Wilshire

__Andrew Junkin, CFA, CAIA__
__Managing Director & Principal__

October 31, 2012

Mr. Henry Jones
Chair of the Investment Committee
California Public Employees' Retirement System
400 Q Street
Sacramento, CA 95814

Re: Global Equity Policy Revision

Dear Mr. Jones:

You requested Wilshire's opinion with respect to Staff's proposed all-encompassing Global Equity Policy. This Policy would replace the host of policies that currently govern Global Equity and would reflect how Staff currently views the Global Equity portfolio – holistically, rather than as an amalgamation of various programs.

While the streamlined nature of the proposed Policy is a significant improvement of the existing number of policies, we believe that there are certain areas that need further thought and attention – several examples are listed below.

- Section V, B, #3 proposes a 75 basis point limit for tracking error for the Global Equity portfolio. We have not identified any current tracking error limit for Global Equity, so this would be the first risk budget in place for the asset class. The PERF risk budget targets a maximum tracking error of 150 basis points, of which 75 basis points is permitted to come from the underlying asset classes and 75 basis points is permitted to come from asset class mis-weights versus the target weights. Given the high levels of tracking error in Private Equity and Real Estate, it is possible that a 75 basis point tracking error budget in Global Equity could be significantly too high. Alternatively, depending on the correlations of active returns across asset classes, 75 basis points could be appropriate or low. Wilshire believes that this requires additional study and a reasoned explanation of the selected tracking error budget.
- Section V, B, #5 speaks to the collateral held for derivatives, not "Notional Leverage." We believe that any references to using derivatives should reference the Derivatives Policy; otherwise changes in one policy could result in conflicts between the two policies. Additionally, according to the Leverage Policy, notional leverage should be

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limited by the asset class policy that permits it. In this case, the proposed Policy speaks to how much of the collateral can be invested in "non cash like collateral", but does not limit the amount of notional leverage. Wilshire believes that the Global Equity program should have minimal, if any, notional leverage (i.e., leverage that causes more assets to be exposed to equity market returns than the collateral would support).

- Section V, B, #6 limits the amount of "illiquid" securities to 15%. Wilshire believes that the term "illiquid" needs to be defined in the context of the Global Equity program before this limitation can be fairly evaluated. Theoretically, some publicly traded positions could be deemed illiquid based on the size of CalPERS' holding relative to typical trading volume. Truly illiquid securities that are not a result of corporate actions or corporate governance activities are likely a better fit for the Private Equity Program.

This list is not intended to be an exhaustive list of items that warrant further evaluation. In fact, our comments to Staff on the proposed Policy cover a bit more ground and Wilshire understands that Staff is reviewing our comments and comments from others. These comments are provided to the Investment Committee to indicate areas that we believe are worthy of attention and input from the Committee.

Should you require anything further or have any questions, please do not hesitate to contact us.

Best regards,