

Michael C. Schlachter, CFA
Managing Director & Principal

March 28, 2013

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

Re: Absolute Return Strategies Policy

Dear Mr. Jones,

You requested our opinion regarding the agenda item from Staff that presents the revisions to the policy for the Absolute Return Strategies program.

Recommendation

Wilshire recommends that the Investment Committee adopt the revisions to the policy as presented by Staff, subject to the discussion regarding the purpose of the ARS program outlined below.

Discussion

As we outlined in our letters of January 29, 2013 (which commented on Staff's annual review of the ARS program) and March 4, 2013 (which commented on the first reading of this policy) , we have long supported the idea of shifting the ARS program to a diversification role, without a public markets overlay, through a dedicated allocation to hedge funds. However, as we also outlined in that letter, this change will have an impact on the expected return for the total fund, especially if the allocation to ARS is increased as a result of the ALM process. While we do not believe that this should prevent the Investment Committee from treating ARS as a diversifying investment, it should be aware of the implications of doing so.

The other significant changes made to the policy explicitly state the expected risk and the residual market exposure for the first time and reduce the monthly expected loss target in the portfolio. We view both of these as positive steps by Staff toward their goal of reducing the overall volatility in the ARS program.



Since the first reading, Staff has made one minor revision to the lists of the types of hedge funds at the request of an Investment Committee member. The change made by Staff is consistent with the request of that member.

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

Best regards,

A handwritten signature in black ink, appearing to read 'Michael A. ...'.