



**Julia K. Bonafede, CFA**  
**President of Wilshire Consulting**

August 22, 2014

Mr. Henry Jones  
Chairman of the Investment Committee  
California Public Employees' Retirement System  
400 P Street, Suite 3492  
Sacramento, CA 95814

Re: Affiliate Funds Strategic Asset Allocation Targets, Recommendations

Dear Mr. Jones:

At the August 2014 Investment Committee meeting, Staff presented analysis supporting the proposed recommendations for the following Affiliate Funds:

- California Employers' Retiree Benefit Trust (CERBT)
- Legislators' Retirement Fund (LRS)
- Judges' Retirement Fund (JRS)
- Judges' Retirement II Fund (JRS II).

Wilshire worked closely with staff on these revisions and the resulting changes to the current asset class allocations. Our recommendation is below.

### **Recommendation**

As noted in our opinion letter dated July 31, 2014, Wilshire has reviewed the strategic asset allocation analysis and the recommended policy portfolios and believe the new asset allocation targets to be prudent given the unique liability streams associated with each fund. We find Staff's rationale for each portfolio recommendation to be thoughtful, appropriate, and in line with CalPERS' Investment Beliefs.

As mentioned in our July letter, the policy portfolio recommendations for each of the four Affiliate Funds reflect a reduction in the overall risk profile for each fund, with the exception of JRS. This reduction in risk is a direct result of a meaningful reduction in the equity allocation of each portfolio thereby reducing overall Growth risk. While this reduction in equity exposure should dampen total volatility, it does increase other risk exposures for these Affiliates. Specifically, as the exposure to fixed income increases, the portfolios will be more exposed to performance issues should interest rates rise significantly. Given the

current state of low interest rates and the planned wind down of Federal Reserve stimulus in the United States, increasing interest rates are possible.

Even with the prospect of a potential higher interest rate environment the recommended policy portfolios offer a reasonable risk/reward profile given the changing demographics of each fund.

We are always available to answer any questions you may have or receive comments.

Sincerely,

A handwritten signature in blue ink, appearing to read "John K. B...". The signature is fluid and cursive, with a long horizontal stroke at the end.