

Real Assets Annual Program Review - Supplemental Report

Period Ending June 30, 2014

Investment Objective

The role of Real Estate is to have ownership risk in real property with stable cash yield and act as an economic diversifier to equity risk. Capital appreciation is an added, but lower source of return.

- CalPERS ALM Workshop (2013)

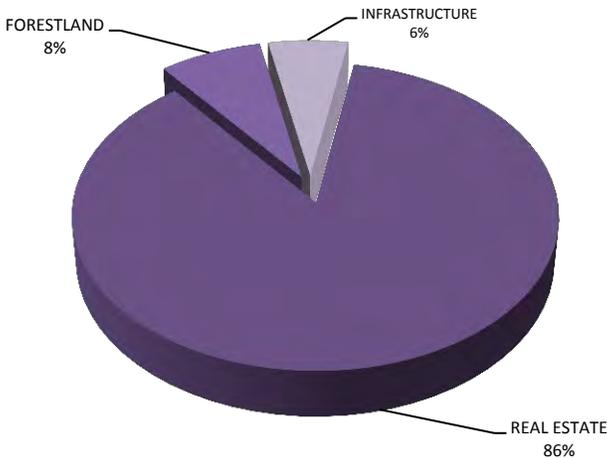
The role of Forestland is to have ownership risk in forestland properties, enhance long-term inflation protection and provide moderate cash yield.

- CalPERS ALM Workshop (2013)

The role of Infrastructure is to have ownership risk in essential infrastructure assets and provide predictable returns with moderate long-term inflation protection. Infrastructure also acts as an economic diversifier to equity risk.

- CalPERS ALM Workshop (2013)

Real Assets Programs



Asset Class Characteristics

Acting Senior Investment Officer: Tom McDonagh

Assets: \$30.0 Billion

Benchmark: 77% Real Estate benchmark + 15% Infrastructure benchmark + 8% Forestland benchmark

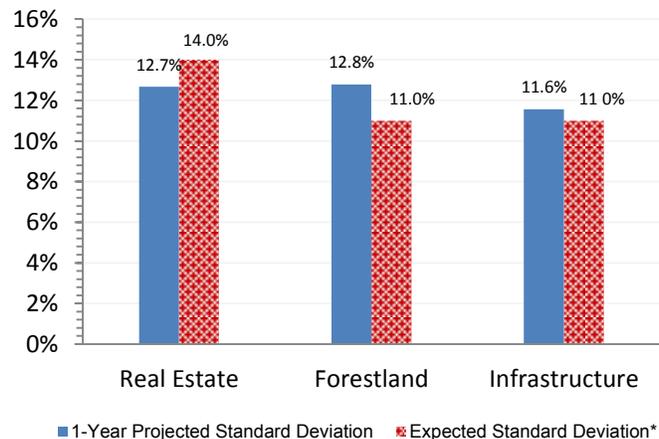
- Real Estate Program
Benchmark: Exceed NCREIF ODCE
 - Stable cash yield with real property ownership
 - Acts as a partial inflation hedge
- Forestland Program
Benchmark: NCREIF Timberland
 - Forestland properties ownership
 - Inflation protection, illiquid
- Infrastructure Program
Benchmark: CPI +4%, lagged one quarter
 - Predictable returns with essential infrastructure assets ownership
 - Economic diversifier

| Class Allocation | Real Estate | Forestland | Infrastructure |
|-----------------------------|-----------------|-----------------|-----------------|
| Strategic Target Range % | 5-15% | 0-2% | 0-2% |
| Interim Strategic Target % | 12% | 1% | 1% |
| Actual Investment % | 9% | 1% | 1% |
| Variance | -3% | (0%) | (0%) |
| Interim Strategic Target \$ | \$ 36.0 Billion | \$ 3.0 Billion | \$ 3.0 Billion |
| Actual Investment \$ | \$ 30.0 Billion | \$ 2.3 Billion | \$ 1.8 Billion |
| Variance \$ | \$(6.1 Billion) | \$(0.7 Billion) | \$(1.2 Billion) |

Note: Strategic Target effective July 1, 2014

Asset Liability Management Expectations

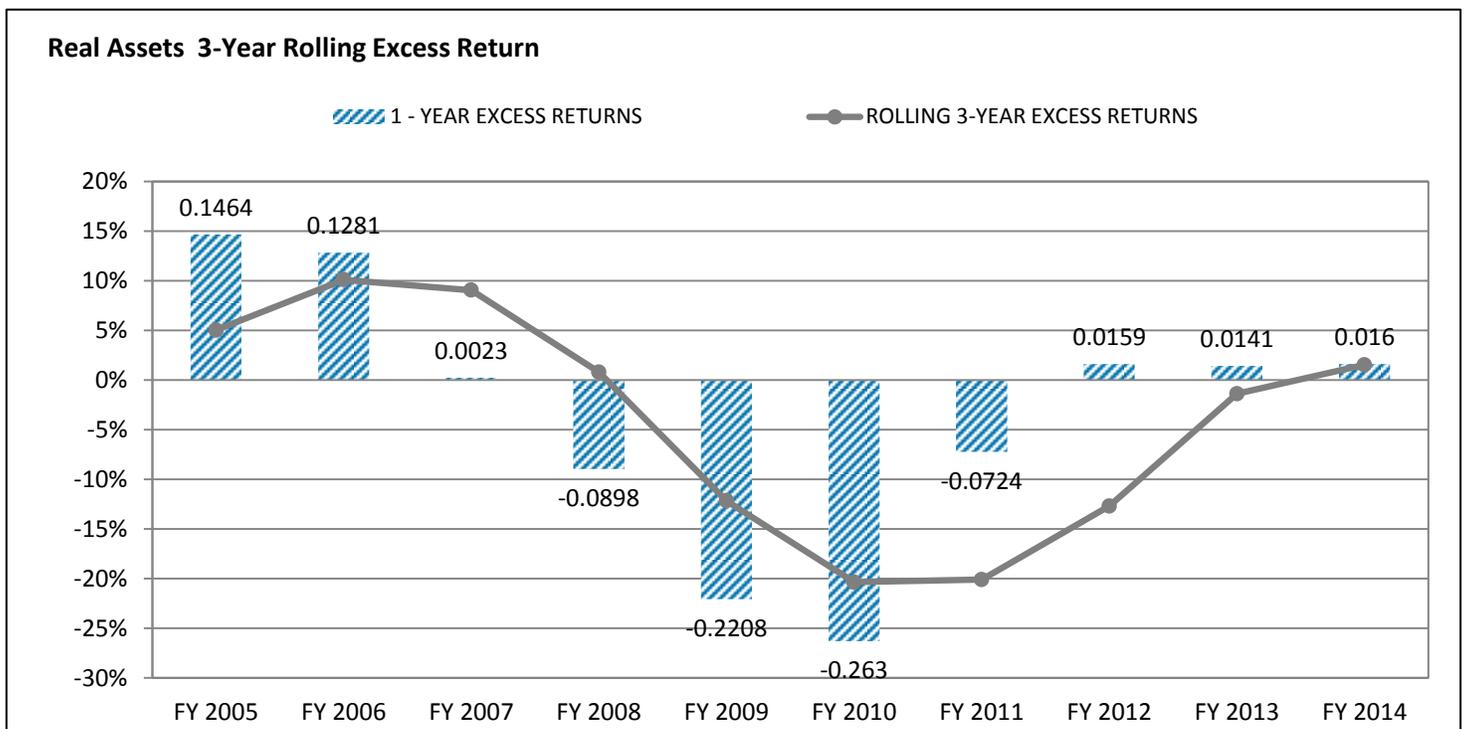
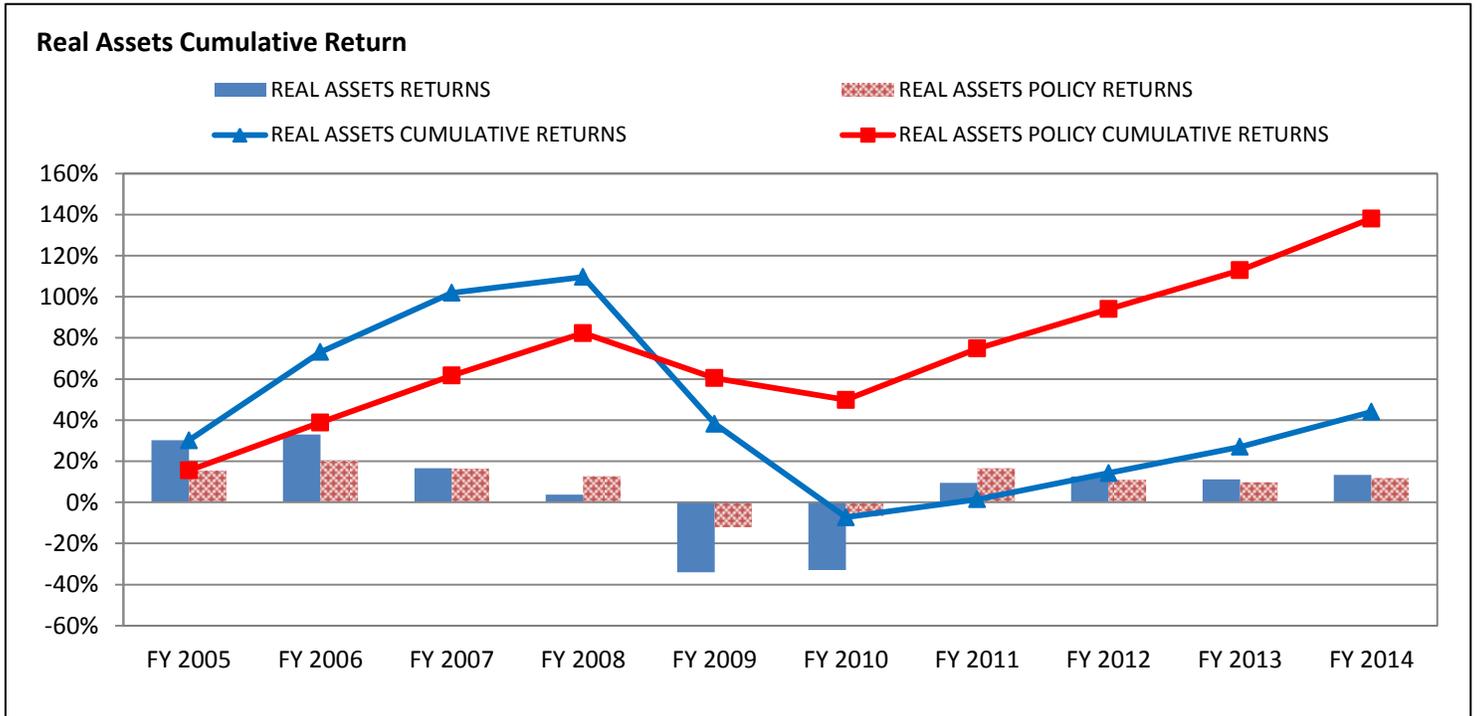
*Capital markets assumptions used in the 2013 ALM Workshop



REAL ASSETS PERFORMANCE

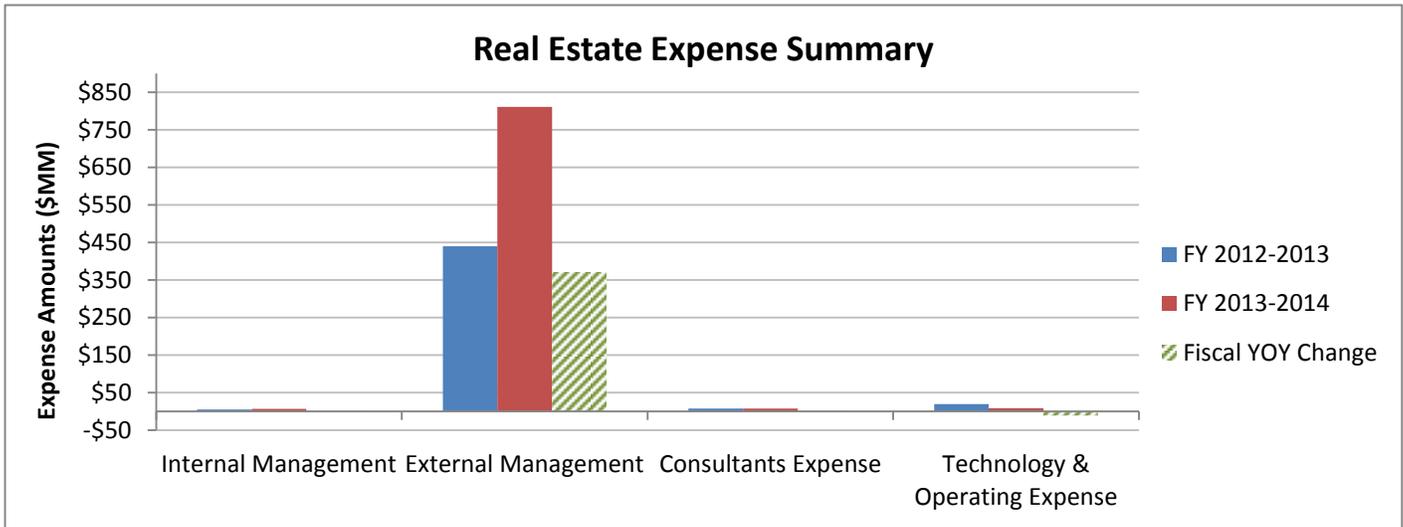
| MONTH ENDING JUNE 30, 2014 | | FYTD | | 3-YR | | 5-YR | | 10-YR | |
|----------------------------|-----------------------|--------------|------------|--------------|------------|-------------|--------------|-------------|--------------|
| Asset Class* | Ending Market Value | Net Return | Excess BPS | Net Return | Excess BPS | Net Return | Excess BPS | Net Return | Excess BPS |
| REAL ASSETS | \$ 30. Billion | 13.4% | 160 | 12.4% | 153 | 0.8% | (739) | 3.7% | (535) |
| REAL ESTATE | \$ 25.9 Billion | 13.9% | 121 | 13.9% | 202 | 0.5% | (937) | 3.1% | (659) |
| FORESTLAND | \$ 2.3 Billion | 2.5% | (724) | (1.0%) | (753) | (0.8%) | (363) | N/A | N/A |
| INFRASTRUCTURE | \$ 1.8 Billion | 22.8% | 1723 | 12.0% | 610 | 23.3% | 1659 | N/A | N/A |

* Performance for the total asset class and top 3 strategies based on ending market value

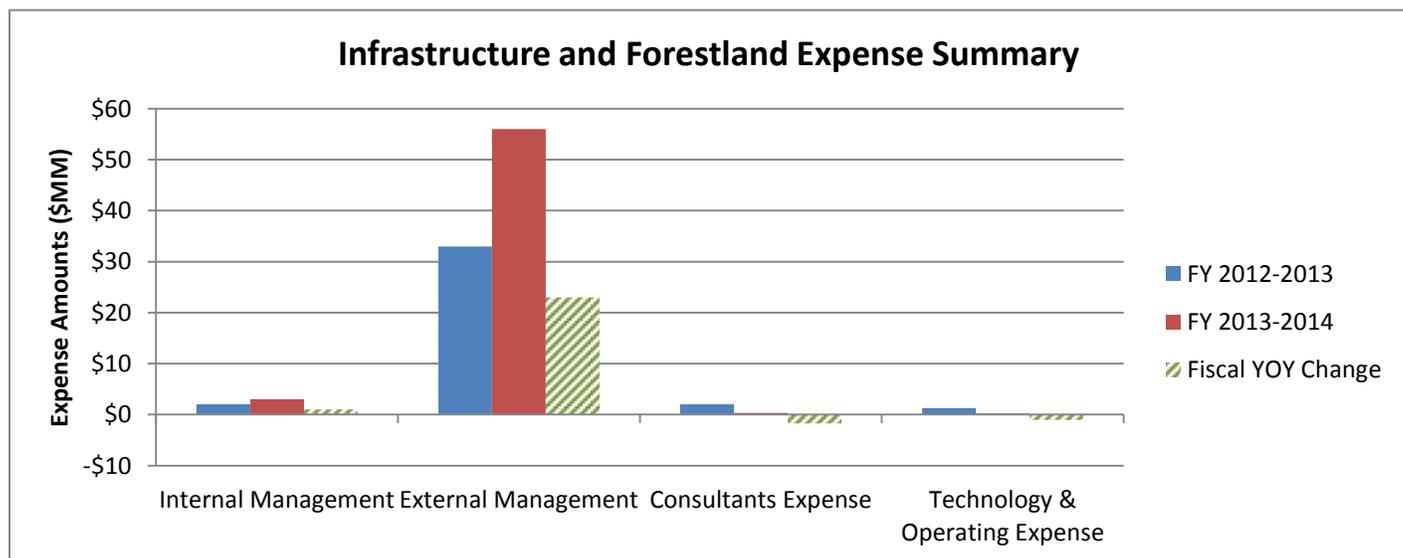


EXPENSES

| Real Estate Expenses | FY 2012-2013 | FY 2013-2014 | Fiscal YOY Change |
|--------------------------------|--------------|--------------|-------------------|
| | (\$millions) | (\$millions) | (\$millions) |
| Internal Management | \$5 | \$7 | \$1 |
| External Management | \$440 | \$811 | \$371 |
| Consultants Expense | \$7 | \$8 | \$0 |
| Technology & Operating Expense | \$20 | \$9 | (\$11) |



| Infrastructure and Forestland Expenses | FY 2012-2013 | FY 2013-2014 | Fiscal YOY Change |
|--|--------------|--------------|-------------------|
| | (\$millions) | (\$millions) | (\$millions) |
| Internal Management | \$2 | \$3 | \$1 |
| External Management | \$33 | \$56 | \$23 |
| Consultants Expense | \$2 | \$0 | (\$2) |
| Technology & Operating Expense | \$1 | \$0 | (\$1) |



STAFFING

| Senior Management Team | Years with CalPERS | Years Experience |
|------------------------------|--------------------|------------------|
| Tom McDonagh - Acting SIO | 8 | 28 |
| Randy Pottle - SPM | 14 | 26 |
| Jim Hurley - SPM | 6 | 25 |
| Randall Mullan - SPM | 5 | 25 |
| Investment Team | Number of Members | |
| Portfolio Managers | 12 | |
| Investment Officers | 29 | |
| Additional Resources | Number of Members | |
| Administrative Support Staff | 14 | |

Real Assets Staffing Updates

- Hired 1 Portfolio Manager
- Hired 6 Investment Officers
- Current Vacancies
 - 1 Portfolio Manager
 - 2 Investment Officers
 - 1 Staff Services Analyst
 - 2 Office Technicians

POLICY

| REVIEWED | AMEND | POLICY/DELEGATION NAME | ACTION |
|----------|-------|------------------------|--------|
| ✓ | NO | Real Assets Policy | None |

CalPERS INVESTMENT BELIEFS

CalPERS Investment Beliefs

#1 Liabilities must influence the asset structure

Real Assets' role, according to the ALM, is to provide long- term stable income, cash yield, and a partial hedge to inflation to match liabilities.

#2 A long time investment horizon is a responsibility and an advantage

Real Assets' strategy is to invest in long-term income producing properties.

#3 CalPERS investment decisions may reflect wider stakeholder views, provided they are consistent with its fiduciary duty to members and beneficiaries

Engagement with Global Governance.

#4 Long-term value creation requires effective management of three forms of capital: financial, physical and human

Sustainability monitoring tools and portfolio policy compliance ensure portfolios are managed according to expectations. Have established leadership with regard to alignment of financial interests and responsible contracting.

#5 CalPERS must articulate its investment goals and performance measures and ensure clear accountability for their execution

Real Assets has clearly stated benchmarks and internal staff compensation is aligned using 3-year rolling excess returns.

#6 Strategic asset allocation is the dominant determinant of portfolio risk and return

The role of real assets, the strategic plan, and the benchmark are all consistent with the Strategic Asset Allocation.

#7 CalPERS will take risk only where we have a strong belief we will be rewarded for it

A majority of the program (75%) to be invested in high quality well located assets held long term with limits and governance on debt financing. Further, staff actively measures risk in determining and underwriting its risk/reward profile.

#8 Costs matter and need to be effectively managed

Management of portfolio consistent with costs of the benchmark as well as external management fee reductions are top Real Assets priority.

#9 Risk to CalPERS is multi-faceted and not fully captured through measures such as volatility or tracking error

Staff has implemented detailed risk measurements for portfolio components.

#10 Strong processes and teamwork and deep resources are needed to achieve CalPERS goals and objectives

Enhanced training has taken team on path to be a world class investment management group. Existing need for enhancement of IT systems.