

# Program Update

## Real Estate

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# Program Role

- The role of Real Estate in the CalPERS portfolio is to have ownership risk in real property with stable cash yields. The major driver is income of which the majority is cash yield.
- Real Estate also provides a partial inflation hedge. The portfolio strives for moderate leverage, low risk, and low correlation to equities.

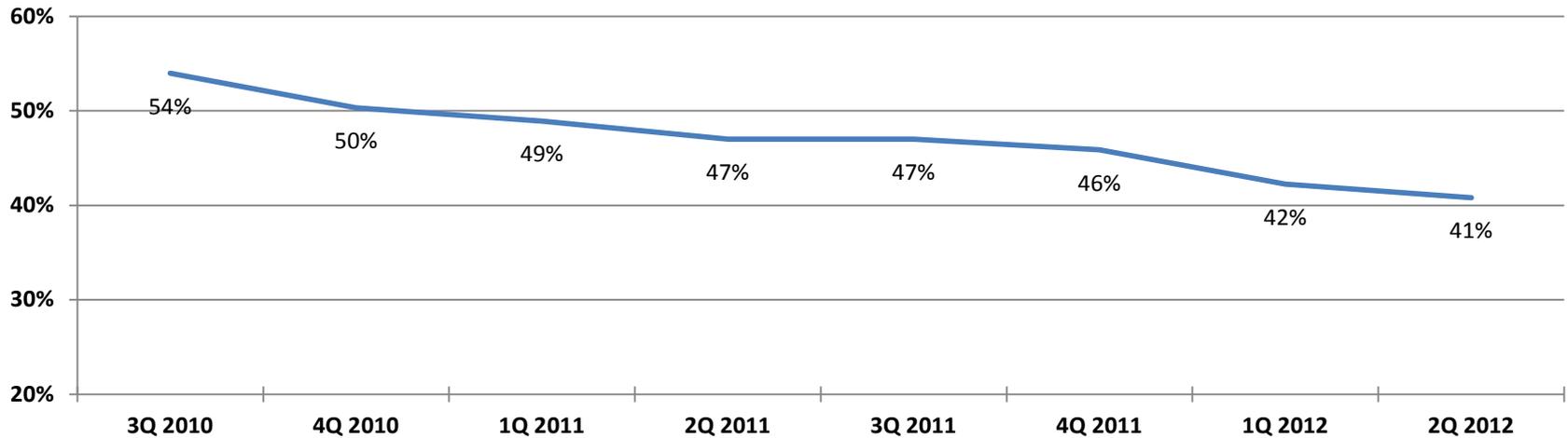
# Policy Targets

Investment Parameters	Interim (thru 6/30/13) Range/Limit as % of Total	Interim (thru 6/30/15) Range/Limit as % of Total	Long-Term Strategic Range/Limit as % of Total	NAV %	Compliance Interim (thru 6/30/13)	Compliance Interim (thru 6/30/15)	Compliance Long-Term
<b>Strategy</b>							
Base	0 - 100%	25 - 100%	60 - 100%	0%	✓	✗	✗
Domestic Tactical	0 - 100%	0 - 60%	0 - 30%	55%	✓	✓	✗
International Tactical	0 - 30%	0 - 25%	0 - 15%	9%	✓	✓	✓
Legacy	n/a	n/a	n/a	37%	n/a	n/a	n/a
<b>Risk Classification</b>							
Core	20 - 100%	50 - 100%	75 - 100%	44%	✓	✗	✗
Value Add	0 - 50%	0 - 40%	0 - 25%	20%	✓	✓	✓
Opportunistic	0 - 60%	0 - 40%	0 - 25%	36%	✓	✓	✗
REITS	0 - 10%	0 - 7.5%	0 - 5%	6%	✓	✓	✗
<b>Property Type</b>							
Office	45%	45%	45%	15%	✓	✓	✓
Industrial	45%	45%	45%	18%	✓	✓	✓
Retail	45%	45%	45%	22%	✓	✓	✓
Multifamily	45%	45%	45%	14%	✓	✓	✓
For Sale Residential & Land Dev.	15%	10%	10%	9%	✓	✓	✓
Hotels	10%	10%	10%	5%	✓	✓	✓
Mixed-Use	10%	10%	10%	6%	✓	✓	✓
Other Property Types	15%	10%	10%	10%	✓	✗	✗
<b>Geography</b>							
Developed Markets	75 - 100%	75 - 100%	75 - 100%	91%	✓	✓	✓
Developed - US	60 - 100%	70 - 100%	85 - 100%	86%	✓	✓	✓
Developed - ex US	0 - 25%	0 - 25%	0 - 25%	14%	✓	✓	✓
Emerging Markets	0 - 15%	0 - 15%	0 - 15%	9%	✓	✓	✓
Frontier Markets	0 - 5%	0 - 5%	0 - 5%	0%	✓	✓	✓
<b>REAL ESTATE PROGRAM</b>	<b>7 - 13%</b>	<b>7 - 13%</b>	<b>7 - 13%</b>	<b>9%</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>

# Policy Targets

Investment Parameters	Interim (thru 6/30/13) Range/Limit as % of Total	Interim (thru 6/30/15) Range/Limit as % of Total	Long-Term Strategic Range/Limit as % of Total	Actuals	Compliance Interim (thru 6/30/13)	Compliance Interim (thru 6/30/15)	Compliance Long-Term
<b>Loan to Value (LTV)</b>							
Total Portfolio	60%	55%	50%	41%	✓	✓	✓
Core	50%	50%	50%	42%	✓	✓	✓
Value Add	65%	60%	50%	23%	✓	✓	✓
Opportunistic	75%	65%	50%	43%	✓	✓	✓
<b>Debt Service Coverage Ratio (DSCR)</b>							
Total Strategic Portfolio	n/a	≥ 1.0	≥ 1.5	n/a	n/a	n/a	n/a
Strategic Core	≥ 1.5	≥ 1.75	≥ 2.0	2.18	✓	✓	✓
<b>Recourse Debt</b>							
Total Permitted Amount	10% of lower of current NAV or Target NAV			3%	✓	✓	✓

**Total Portfolio LTV Time Series**

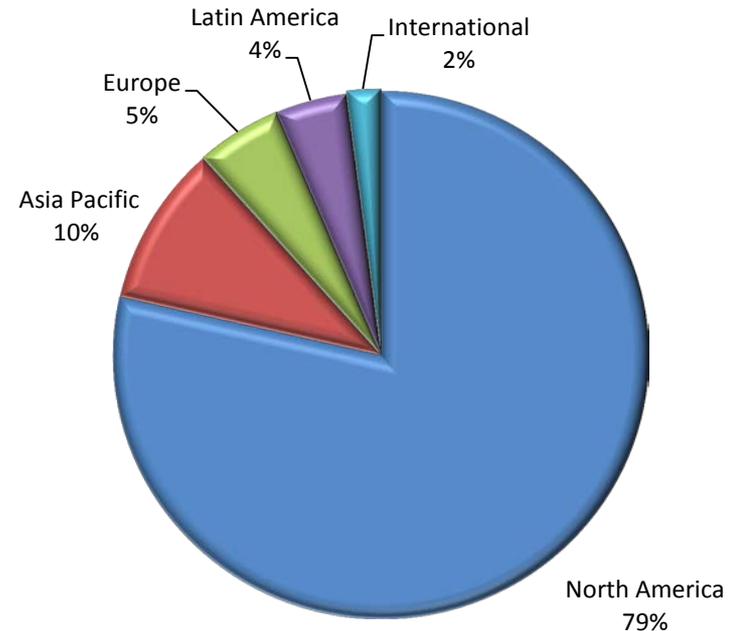


# Characteristics: Property Type & Region Allocation

## By Property Type

Property Type	% of Total Portfolio	NFI-ODCE <sup>1</sup>	Difference
Apartment	14%	24%	-9%
Industrial	18%	15%	3%
Office	15%	38%	-23%
Retail	22%	18%	4%
Hotel	5%	3%	3%
Other <sup>2</sup>	<u>25%</u>	<u>3%</u>	22%
	100%	100%	

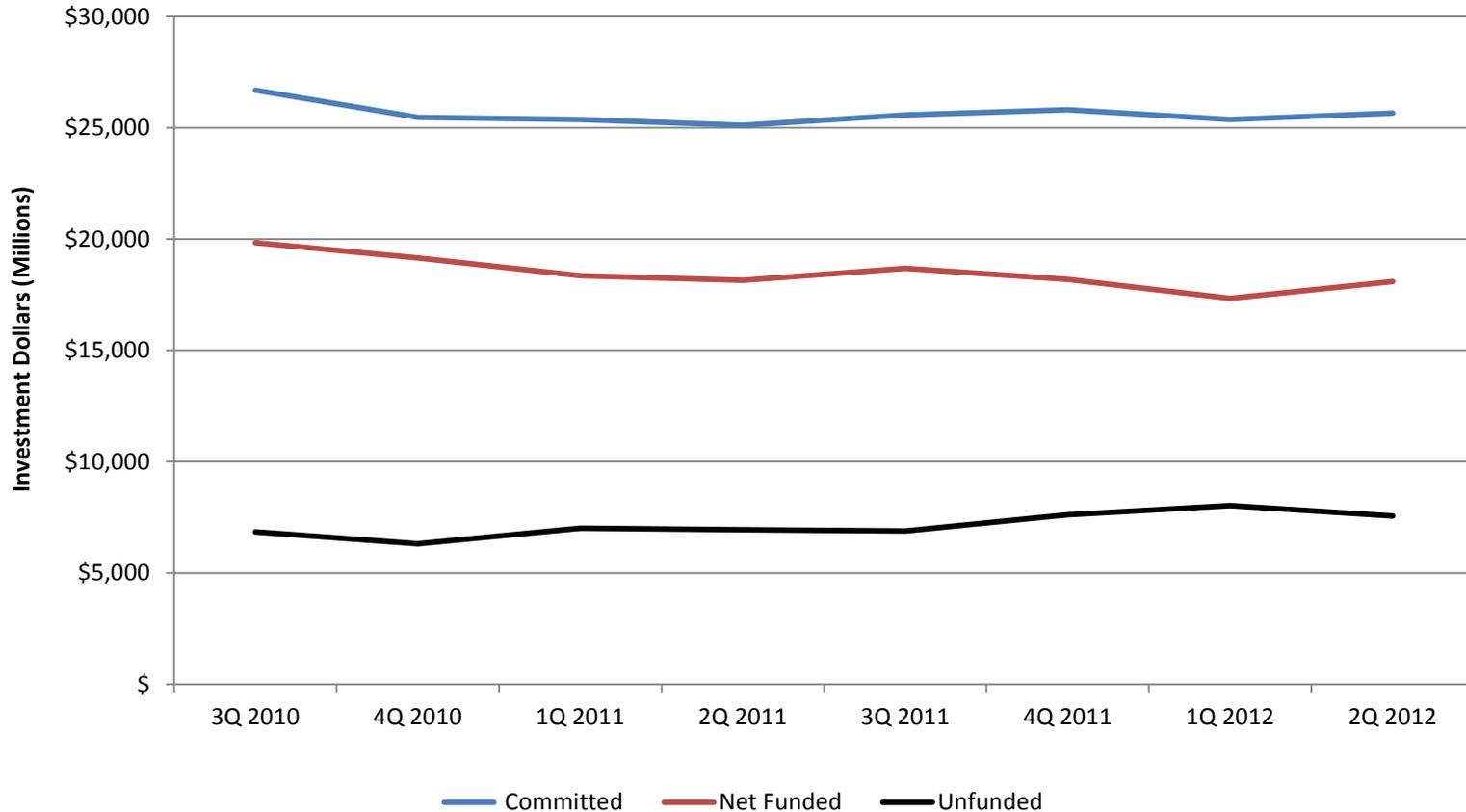
## By Global Region



<sup>1</sup> Benchmark: NCREIF Fund Index - Open-End Diversified Core Equity (NFI-ODCE)

<sup>2</sup> Property Type labeled "Other" includes: Entertainment, Healthcare Facilities, Housing, Land, Mixed Use, Senior Housing, etc.

# Capital Allocation



# Market History Snapshot

## Real Estate ( Quarter Trend | Annual Trend )

	Apartment		Industrial		Office		Retail	
Cap Rates	↔	↔	↔	↔	↔	↘	↔	↘
Vacancy Rates	↘	↘	↘	↘	↘	↘	↔	↔
Absorption	↗	↗	↗	↗	↗	↗	↔	↗
Rent	↔	↗	↔	↔	↗	↗	↔	↔

## Real Estate Market History Comments

- Fundamentals and capital markets continued to show slow and steady improvement during Q2 2012.
- Capitalization rates have leveled off for all sectors. Retail and Office have shown a slight decline in cap rates over the past year.
- Vacancy rates declined on an annual basis in all sectors, the Industrial sector showed the most improvement the past year.
- Apartments are leading and Retail is lagging in product absorption during the past quarter and year.
- In this quarter, rents remained relatively flat in all sectors except for Office which has shown steady improvement all year.

Increasing rapidly  
 Increasing moderate pace  
 No change or flat  
 Decreasing moderate pace  
 Decreasing rapidly

**Commercial Real Estate Indicator Notes:** Data is the most current quarterly data, which lags the Program Update Quarter End date by one quarter.  
**Source:** CBRE Econometric Advisors and National Council of Real Estate Investment Fiduciaries (NCREIF)

# Performance: Overview

## Total Real Estate Portfolio

- The total Real Estate portfolio returns exceeded the benchmark for the 1 year period.

## Strategic Portfolio

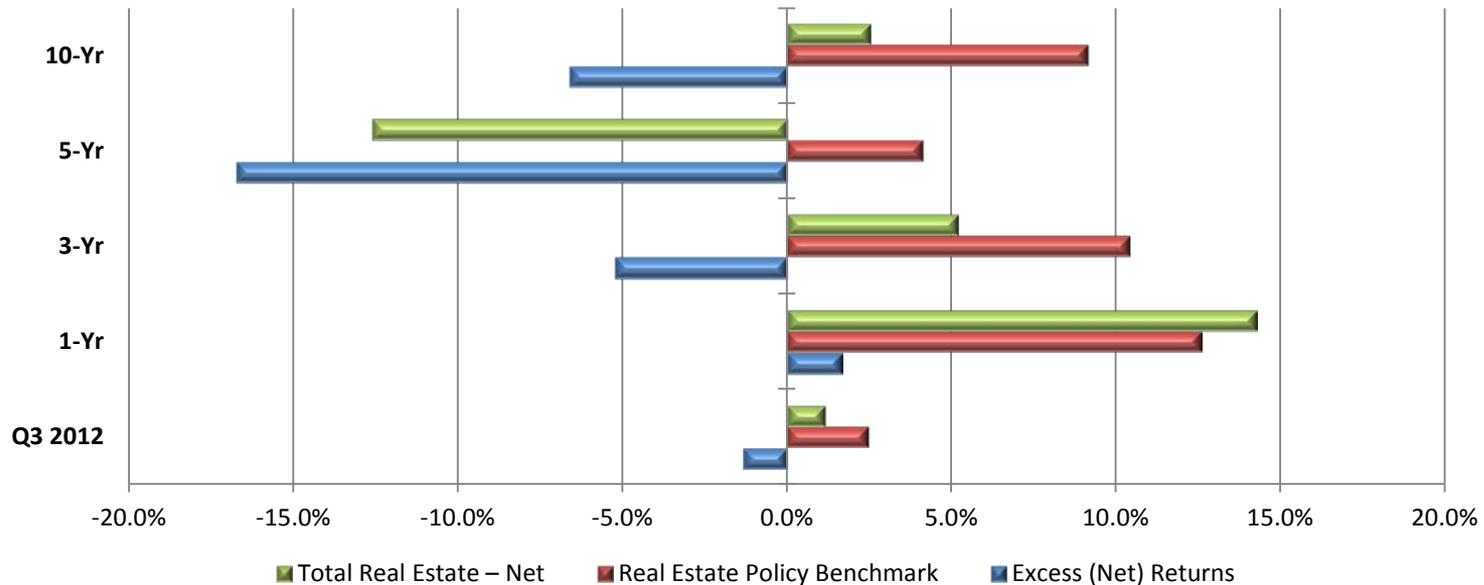
- The Strategic Portfolio, which represents 63% of the portfolio, out performed the benchmark on a 1 year, 3 year, 5 year, 10 year, and since inception.

## Legacy Portfolio

- The Legacy Portfolio, which represents 37% of the portfolio and the Public Real Estate Securities, underperformed the benchmark for all time periods.

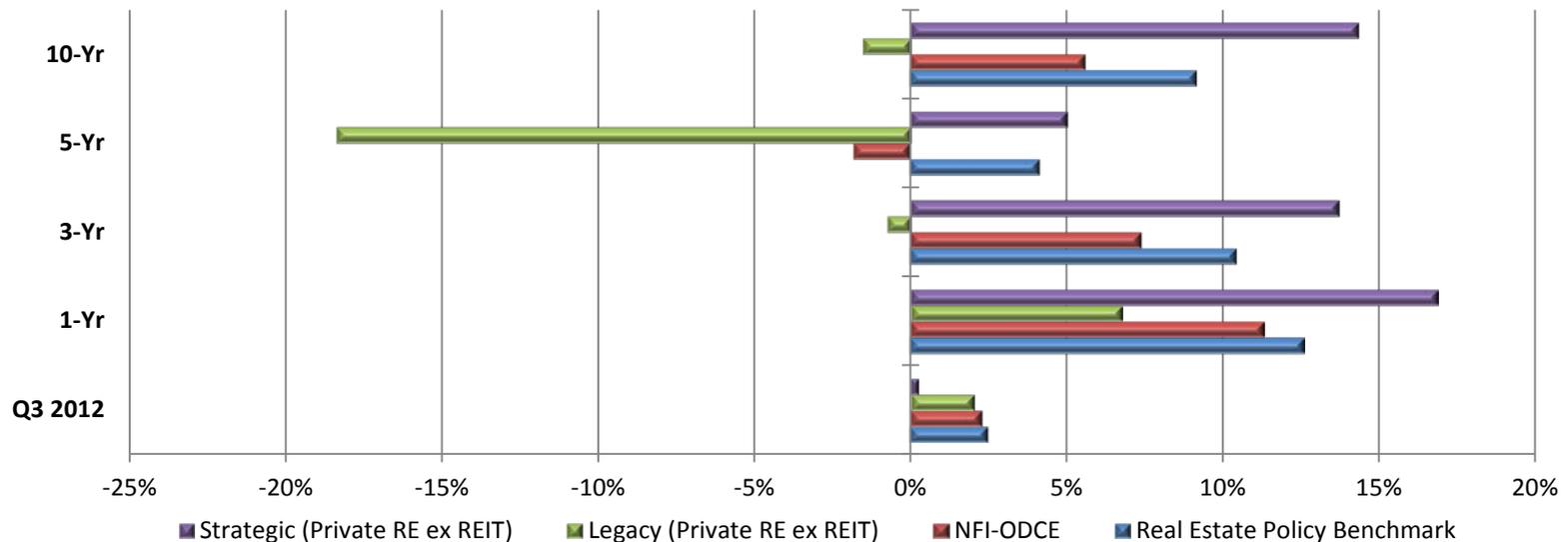
# Performance: Portfolio Returns

Nominal Returns	Q3 2012	1-Yr	3-Yr	5-Yr	10-Yr
Total Real Estate – Net	1.2%	14.3%	5.2%	-12.6%	2.5%
Real Estate Policy Benchmark	2.5%	12.6%	10.4%	4.1%	9.2%
<b>Excess (Net) Returns</b>	<b>-1.3%</b>	<b>1.7%</b>	<b>-5.2%</b>	<b>-16.7%</b>	<b>-6.6%</b>



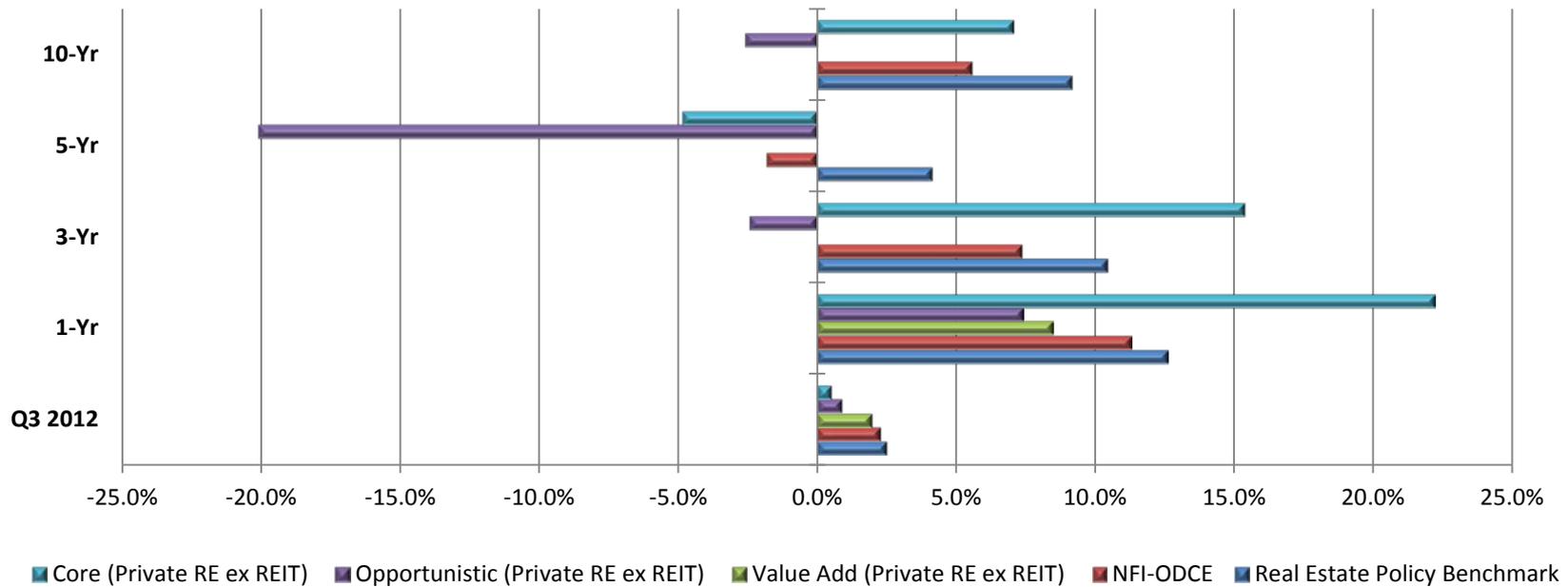
# Performance: Net Returns by Strategy

Private Real Estate	Q3 2012	1-Yr	3-Yr	5-Yr	10-Yr
Strategic (Private RE ex REIT)	0.3%	16.9%	13.7%	5.0%	14.3%
Legacy (Private RE ex REIT)	2.0%	6.8%	-0.8%	-18.4%	-1.5%
NFI-ODCE	2.3%	11.3%	7.4%	-1.8%	5.6%
Real Estate Policy Benchmark	2.5%	12.6%	10.4%	4.1%	9.2%



# Performance: Net Returns by Risk Category

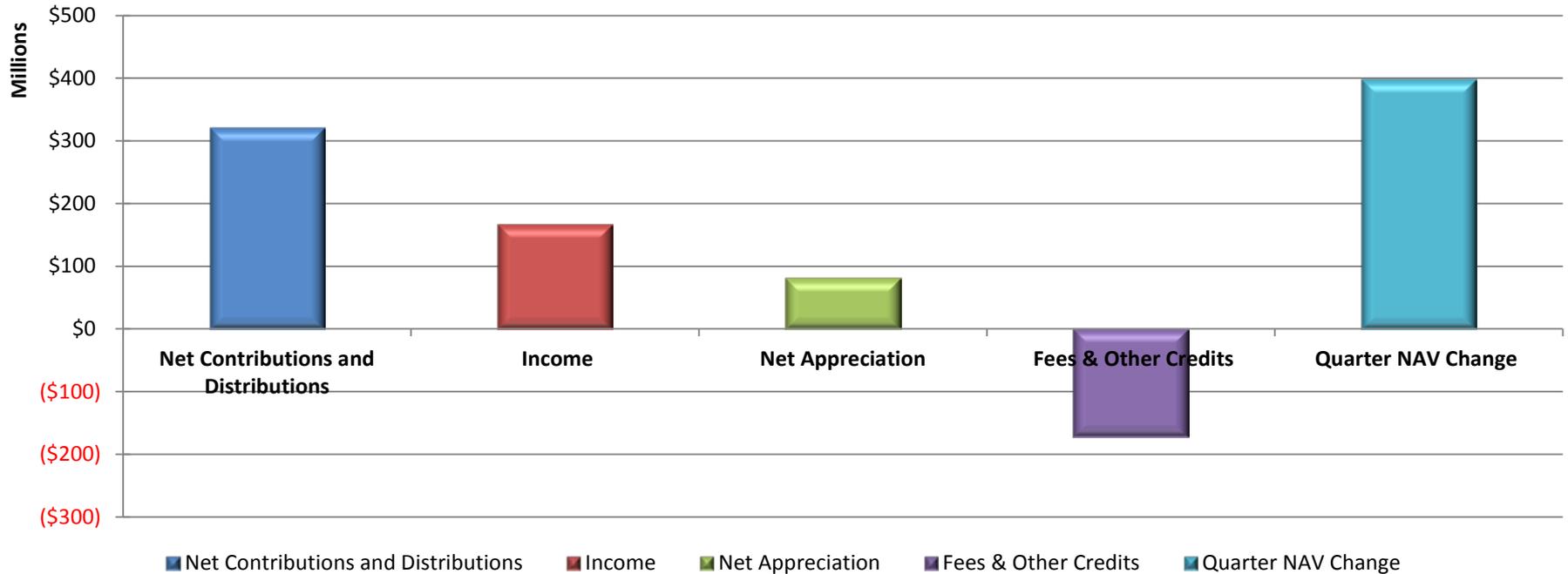
Private Real Estate (RE)	Q3 2012	1-Yr	3-Yr	5-Yr	10-Yr
Core (Private RE ex REIT)	0.5%	22.2%	15.4%	-4.8%	7.1%
Value Add (Private RE ex REIT)	2.0%	8.5%	n/a	n/a	n/a
Opportunistic (Private RE ex REIT)	0.9%	7.4%	-2.4%	-20.1%	-2.6%
NFI-ODCE	2.3%	11.3%	7.4%	-1.8%	5.6%
Real Estate Policy Benchmark	2.5%	12.6%	10.4%	4.1%	9.2%



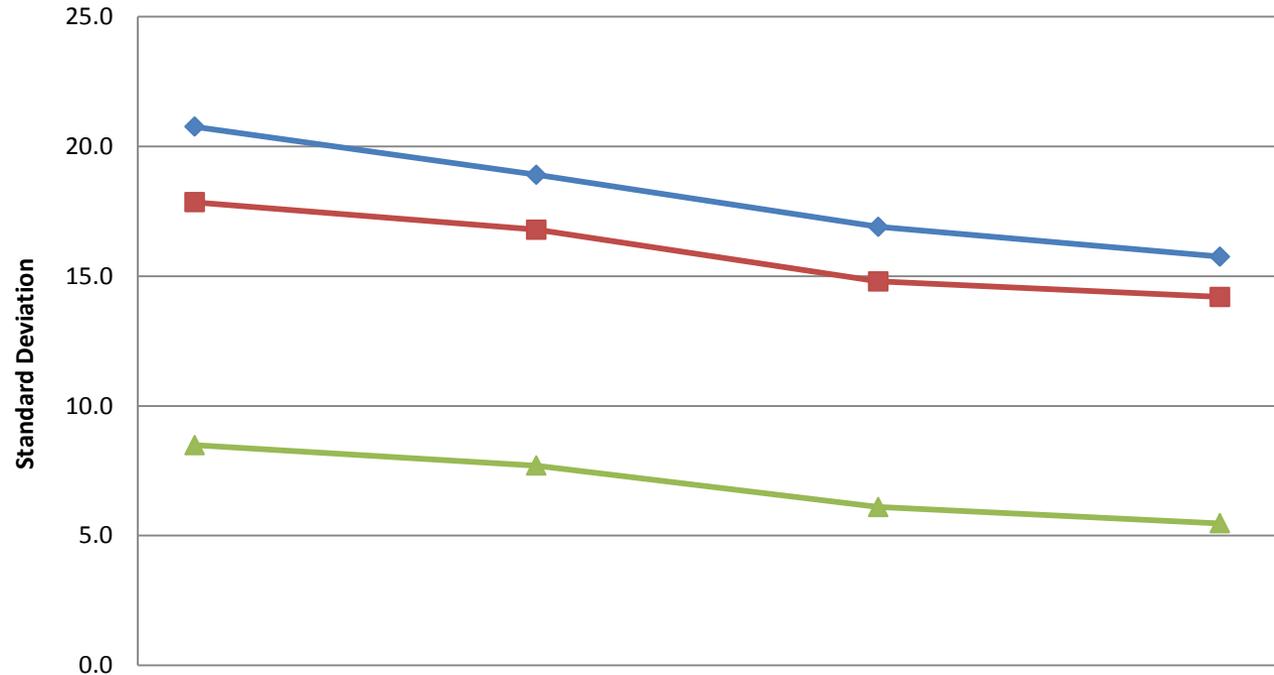
# Quarterly NAV Change Analysis (in millions)

Asset Class	(+) BNAV	(+) Contribution	(-) Distribution	(+) Income	(+) Unrealized Appreciation	(+) Realized Appreciation	(-) Fees	Other Credits (-)	(-) ENAV
Real Estate Investments	\$21,092	\$1,632	\$1,207	\$168	\$32	\$50	\$54	\$118	\$21,492

Quarterly NAV change **\$400**



# Total Portfolio Risk Trending



	9/30/2011	12/31/2011	3/31/2012	6/30/2012
◆ Total Real Estate Portfolio Risk	20.8	18.9	16.9	15.8
■ RE Policy Benchmark Risk	17.9	16.8	14.8	14.2
▲ Active Risk	8.5	7.7	6.1	5.5

\*Output from BarraOne Risk System based on RE 6/30/12 Values

# Investment Activity

- The Real Estate Program's capital allocation request of \$6 billion for Fiscal Year 2012-13 was approved by the Investment Strategy Group in June 2012.
- Allocated approximately \$4 billion to the Strategic Portfolio.
- Deployed \$436 million (Strategic \$368 million, Legacy \$68 million) for land and building purchases during the first quarter of activity from July 1, 2012 - September 30, 2012.
- Dispositions totaled \$413 million (Strategic \$99 million, Legacy \$314 million) for sale or partial sale of investments during the first quarter of activity from July 1, 2012 - September 30, 2012.