to more illiquid assets in the strategic asset allocation. Ms. Jimenez informed the committee that the next Asset Liability Management (ALM) study will be more explicit on how liquidity is managed in each asset class. The committee also discussed the difference between liquidity and illiquidity and the various tools that are available to raise liquidity if needed.

MOTION duly made by Controller Yee, seconded by Ms. Yamamoto, and carried to adopt the proposed Investment Policy and Management Plan revisions to increase the Real Estate and Inflation Sensitive target weights, decrease Public Equity target weight, and increase the maximum policy limit for illiquid assets effective as of July 1, 2022.

Members Voting	Aye	Nay	Abstain
Ms. Bradford	X		
Mr. Gunning	X		
Mr. Tang	X		
Ms. Urdan	X		
Ms. Yamamoto	X		
Ms. Miller for the Director of Finance	X		
Mr. Ruffino for the State Treasurer	X		
Mr. Johnson for the Superintendent of Public Instruction	X		
Controller Yee	X		
Chairperson Prezant	X		

IV. CHIEF INVESTMENT OFFICER’S REPORT (Item 4)

The committee received the Open Session Chief Investment Officer report from Mr. Ailman, including a discussion regarding the Investment Portfolio Risk Report, the 2021-2022 fiscal year financial market conditions, potential risks on the horizon and recent proxy voting efforts. Mr. Ailman welcomed the investment student interns and each student intern introduced themselves to the committee.

Mr. Ailman noted there was a solid start to the fiscal year and informed the committee that between July 2021 and December 2021 the U.S. stock market grew 8.5% and the fund grew to an all-time high of \$327 billion. Mr. Ailman also noted that the second half of the fiscal year was much different as the Federal Reserve began to raise interest rates to combat rising inflation. Mr. Ailman informed the committee that between January 2022 and June 2022, the U.S. stock market fell by 21% and the fund fell below \$300 billion. Mr. Ailman indicated the U.S. stock market fiscal year return was negative 14.1%, but the three-year return was positive and projected at 9.4%. Mr. Ailman noted that most of the negative 17.7% one-year return on non-U.S. stock market(s) was caused by the strong U.S. dollar. Mr. Ailman reported the fiscal year end value of the fund will be over \$300 billion in total assets, but the final fiscal year return number won't be available for another week. Mr. Ailman estimated that the final fiscal year return number will likely be a small negative number such as 1% or 2%. Mr. Ailman informed the committee that even if returns for the next year were flat that the overall three-year return would remain positive at 7% or better.

Mr. Ailman noted positives moving forward, such as a strong labor market and solid corporate balance sheets, but also outlined key risks to monitor such as high inflation, Central Bank/Fed policies and rising interest rates. Mr. Ailman also discussed uncertainties moving forward such as the Fed continuing to raise interest rates and possible recession. The committee discussed rising inflation, stagflation, rising interest rates and the impacts on the portfolio moving forward. The committee also discussed the importance of the Inflation Sensitive and RMS asset classes. Mr. Ailman stated the house view on asset allocation is defensive and that diversification is the number one tool to mitigate risk. The committee also considered the potential impacts to the portfolio such as climate extremes, pandemics, digital/cyber attacks, Russia/Ukraine war, China & Taiwan tensions, North Korea and Iran aggression and the U.S. & global energy transition. Mr. Bartow reported that the board has recognized the risks of digital/cyber attacks for years and noted that it is reflected as the number one risk on the board's risk evaluation and risk management report. Mr. Bartow also highlighted the rigorous security measures that CalSTRS implements internally and with our business partners to mitigate potential digital/cyber attacks.

V. FISCAL YEAR 2022-2023 INVESTMENT BUSINESS PLANS (Items 5a-5k)

Mr. Ailman presented an overview of the Fiscal Year 2022-2023 Investment Business Plans, which focus on the core objectives for both the Investment Committee and the CalSTRS' strategic plan.

The committee discussed the core objectives of the business plans, including: (i) earn the assumed rate of return, net of costs, on average over rolling three-year periods (ii) exceed the respective benchmarks of each unit net of fees (iii) keep costs down by continued implementation of Collaborative Model 2.0 (iv) achieve net zero in the Investment Portfolio by 2050 or sooner, and (v) strive to expand the diversity and inclusion of the management of investments both external managers and internal staff. Mr. Ailman emphasized that the number one goal is fully funding the pension plan and to exceed the benchmarks and earn 7% on average over 20 years. Mr. Ailman informed the committee

that Collaborative Model 1.0 saved close to \$300 million per year in fees and indicated that moving forward Collaborative Model 2.0 could double the annual cost savings and reasonably save \$750 million per year. The committee considered the annual cost savings and discussed how those savings are being reported in the cost report. The committee also considered whether the cost savings were net of expenses and requested that an additional breakdown of costs for external consultants be included in the next cost report.

Mr. Ailman also informed the committee that to fully implement Collaborative Model 2.0 and achieve full cost savings, the use of more specialized external consultants will be needed, as well as hiring highly skilled workers and paying competitive salaries. The committee considered the increased costs needed to fully implement Collaborative Model 2.0, discussed the need to utilize more external consultants and pay competitive salaries in order to recruit and hire necessary talent to manage the investment needs of the pension fund going forward. The committee also discussed the constraints of paying competitive salaries in a civil service state and the necessity to be risk driven in determining what is needed to manage more complex risk going forward.

VI. INFLATION SENSITIVE ASSET CLASS POLICIES – FIRST READING (Items 6a and 6b)

The committee received the first reading of the proposed revisions to the Inflation Sensitive Investment Policy and the Infrastructure Investment Policy from Mr. Shantic and Mr. Fitzpatrick. The committee discussed and considered the proposed policy revisions to (i) clarify that Inflation Sensitive investment approvals will follow the same policies and procedures as those currently utilized by the Infrastructure portfolio involving internal recommendations and external consultant review (ii) clarify that Infrastructure related loan or debt securities are governed by the Inflation Sensitive policy as they are more akin to floating rate debt and debt-like securities rather than equity (iii) add language from the Infrastructure policy regarding staff approval levels, single manager investment limits, and the 5% asset limit, and (iv) slightly modify the performance objective benchmark to recognize the discontinuation of the Alerian Index.

The committee considered the Inflation Sensitive allocation relative to the total portfolio and discussed how the debt portion of the Inflation Sensitive portfolio collaborates with other asset classes such as Private Equity, Fixed Income and Real Estate. Mr. Shantic informed the committee that 50% to 60% of the Inflation Sensitive portfolio resides in the Infrastructure portfolio and the majority of those assets are tied to and move with inflation. Mr. Shantic also noted that the portfolio holds commodities and TIPS which are managed with the assistance of Fixed Income. Mr. Shantic informed the committee that since inflation has increased the commodities portion of the portfolio has hit its limits but as inflation begins to drop the TIPS portfolio is expected to perform better. The committee discussed looking at private debt strategies within Inflation Sensitive to increase returns within the portfolio. The committee also considered moving the debt portion of the portfolio into the Inflation Sensitive portfolio in order to look at managers and strategies across a broad spectrum. The committee considered the increase in

competition for value-added infrastructure assets as demand remains high for the core investments. The committee also discussed how the unit began as Infrastructure and expanded into the broader Inflation Sensitive asset class wherein Infrastructure now resides.

MOTION duly made by Ms. Urdan, seconded by Ms. Miller, and carried to adopt the proposed revisions to the Inflation Sensitive Investment Policy and the Infrastructure Investment Policy.

Members Voting	Aye	Nay	Abstain
Ms. Bradford	X		
Mr. Gunning	X		
Mr. Tang	X		
Ms. Urdan	X		
Ms. Yamamoto	X		
Ms. Miller for the Director of Finance	X		
Mr. Ruffino for the State Treasurer	X		
Mr. Johnson for the Superintendent of Public Instruction	X		
Controller Yee	X		
Chairperson Prezant	X		

VII. FISCAL YEAR 2022-2023 INVESTMENT COMMITTEE WORK PLAN (Item 7)

The committee received and considered the Fiscal Year 2022-2023 Investment Committee Work Plan. Mr. Ailman informed the committee that the purpose of the Work Plan is to guide the committee and gain the committee’s support on the upcoming year’s objectives. Mr. Ailman reported that the 2023 Asset Liability Management (ALM) study is the major project outlined within the Work Plan along with the goal of achieving net zero emissions by 2050 or sooner and the Collaborative Model 2.0. Mr. Ailman noted that the Collaborative Model and the transition to net zero objectives will continue to be part of the Work Plan for a long time because they are multi-year decade-long efforts. Mr. Ailman also informed the committee that the ALM study is the single most important decision that the committee makes because it differentiates our return from everyone else in the world. Mr. Ailman noted that this fiscal year commences the start of the 2023 ALM, which will commence with discussions regarding geopolitical risks, the energy transition, global pandemics and how these issues can impact the portfolio. Mr. Ailman stated that in November the committee will undertake the traditional asset allocation study, select asset classes and establish limits. Mr. Ailman informed the committee that the ALM study usually takes about nine months to complete and then it takes a couple of years to shift to the new asset allocation target(s). The committee considered the three main work core objectives outlined in the Work Plan and discussed the challenges of the ALM study. Mr. Ailman indicated that the 2023 ALM study will dominate the Work Plan, but the net zero and Collaborative Model objectives will continue to carry forward as well as the committee’s traditional workload and

responsibilities to monitor and evaluate the investment portfolio. Mr. Emkin of Meketa informed the committee that the biggest challenge is that the future is unknown and that decisions need to be made under uncertainty utilizing generally accepted tools to make prudent decisions. Mr. Emkin also reported that the ALM study is a huge responsibility and the most important undertaking that the committee can do because it will have the largest impact on the risk and return of the portfolio.

The Fiscal Year 2022-2023 Investment Committee Work Plan was received, considered, and approved by the consent of the committee.

Members Voting	Aye	Nay	Abstain
Ms. Bradford	X		
Mr. Gunning	X		
Mr. Tang	X		
Ms. Urdan	X		
Ms. Yamamoto	X		
Ms. Miller for the Director of Finance	X		
Mr. Ruffino for the State Treasurer	X		
Mr. Johnson for the Superintendent of Public Instruction	X		
Controller Yee	X		
Chairperson Prezant	X		

VIII. APPROVAL OF THE MINUTES OF THE MAY 5, 2022 INVESTMENT COMMITTEE MEETING – OPEN SESSION (Item 8)

The Minutes of the May 5, 2022, Investment Committee Meetings – Open Session were received, considered, and approved by the consent of the committee.

Members Voting	Aye	Nay	Abstain
Ms. Bradford	X		
Mr. Gunning	X		
Mr. Tang	X		
Ms. Urdan	X		
Ms. Yamamoto	X		
Ms. Miller for the Director of Finance	X		
Mr. Ruffino for the State Treasurer	X		
Mr. Johnson for the Superintendent of Public Instruction	X		
Controller Yee	X		
Chairperson Prezant	X		

IX. REPORT PURSUANT TO ASSEMBLY BILL 2833 (Item 9)

The committee received the annual report pursuant to Assembly Bill 2833.

X. ANNUAL REVIEW OF DELEGATION TO STAFF (Item 10)

The committee received the Annual Review of Delegation to Staff.

XI. REVIEW INFORMATION REQUESTS (Item 11)

Regarding Item 5, the committee requested a breakdown of the increased costs associated with the use of external consultants to implement the Collaborative Model be included in the next cost report, and also requested clarification whether cost savings related to the Collaborative Model are net of expenses.

XII. DRAFT AGENDA FOR NEXT COMMITTEE MEETING (Item 12)

The committee received and reviewed the draft agenda for the next meeting.

XIII. OPPORTUNITY FOR ADDITIONAL STATEMENTS

There were no additional statements from the public.

RECESS

The Open Session of the committee meeting recessed at 11:21 a.m. and the committee went into Closed Session. The committee meeting reconvened in Open Session at 12:11 p.m.

Chairperson Prezant stated that there was nothing to report out as the committee took no action while in Closed Session.

XIV. ADJOURNMENT

There being no further business to conduct, Chairperson Prezant adjourned the meeting at 12:11 p.m.

Cassandra Lichnock, Chief Executive Officer
And Secretary to the Teachers' Retirement Board

William Prezant, Chairperson

Prepared by: Alex Holtz, Senior Counsel