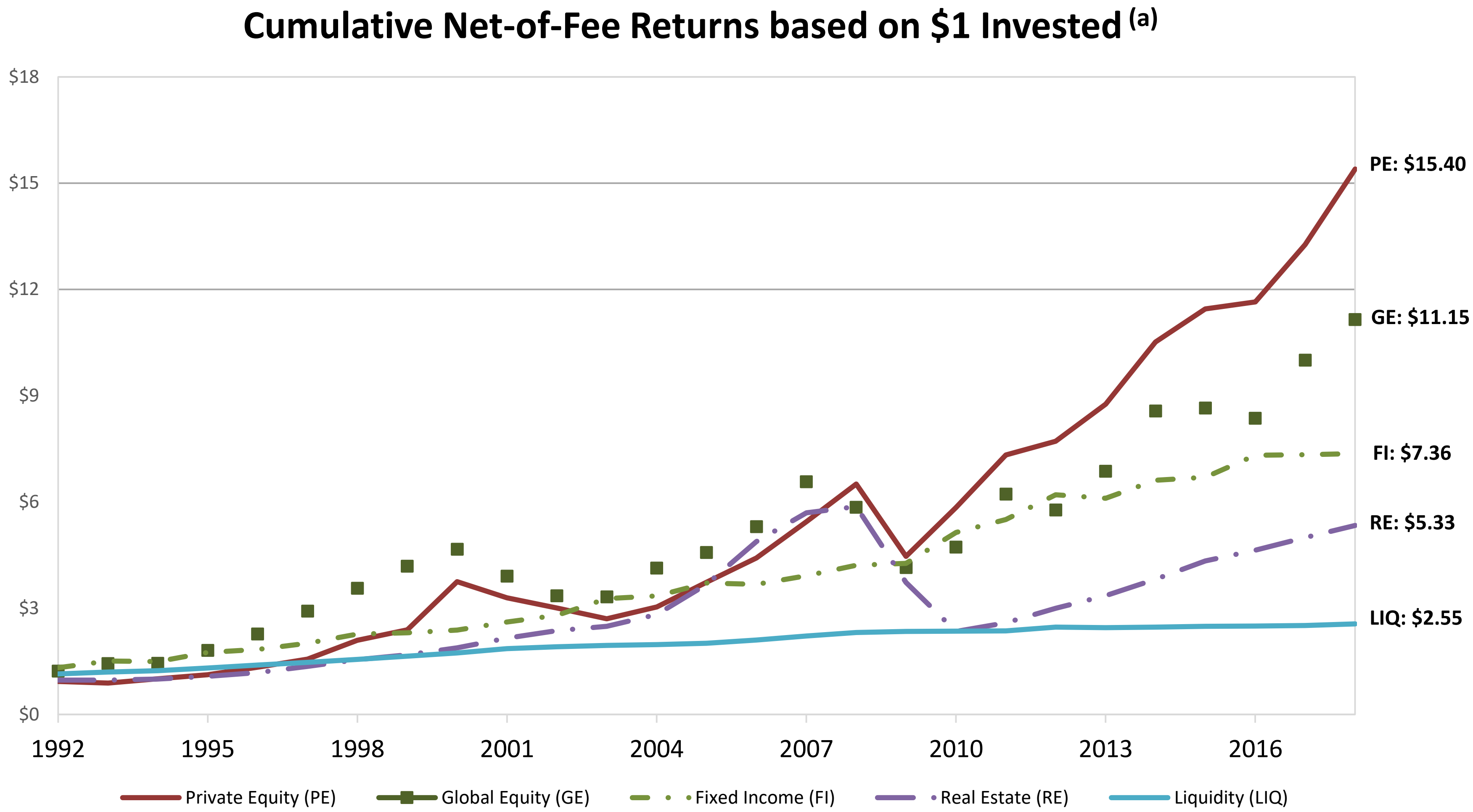
Summary of Private Equity Business Models

Investment Committee
February 19, 2019

CalPERS

Value Added From Private Equity



(a) Source: StateStreet – Based on annual data for 28 fiscal years ending June 30, 2018; Inflation-sensitive, Infrastructure and Forestland asset classes were excluded due to data limitations

Impact of Private Equity on Total Fund Return

Asset Allocation of Theoretical Candidate Portfolios			
Asset Class Component	Existing ALM Policy Portfolio	0% Weight in Private Equity	16% Weight in Private Equity
Global Equity	50%	55%	46%
Private Equity	8%	0%	16%
Fixed Income	28%	31%	25%
Real Assets	13%	13%	12%
Inflation Assets	0%	0%	0%
Liquidity	1%	1%	1%
Expected Return/Discount Rate	7.00%	6.70%	7.30%
Employer Contribution Rate[1]	31%	34%	29%

[1] Contribution Rate was interpolated from ±1% Discount Rate Sensitivity Study for State Miscellaneous Members

Why Allocate to Private Equity?

- Private Equity (PE) is an increasingly important part of global equity capital markets
- Private Equity Program is the only asset class that is expected to exceed the actuarial rate of 7% (based on 2017 ALM)
- Provides drawdown mitigation as a result of the lag in valuations and market inefficiencies
- Historically improved the funded ratio
- Decreases volatility of contribution rates
- Many attributes of Focus #3 (Comparative Advantages)
  - Scale and brand
  - Long term investment horizon
  - Innovation

Why Pillar II <u>and</u> Pillars III & IV

- CalPERS needs to continue to invest in and explore additional options within Pillar II (expand capabilities in co-investments, secondaries and separate accounts)
- Adding Pillars III and IV will provide CalPERS with the ability to;
  - Scale the PE Program and, over time, increase the allocation to PE
  - Improve the capabilities in less efficient markets (Focus #1, Investment Capabilities)
  - Have more control, reduce costs, improve CalPERS' transparency and better align interests with CalPERS investment objectives
- Pillar III
  - Takes advantage of companies staying private for longer
  - Accesses a higher growth segment of the capital markets
- Pillar IV
  - Allows for long term investing
  - Decreases friction costs and helps avoid redeeming from ourselves (Focus #4, Long-Term)

Transparency for Pillars III and IV

- Transparency to Staff would be greater than what is currently received from comingled funds
- Transparency to the Public is the same as it is for existing Private Equity Fund Investments

Strategy	Transparency to CalPERS	Transparency to the Public
Comingled Funds	• Financial Statements • Quarterly Templates • Annual Meeting Materials • Capital Calls and Distribution Notices • Limited Portfolio Company Information • Limited visibility on costs	• Commitment and Performance Information • Annual Management Fees and Expenses • Carried Interest Distributed • Pro rata share of fees and expenses paid by portfolio companies
Pillars III & IV	All of the above plus • Detailed Portfolio Company Information • Budget – full details on costs • Periodic Meetings between Senior INVO Staff and the Investment Manager • Detailed Investment Pipeline Information	• Commitment and Performance Information • Annual Management Fees and Expenses • Carried Interest Distributed • Pro rata share of fees and expenses paid by portfolio companies

Pillar III & IV Implementation

(Why) Conceptual Fit → (Who) Capable Partners → (How) Aligned Governance → (What) Commitment Size/# of Managers