Long-Term Care Fund Investment Policy Update

Christine Reese, Investment Director – TLPMI

Investment Committee

June 14, 2021

CalPERS

Executive Summary

The Asset Liability Management review for the Long-Term Care Fund necessitates the following policy updates:

1. Strategic Asset Allocation Targets and Ranges
2. Benchmark Composition
3. Tracking Error Limit

- The Strategic Asset Allocation Targets were approved in March and are presented with slight amendments to include the U.S. TIPS[1] allocation in the Global Fixed Income asset class and to confirm the Liquidity asset class, which is currently in policy.

- Recommendation: Adopt the proposed policy updates for the Long-Term Care fund, to be implemented as an administrative policy update in the month in which the assets transfer to the new strategy.

[1] U.S. TIPS are Treasury Inflation Protected Securities.

Strategic Asset Allocation Targets

Asset Class	Approved Policy Target[1]	Proposed Policy Target
Global Equities	30%	30%
Global Fixed Income	54%	60%
U.S. TIPS	6%	-
REITs[2]	7%	7%
Commodities	3%	3%
Liquidity	n/a	0%

The Strategic Asset Allocation Policy Targets approved in March included U.S. TIPS as a separate asset class and did not include a Liquidity asset class, which is currently in Policy.

Proposal:

1) Include the TIPS allocation with the Global Fixed Income asset class to align the allocation with the asset class management and account structure.

2) Include a Liquidity asset class with a target of zero to allow for operational cash flows.

Ranges relative to policy are presented on the following page.

[1] Approved by the Board at the March 2021 meeting.
[2] REITs are Real Estate Investment Trusts.

CalPERS

Strategic Asset Allocation Targets and Ranges

Asset Class	Proposed Policy Target	Proposed Policy Range	Current Policy Target	Current Policy Range
Global Equities	30%	+/- 7%	15%	+/- 4%
Global Fixed Income	60%	+/- 7%	60%	+/- 5%
U.S. TIPS	-	-	6%	+/- 2%
REITs	7%	+/- 3%	11%	+/- 4%
Commodities	3%	+/- 2%	8%	+/- 2%
Liquidity	-	+ 2%	0%	+ 2%

- The proposed policy ranges are intended to allow for market drift between quarterly rebalances. The wider ranges for the new allocation are to mitigate the need to rebalance the portfolio mid-quarter and away from the benchmark.
- There will be no active asset allocation between asset classes in the investment strategy.
- The +2% liquidity range is constrained to frictional/operational cash flows.

CalPERS

Benchmark Composition

Asset Classes/Components	Benchmark
Total Portfolio	Custom Weighted Based on Asset Class Benchmarks
Global Equities	Custom Weighted Based on Component Benchmarks
US Large Cap Equities	MSCI Developed – US Total Return Index Gross
Developed Ex-US Equities	MSCI World ex-US Hedged Index Net
Emerging Market Equities	MSCI Emerging Market Index Net
Global Fixed Income	Custom Weighted Based on Component Benchmarks
US Cash	Bloomberg Barclays T-bill 1-3 Month Index
US Government 10+ years	Bloomberg Barclays Long Government Index
Global ex-US Treasuries	Bloomberg Barclays Global Aggregate Treasury Index ex-US Hedged
US Investment Grade Credit - Long Bonds	Bloomberg Barclays US Long Credit Index
US Investment Grade Credit – Long BBB	Bloomberg Barclays Long Corporate Index BBB
US High Yield	Bloomberg Barclays US Corp High Yield 2% Issuer Capped Index
US Inflation Linked Government Bonds	Bloomberg Barclays US Treasury Inflation 15Yr+ Index
ABS in USD	Bloomberg Barclays ABS Index
US Agency MBS	Bloomberg Barclays MBS Index
US CMBS	Bloomberg Barclays CMBS, Eligible for US Aggregate Index
US CMBS Sub	Bloomberg Barclays US CMBS ex-AAA Index
EM Bonds (USD denominated)	JP Morgan EMBI Global Diversified Index
REITs	FTSE EPRA/NAREIT Developed REITs 100% Hedged to USD Net Index
Commodities	Bloomberg Commodity Total Return Index

CalPERS

Tracking Error Limit

The proposed Tracking Error limit of up to 1% for the Long-Term Care Fund is in alignment with the proposed limit for the Total Fund.

- Current Policy: The Fund will be managed within a target forecast annual tracking error as described in the CalPERS Total Fund Investment Policy, Asset Allocation Strategy Section.

- Proposed Update: The Fund shall be managed with an active risk target consistent with forecast tracking error up to 1% relative to the Policy benchmark. The tracking error will be monitored regularly, and in the event of a breach, staff will inform the Board of the cause and develop a plan to move the tracking error within the target range, if deemed advisable, taking into account strategy horizon, transaction costs, and liquidity conditions.

CalPERS

Recommendation and Next Steps

Recommendation:

Adopt the proposed policy updates for the for the Long-Term Care fund, to be implemented as an administrative policy update in the month in which the assets transfer to the new strategy.

1. Strategic Asset Allocation Targets and Ranges
2. Benchmark Composition
3. Tracking Error

Next Steps:

1. Complete Contracting – June/July
2. Complete Setup and Implementation – Aug/Sept[1]

[1]Implementation is expected to take 1-2 months and includes setup, testing, and launch for accounts, benchmarks, systems, trading, operations, and the asset transition.

CalPERS

Asset Allocation Timeline

Milestone	2020									2021								
	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S
Evaluate Current Portfolio	░	░	░															
Conduct Research			░	░														
Draft & Release RFP					░	░												
Receive Proposals							░											
Evaluate Proposals							░	░	░	░								
Approve Discount Rate (Nov IC)								░										
Prepare Allocation Recommendation										░								
Adopt Asset Allocation (March IC)											░							
Contracting & Planning												░	░					
Approve Investment Policy (June IC)															▓	▓		
Complete Contracting															▓	▓	▓	
Complete Setup and Implementation																	▓	▓