

May 16, 2016

**Item Name:** Investment Office Roadmap and Target Operating Model Update

**Program:** Total Fund

**Item Type:** Information

**Executive Summary**

This agenda item provides an update on the Investment Office (INVO) business plan and related initiatives, including progress on the INVO Roadmap and Target Operating Model (TOM), key components of the CalPERS overall Business Plan.

**Strategic Plan**

This agenda item supports the CalPERS Strategic Plan Goal A: Improve long-term pension and health benefit sustainability. Specifically, the INVO Roadmap supports delivering target risk-adjusted investment returns by implementing programs and initiatives that improve investment performance and ensure effective systems, operations, and controls.

**Background**

Since 2010, in alignment with the five-year CalPERS Strategic Plan and the two-year CalPERS business plan, INVO has created a rolling two-year INVO Roadmap to communicate strategic objectives and initiatives supporting key priorities and the CalPERS mission.

In 2014, with new senior leadership in place INVO refreshed its' 5-Year business plan and introduced the "INVO 2020 Vision". Foundational to the INVO 2020 Vision is the CalPERS Strategic plan and the Pension and Investment Beliefs. These critical components shaped new INVO Mission and Vision statements, first communicated to the INVO staff and Investment Committee in December 2014. These statements articulate INVO's mission of managing the CalPERS investment portfolio in a cost effective, transparent, and risk-aware manner in order to generate returns to pay benefits.

With the INVO 2020 Vision providing guidance and direction in early 2015 staff developed the INVO 2015-17 Roadmap (Roadmap) and 36 underlying initiatives focused on building repeatable, predictable, and scalable portfolios and investing practices. Five Strategic Objectives were developed:

- Capital Allocation
- Business Effectiveness
- Investment Beliefs and ESG
- Investment Platform and Controls
- Investment Risk Management

Integrated into the Roadmap is the Target Operating Model (TOM), which defines the people, process, technology, and data needed to effectively manage the CalPERS Investment portfolio. Through periodic risk assessment and comparison to industry benchmarks each TOM function is evaluated to determine the current level of operational risk. The level of operational risk informs the development of Roadmap initiatives and allocation of resources.

In April 2015, INVO staff conducted an Internal Risk Assessment and Cutter Associates performed industry benchmarking related to the TOM. The risk assessment included staff surveys, analysis of Operating Events, and review of INVO's operational practices against peers to determine relative risk level of each investment function. Information was provided to a focused project team and INVO Senior Management, who then evaluated, discussed, and finalized the 2015 TOM Dashboard. The updated risk levels and definitions also served to inform the development of the 2015-17 Roadmap initiatives. This information was presented to the Investment Committee in May of 2015.

### **Analysis**

In December 2015, staff reported on the status of the overall Roadmap to the Investment Committee. Since that time, significant progress has been made on the 36 Roadmap initiatives, with six having been completed and an additional ten anticipated for completion over the next month. Highlights of current Fiscal Year accomplishments are provided in Attachment 1.

In addition to the reported progress, staff is presenting an updated TOM Dashboard. Changes from December 2015 are the result of an Internal Risk Assessment, including analysis of the impact of Roadmap initiatives. The ongoing risk assessment framework presents a refinement to prior TOM risk assessments, which occurred biennially. Excluding a change in external environment, significant operating event or completion of a mitigation strategy each TOM function will be reviewed on a 12-month rotation, with prioritization and oversight by the INVO Operating Committee. As a result of this continuous, rolling review cycle, the Investment Committee can anticipate viewing updated TOM Dashboards at each semi-annual Roadmap update.

For the April 2016 Risk Assessment, the INVO Operating Committee approved reducing the estimated risk level for three TOM functions, as listed below.

- Investment Policy Delegation
- Investment Cash Processing and Forecasting
- Portfolio Management – Private Markets

The lower risk levels are due to significant efforts made on related Roadmap Initiatives.

Looking forward, INVO Executive staff has begun to develop key priorities for the INVO 2016-17 Roadmap, which is expected to include:

- Continued build-out of more effective investment risk and performance attribution review and analysis processes within and across asset classes;
- Developing enhanced governance and efficiencies in monitoring and engaging external managers and opportunistic investments;
- Exploring key considerations concerning business model, talent management, and locations related to investing in the future; and,
- Continuing the integration of CalPERS Investment Beliefs and ESG risk considerations into the investment decision-making process.

By the end of June 2016, staff will finalize the INVO 2016-17 Roadmap initiatives and report progress towards these efforts at the December 2016 Investment Committee.

**Budget and Fiscal Impacts**

Funding for Roadmap activities is included in the approved and existing INVO budget.

**Benefits and Risks**

The progress and completion of the 2015-17 Roadmap initiatives are an integral part of managing INVO's operational risks. As initiatives are completed, critical operational risks are expected to decrease in severity.

**Attachments**

Attachment 1 – Investment Office Roadmap and Target Operating Model Update

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Chief Operating Investment Officer

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**Theodore Eliopoulos**

Chief Investment Officer