

Strategic Business Models for Private Equity Investing

June 18, 2018

Ted Eliopoulos, *Chief Investment Officer*

Elisabeth Bourqui, *Chief Operating Investment Officer*

John Cole, *Investment Director*

Purpose

Higher returns:

A direct model allows CalPERS to better source and take advantage of investment opportunities in private equity.

Address costs:

Private equity's overall success can't be ignored, but its fees and expenses are higher than other asset classes. Over time, this model enables us to move away from asset-based fees and keep more money in the Fund.

Achieve asset allocation:

As the Fund grows, this model helps us maintain our target of investing about 10 percent of the total portfolio in private equity.

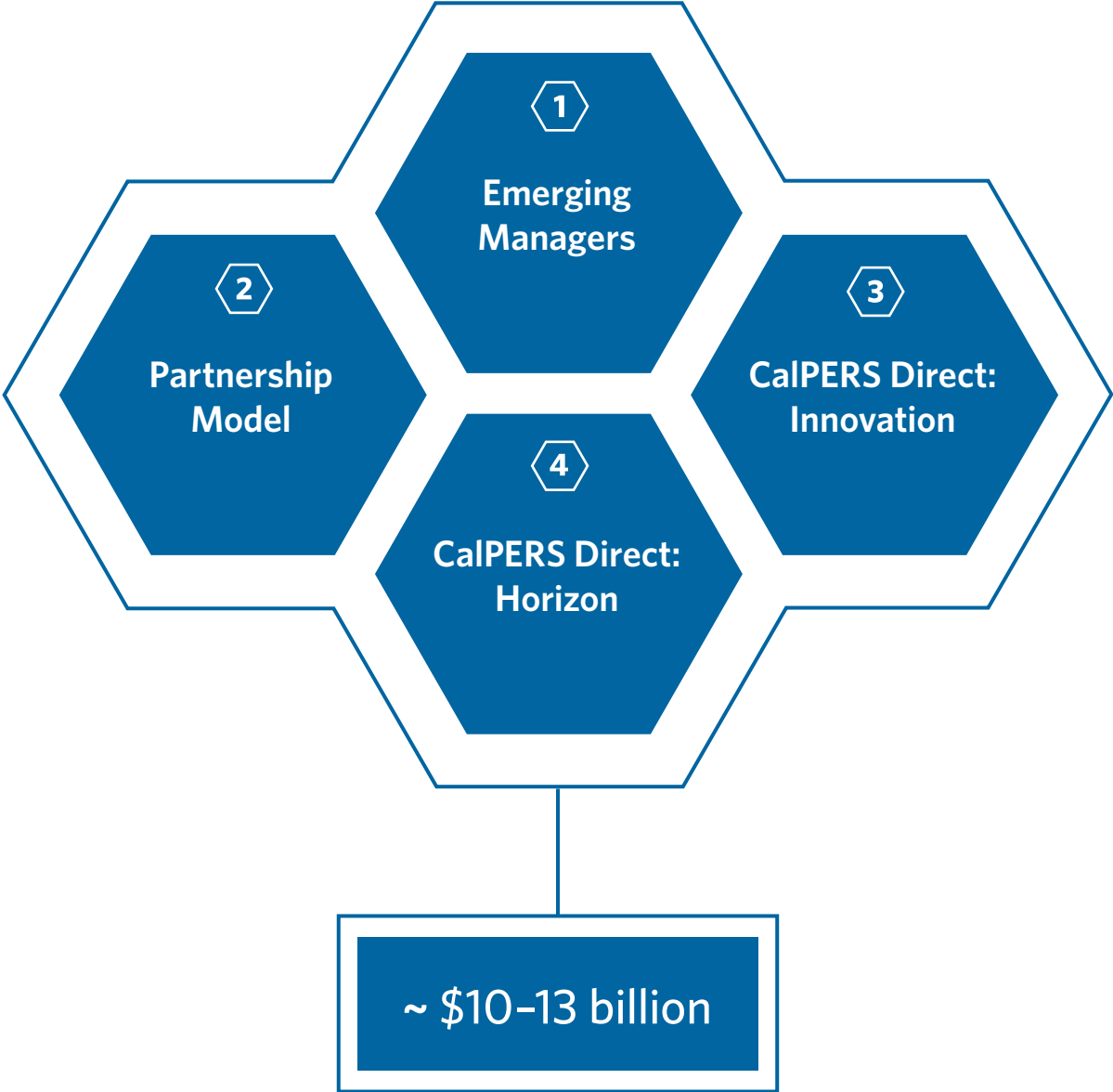
Framework

To develop an enduring and innovative framework that is focused on CalPERS' mission and beliefs, good governance practices, and striving for optimal alignment of interests.

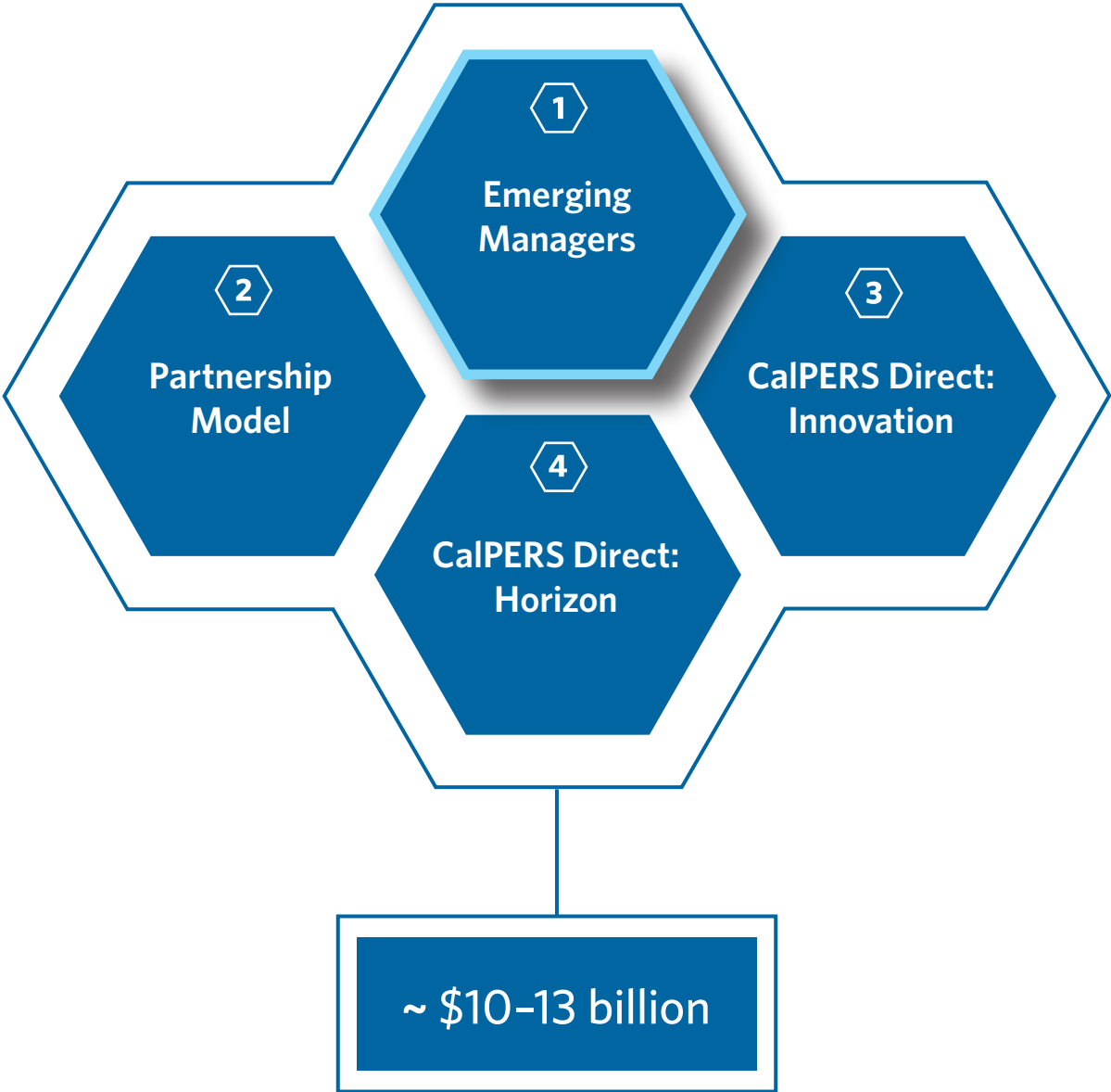
This framework is built with three key attributes in mind:

1. Adaptable as the industry evolves.
2. Invest in aggregate, both capably and continuously, at scale to maintain Private Equity at a material level (approximately 10% of Total Fund).
3. Focused on building a strong base of talent and relationships that will grow and strengthen over time.

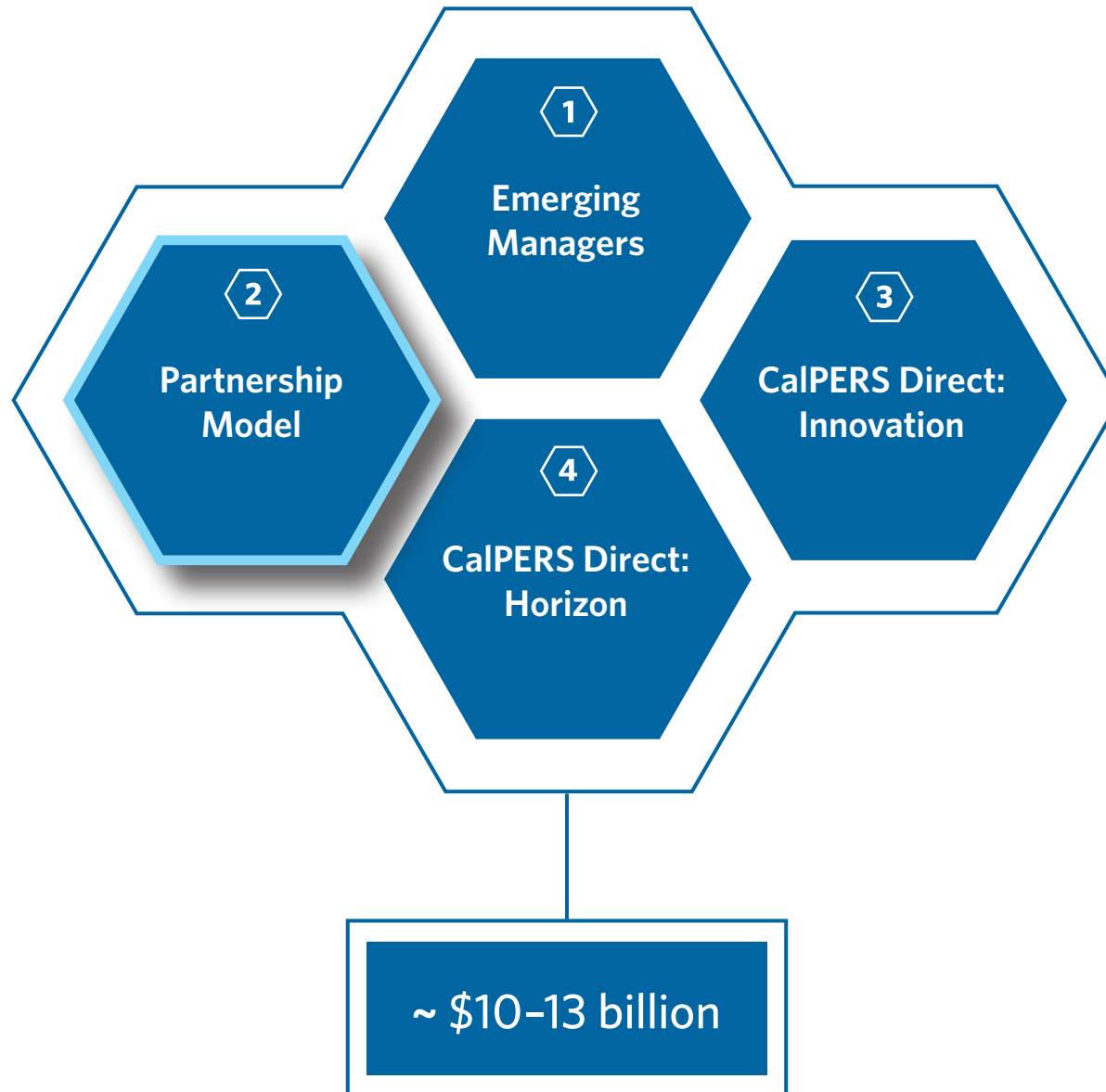
Private Equity Strategy Pillars



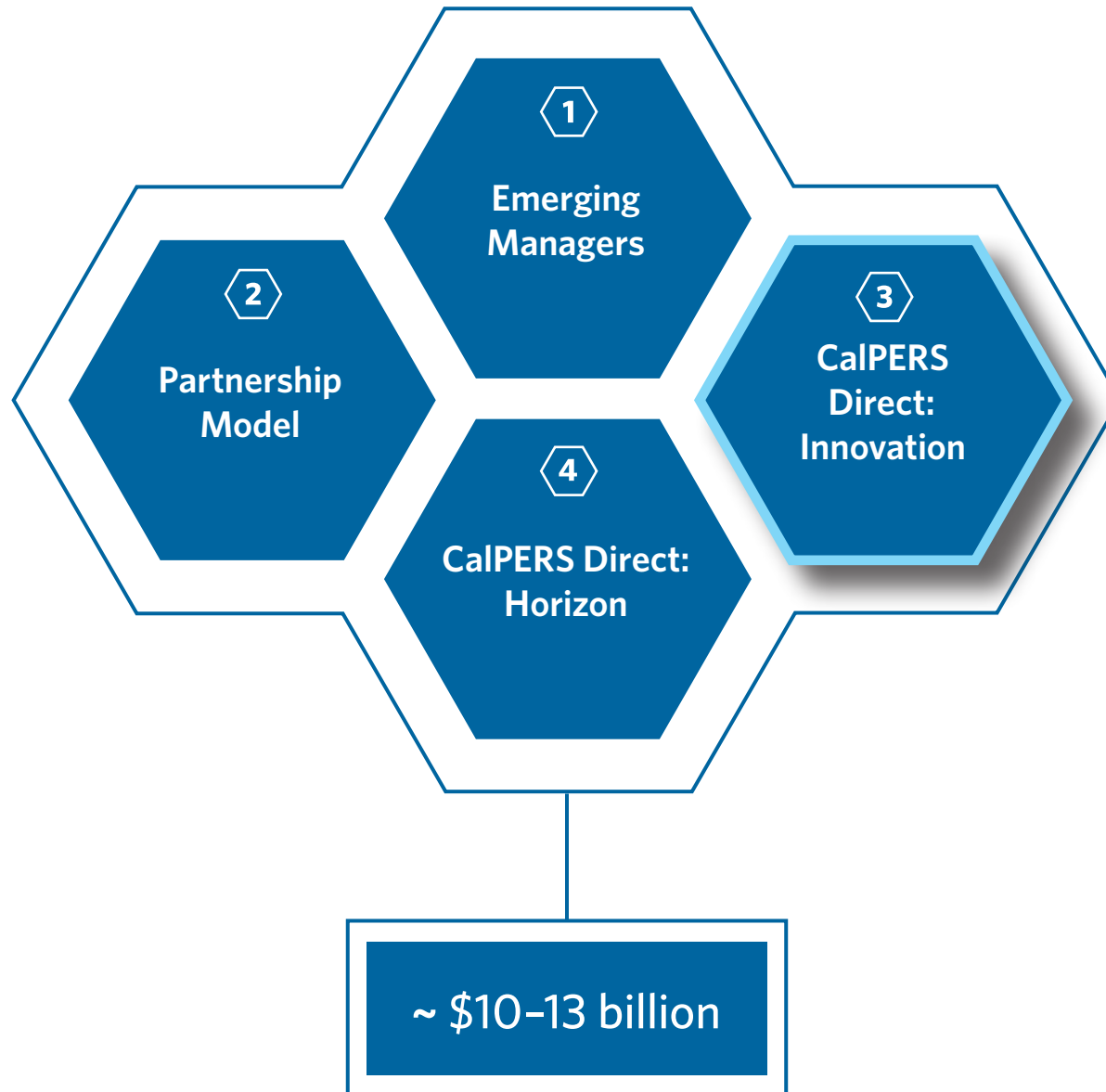
Private Equity Strategy Pillars



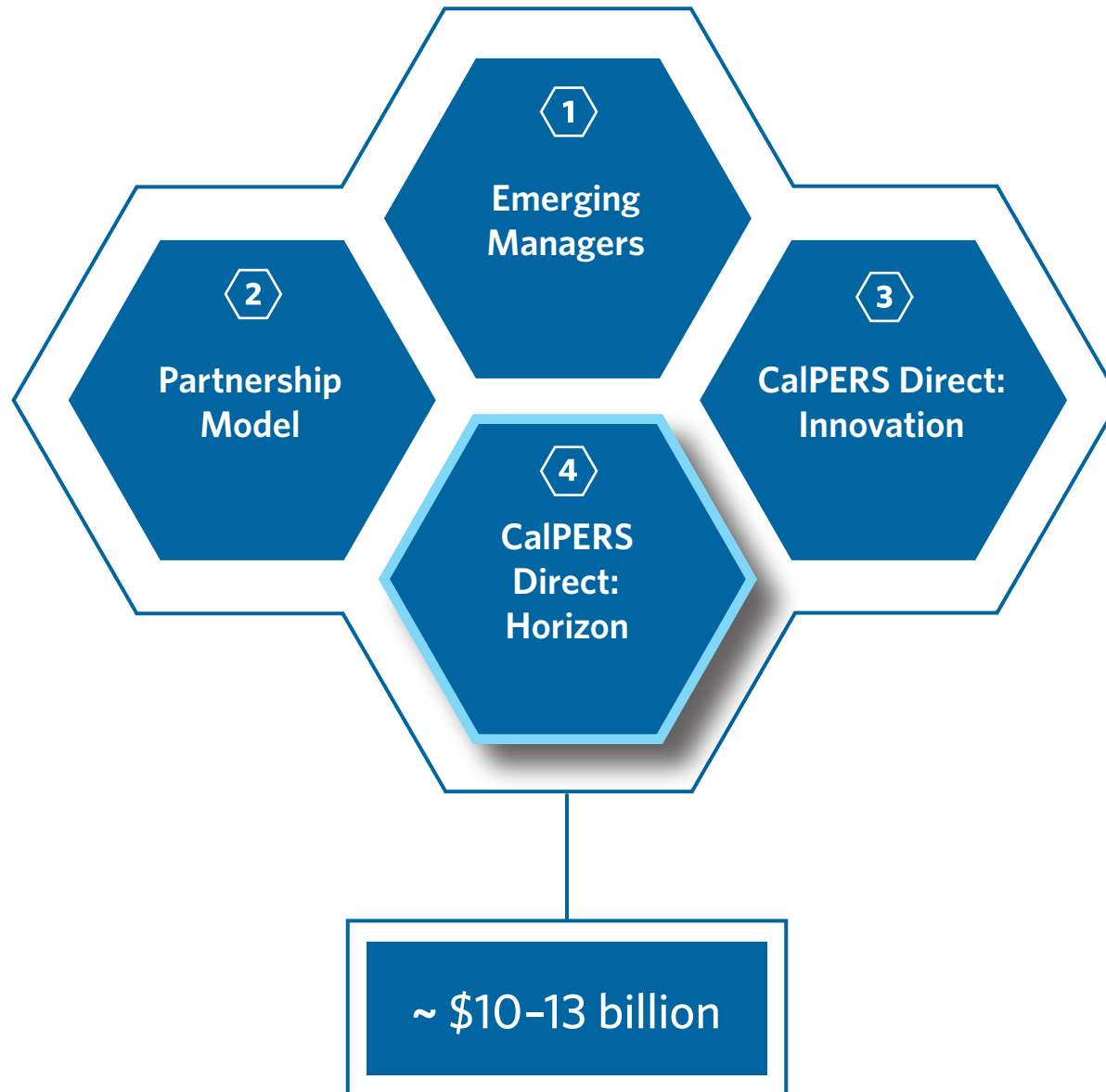
Private Equity Strategy Pillars



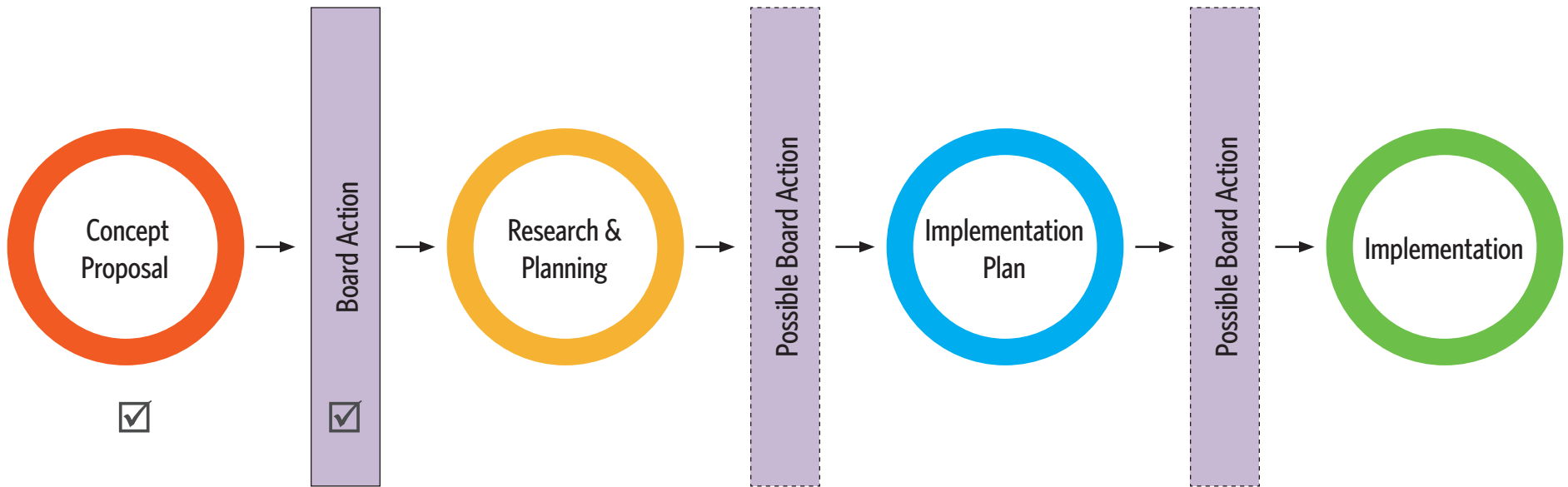
Private Equity Strategy Pillars



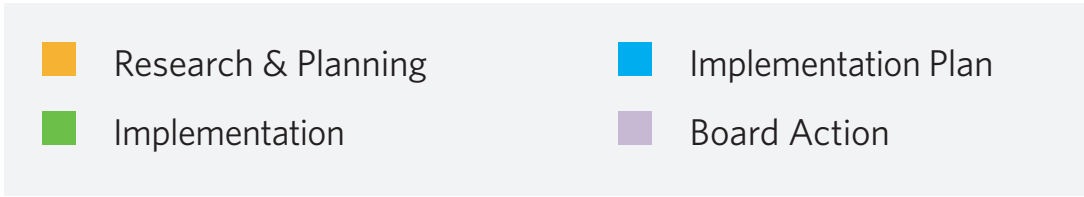
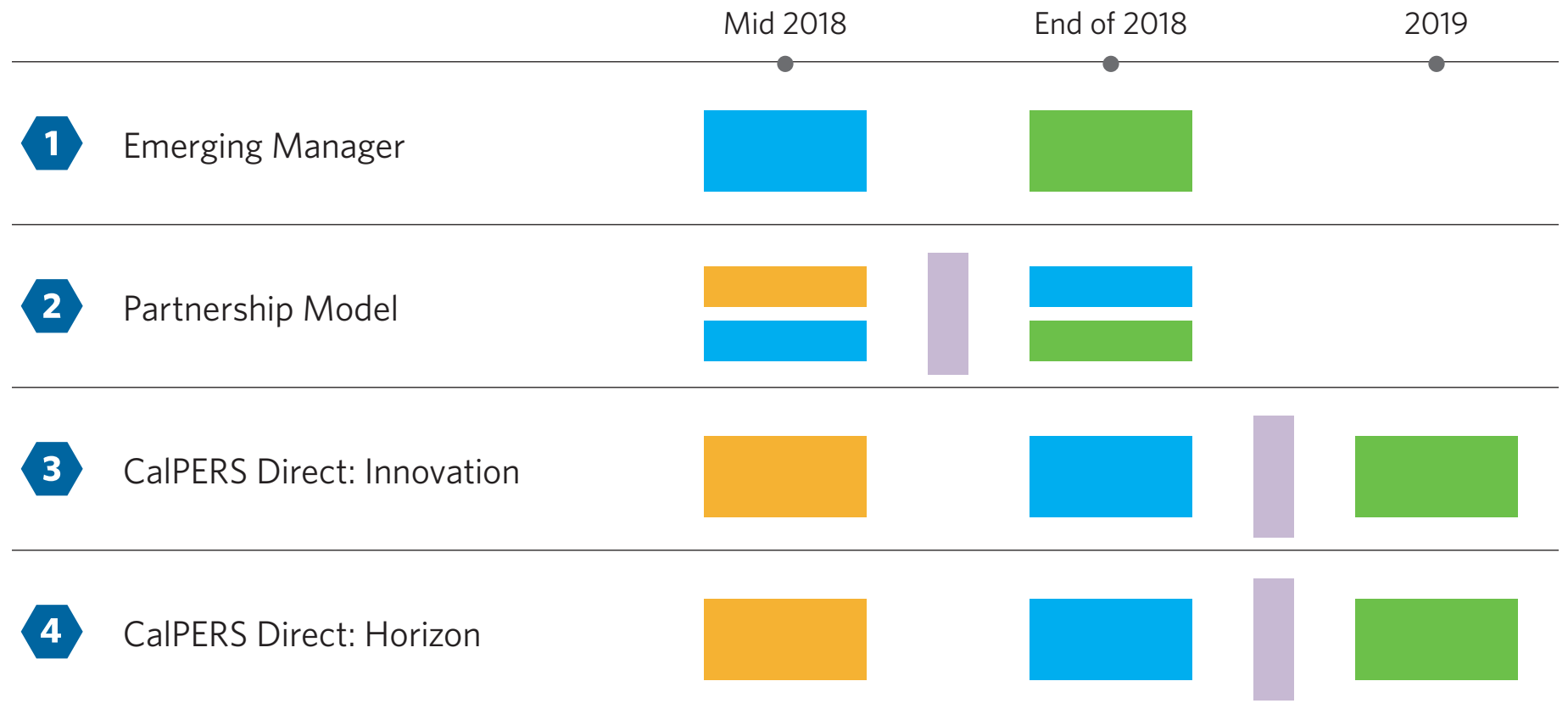
Private Equity Strategy Pillars



Private Equity Strategic Model Review Process



Timelines Overview



Investment Committee Checklist – Direct Investment Vehicles

-
- Partnership terms (ownership, key persons (management and Board), compensation framework, first year expense budget, other material terms and conditions)

 - Evaluate potential role and involvement of CalPERS Direct Board, Innovation Board and Horizon Board

 - Fiduciary counsel input

 - Prudent Person Opinions (PPO)

 - Staff workforce strategic plan

 - Roles of Board consultant and senior CalPERS staff

 - Summary of key risks

Nonfinancial Risks Controlled in Private Equity

	Risk category	Examples of risk exposure
Partner level	Reputational	» Governance (e.g., corruption)
	People	» Succession of key personnel
	Process	» Investment process (e.g., diligence)
Asset level	Reputational	» Environmental, social, and governance (e.g., environmental damage)
	Regulatory	» Regulatory efficiency
	Political	» Safety and instability (e.g. social unrest)
		» Politics and policies (e.g., tax legislation)
	People	» Unauthorized activity/employee misdeed (e.g. noncompliance)
	Process	» Corporate crisis management
		» Third party risk
	Systems	» Cyber security and technology risk
	Other operational risks	» Health, safety and work environment
» Litigation		

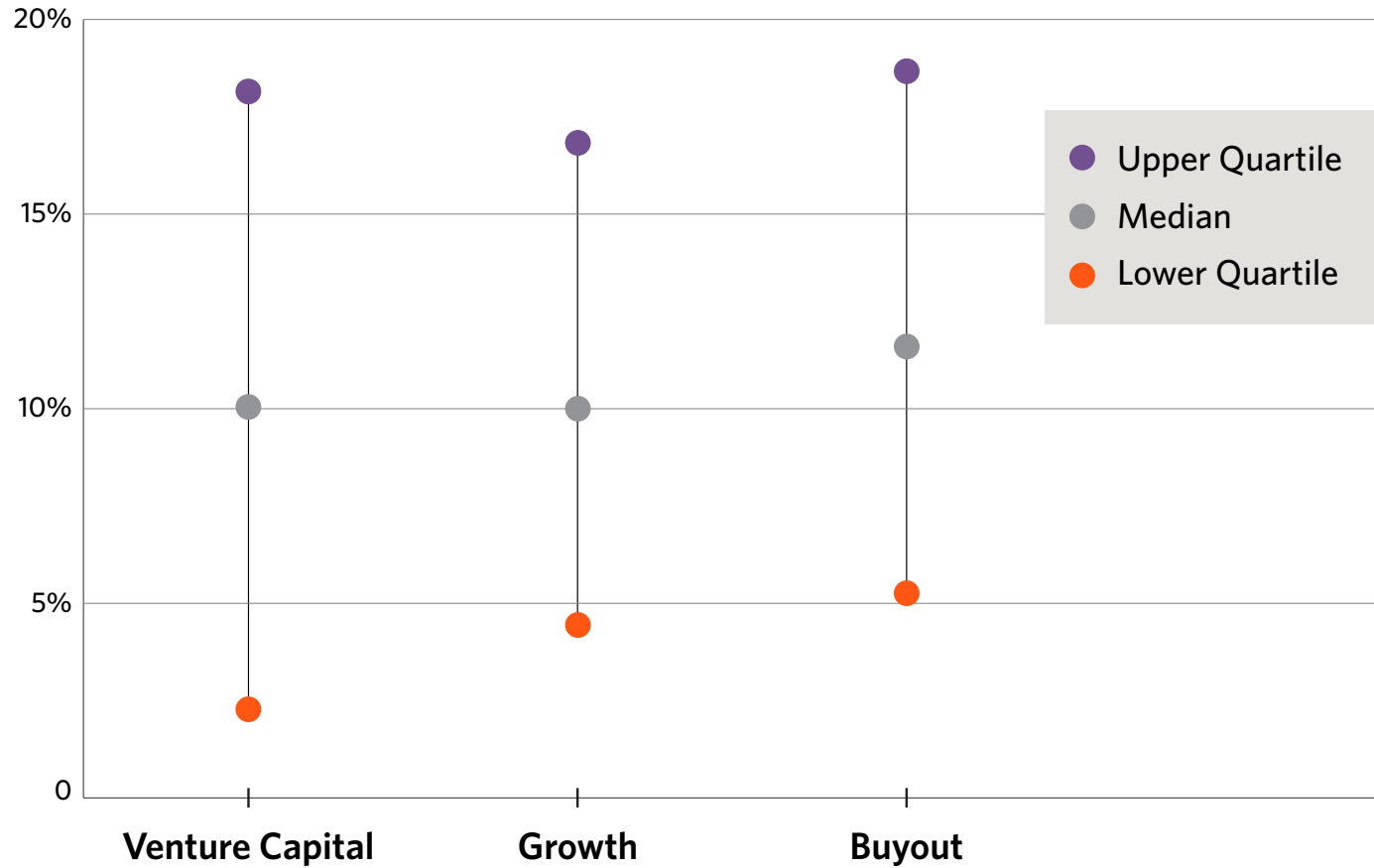
Source: McKinsey & Company

Net Returns Matter

Importance of hiring teams capable of high-gross returns

Wide Range Of Investment Results Over Ten Year Period (2005-2015)*

* Data from Cambridge Associates



Higher Returns Take Pressure Off Funded Ratio

