Strategic Class Overview

CalSTRS historically organizes investments into asset classes based upon underlying security types and strategy implementation. For example, CalSTRS current classes include:

- The Global Equity class comprises investments in public equity securities in ways that are expected to track or outperform common equity indices like the MSCI ACWI.
- The Real Estate asset class invests in global real estate properties, with a majority invested in the U.S.
- The Risk Mitigating Strategies class blends investments defined largely by the underlying security type with investments defined by the strategy, with the common objective of diversification to global growth.

This framework is useful as the definitions generally line up with the broader investment industry's definitions and has been used over time. However, there are other ways to organize investments as this framework ignores some common drivers of risk.

Underlying many of the asset classes is a smaller number of underlying economic risks. For example, public equity has a strong connection to economic growth. Real Estate has a connection to inflation risk and economic growth risk. The common theme is the idea of a small number of economic risk factors that drive asset returns.

Combining asset classes that are organized around security type and strategy with a small number of economic risk drivers, it is possible to get a more complete picture of risk in the portfolio to better manage this risk. Table 2 below summarizes the traditional CalSTRS asset classes and economic drivers of risk.

Table 2. Asset Classes & Economic Risk Factors

Asset Class	Major Economic Risk Factors
Public Equity	Economic Growth
Private Equity	Economic Growth
Real Estate	Inflation
	Economic Growth
Inflation Sensitive	Inflation
Fixed Income	Economic Growth (Diversifying)
	Inflation
Risk Mitigating Strategies	Economic Growth (Diversifying)
	Inflation
Cash	Economic Growth (Diversifying)

As Economic Growth is so important to the CalSTRS portfolio, considering a spectrum of exposure in different assets can be helpful. Figure 1 below shows the exposure to growth risk for several assets in the portfolio; assets on the left have higher exposure to growth and tend to move together. Assets to the right tend to have less growth risk and offer diversification to the growth assets. The diversification benefit and balancing risks is a big focus in any ALM and led to CalSTRS' adoption of Risk Mitigating Strategies in 2015.

Figure 1. Asset Exposure to Economic Growth

Asset Classes to Strategic Classes

Exposure to these economic risk factors ultimately drives the risk and return of the CalSTRS portfolio. By viewing the portfolio this way, it is possible to first consider the appropriate amount of risk and the balance of major sources of risk, before moving on to the best way to achieve the desired mix of risks. This is a natural evolution in the process to better view and manage the long-term asset allocation.

The portfolio modeling in subsequent steps of the ALM Study uses these strategic classes to focus the discussion on the most significant drivers of risk and return in the CalSTRS portfolio. This framework also enables more dynamic modeling of any changes to the long-term asset allocation. This strategic class framework also enables a broader discussion about risk appetite, particularly in the early stage modeling in March 2023.

Strategic Classes

<table>
<tr><th>Strategic Class</th><th>Economic Growth</th></tr>
<tr><td>Role of Strategic Class</td><td>The role of the economic growth class is to provide relatively high long-term returns to the portfolio. The Economic Growth class is expected to a significant majority of the long-term portfolio return.</td></tr>
<tr><td>Composition</td><td>The Economic Growth class comprises Total Public Equity and Private Equity.</td></tr>
<tr><td>Current Allocation</td><td>
<table>
<tr><th></th><th>% Total Fund</th><th>% Strategic Class</th></tr>
<tr><td>Public Equity</td><td>42%</td><td>77%</td></tr>
<tr><td>Private Equity</td><td>13%</td><td>23%</td></tr>
<tr><td>Total</td><td>55%</td><td>100%</td></tr>
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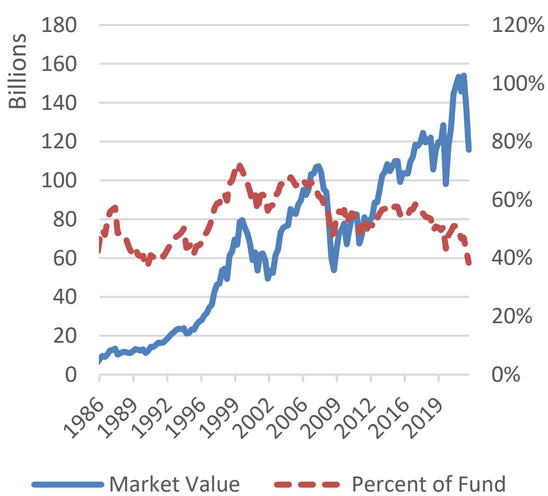
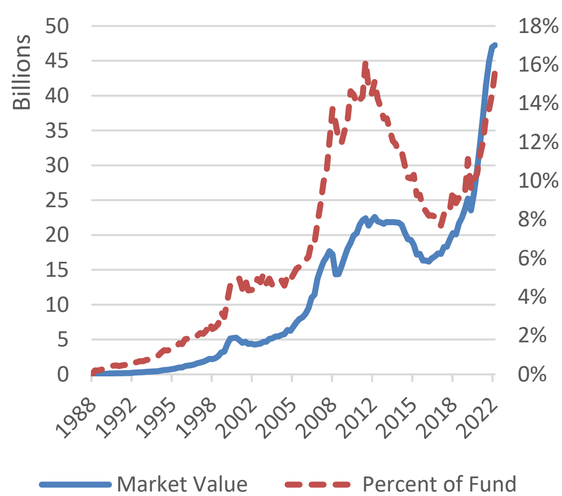
Total Public Equity

CalSTRS' Public Equity program was established in 1986. The first internally managed U.S. portfolio was implemented in 1998. Internal Canada and EAFE portfolios were added in 2009 and 2016 respectively.



Private Equity

CalSTRS' Private Equity program was established in 1988. Components include limited partnership commitments, side-by-side co-investments, and secondary transactions.



<table>
<tr><th>Strategic Class</th><th>Real Assets</th></tr>
<tr><td>Role of Strategic Class</td><td>The role of the Real Assets class is to provide long-term returns to the portfolio by investing in assets that benefit from or provide protection from inflation. Real Assets have some exposure to economic growth risks but tend to provide modest diversification to the growth risk of the Economic Growth strategic class.</td></tr>
<tr><td>Composition</td><td>The Real Assets class comprises Real Estate and Inflation Sensitive.</td></tr>
<tr><td>Current Allocation</td><td><table>
<tr><th></th><th>% Total Fund</th><th>% Strategic Class</th></tr>
<tr><td>Real Estate</td><td>15%</td><td>75%</td></tr>
<tr><td>Inflation Sensitive</td><td>6%</td><td>25%</td></tr>
<tr><td>Total</td><td>21%</td><td>100%</td></tr>
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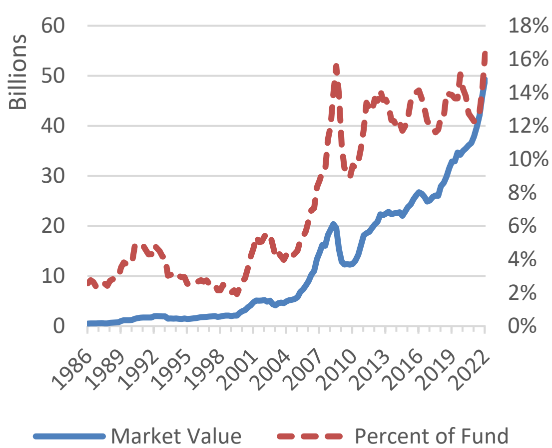
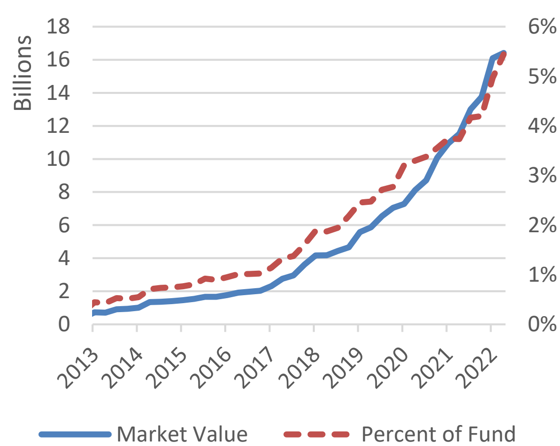
Real Estate	Inflation Sensitive
The Real Estate equity portfolio was established in 1986 as one of CalSTRS' original asset classes.	In the 2012-13 asset allocation study, the Board approved an allocation to Inflation Sensitive. CalSTRS' Inflation Sensitive portfolio now includes infrastructure, commodities, TIPS, agriculture, and timber assets.



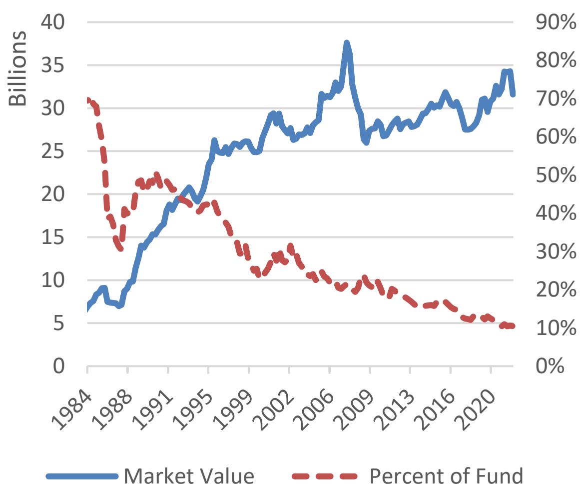


Strategic Class	**Diversifying**
Role of Strategic Class	The role of the Diversifying class is to provide modest long-term returns to the portfolio while diversifying the growth risk of the Economic Growth strategic class.
Composition	The Diversifying class comprises Fixed Income, Risk Mitigating Strategies, and Cash.
Current Allocation	

	% Total Fund	**% Strategic Class**
Fixed Income	12%	50%
Risk Mitigating Strategies	10%	42%
Cash	2%	8%
Total	24%	100%

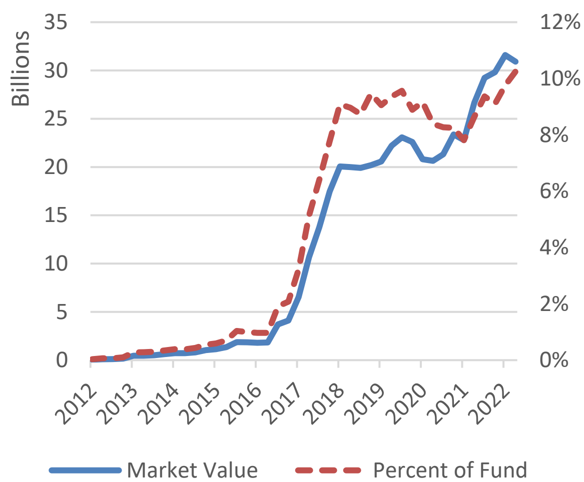
Fixed Income

The CalSTRS portfolio was primarily Fixed Income instruments until the mid-1980s. Fixed Income became the first internally managed asset class in 1987.



RMS

CalSTRS' RMS asset class was approved by the Investment Committee in 2015. RMS comprises Trend Following / CTA strategies, Long Duration US Treasuries, Global Macro strategies, and Systematic Risk Premia.



Strategic Class	**Credit**
Role of Strategic Class	The role of the Credit class is to provide long-term income returns to the portfolio. Credit has some exposure to Economic Growth and to Diversifying.
Composition	The Credit class is unique as it spans public and private investments in several asset classes and Innovative Strategies. Credit exposure comes from Private Equity, Real Estate, Inflation Sensitive, Fixed Income, and Innovative Strategies.
Current Allocation	see table below

Current Allocation

	% Total Fund	**% Strategic Class**
Private Equity	1%	13%
Real Estate	1%	16%
Inflation Sensitive	0%	0%
Fixed Income	4%	57%
Innovative Strategies	1%	15%
Total	6%	100%

Opportunities Portfolio	
Role of Strategic Class	The role of the Opportunities Portfolio is to provide a flexible pool of capital to capture market that may cross asset classes or don’t fit into an existing asset class.
Composition	The Opportunities Portfolio spans public and private investments in several asset classes through three components: Innovative Strategies, Tactical Opportunities, and the SISS Innovation portfolio.