CALSTRS

Regular Meeting
Item Number 5 – Open Session

Subject: Benchmarking Review Project

Presenters: Kristel Turko / Stephen McCourt, Meketa Investment Group

Item Type: Information

Date & Time: January 25, 2023 – 30 minutes

Attachment(s): Meketa Opinion Memo– Total Fund Benchmarking Project

PowerPoint(s): Benchmarking Review Project

Item Purpose

The purpose of this item is to continue the board's conversation from its January 2022 meeting regarding investment benchmarking and to provide potential options to simplify the Total Fund benchmark.

Recommendation

Meketa Investment Group (Meketa) and Human Resources seek feedback and direction on next steps. Meketa and Human Resources recommend the following:

- The board to contemplate and adopt its preferred style of the Total Fund benchmark

- Meketa to provide a variety of potential benchmark options with back tested performance data

Executive Summary

For this item Stephen McCourt of Meketa will provide a presentation and updates regarding the Benchmarking Review Project. This item is intended to be exclusively focused on benchmarking CalSTRS' investment performance (Risk and Return). The role of benchmarks in determining incentive compensation will be addressed by the board at a later date. Mr. McCourt will refresh the board discussion from the January 2022 Regular Meeting and provide a review of the findings from the benchmarking surveys and interviews Meketa conducted with board members and with peer public pension funds.

The overall findings provided the following areas of consensus:

- The benchmarks should be simplified and provide more transparency

- The current set of benchmarks are overly complex and difficult to understand

- Benchmarks should be reviewed when asset allocation is reviewed

- The board should be involved when approving benchmarks for the Total Fund.

- The board should not be involved when approving benchmarks for sub-asset classes

- Benchmarks should be aligned with the CalSTRS' long-term objectives (not short-term considerations)

Based on the board's feedback, it is apparent that the Total Fund benchmark is complex and not easily understood and there is desire for greater transparency. For today's discussion, Mr. McCourt will present potential benchmarking options for the board's consideration.

Background

To assist the board in its review of the benchmarking program, Stephen McCourt provided a presentation at the January 2022 Regular Meeting with focus on three areas 1) Current state of CalSTRS benchmarks, 2) Key themes solicited from a board member survey and one-on-one interviews from board members who requested them, and 3) A survey of peer public pension systems. The board was presented with an overview of CalSTRS current state of investment benchmarks and received information on the governance structure currently in place to establish and/or revise investment benchmarks.

Mr. McCourt facilitated board discussion regarding the complexity of CalSTRS benchmarks. Meketa staff remarked that the CalSTRS benchmark structure is by far the most complex they have come across. Meketa staff noted that the Total Fund benchmark is very complex because it is essentially a roll-up of very complex asset class benchmarks with roll-ups of sub-asset class benchmarks and includes thousands of pieces of information. CalSTRS has 179 unique benchmarks across all levels of the portfolio (total policy, asset class, sub asset class, and external manager). The number of benchmarks across the total plan extends to 428 when considering duplicates across multiple funds and asset classes.

Based on Meketa's findings and analysis, the board members agreed that the current state of benchmarking is overly burdensome and complex. The board expressed interest in simplification and directed Meketa to explore options to streamline and simplify the benchmarking program to be presented at a future meeting.

Strategic Plan Linkage: Goal 1: Trusted Stewards – Ensure a well-governed, financially sound trust fund. with Objective A: Achieve full funding of the Defined Benefit Program by June 30, 2046.

Board Policy Linkage: CalSTRS Investment Policy and Management Plan, Compensation Policy for Designated Executive Management and Investment Staff and its Administrative Procedures.

Reference Material:

January 2022 Regular Meeting:

- Item 13 - Benchmarking Review Project
- Item 13 - Attachment 1 - Overview of Benchmarking
- Item 13 - PowerPoint - Benchmarking Project