

CalPERS Investment Policy for Global Fixed Income Program

Effective Date

~~November 16, 2015~~

This Policy is effective ~~immediately upon adoption~~ [Month DD, Year] and supersedes all previous Global Fixed Income Program ~~and Credit Enhancement Program~~ investment policies.

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Introduction

The California Public Employees' Retirement System (CalPERS) Total Fund Investment Policy, adopted by the CalPERS Investment Committee (Committee), sets forth the CalPERS investment beliefs and overarching investment purposes and objectives with respect to its investment programs. The CalPERS Total Fund Investment Policy specifically covers key areas of investment strategy, including performance objectives, asset allocation strategies, benchmark selection, investment risk management, and derivatives, leverage, and divestment policies, among other elements that are applicable to all asset classes and programs at CalPERS.

This document sets forth the investment policy (Program Policy) for the Global Fixed Income Program (Program). The design of this Program Policy ensures that staff, investors, managers, consultants, and other participants selected by CalPERS take prudent and careful action while managing the Program. Additionally, use of this Program Policy assures sufficient flexibility in managing investment risks and returns associated with the Program.

This Program Policy should be read in conjunction with and is subject to conditions contained within the CalPERS Total Fund Investment Policy (Total Fund Policy). This Program Policy shall also be managed to comply with all applicable Investment Office policies.

Strategic Objective

The Program ~~seeks to~~ has three strategies: Long Treasury, Long Spread, and High Yield, each defined as an "Asset Segment" and having the strategic objectives outlined below.

A. The Long Treasury Segment of the Program has the following strategic objective:

- ~~diversify and reduce overall risk for CalPERS investment programs while enhancing CalPERS total returns.~~ To serve as an economic diversifier to equity risk and be a reliable source of liquidity.

B. The Long Spread Segment of the Program has the following strategic objective:

- To provide a reliable source of income and an additional source of liquidity.

C. The High Yield Segment of the Program has the following strategic objective:

- To provide exposure to economic growth and be a reliable source of income.

Responsibilities

Details regarding various levels of responsibility for this Program are provided in Appendix 1, Reporting to the Investment Committee, and Appendix 2, Investment Responsibilities, to this Program Policy.

Investment Approaches & Parameters

All investment programs shall have specific written guidelines. The guidelines shall outline the investment approaches, permissible and restricted activities, and a performance objective that is commensurate with the program's purpose.

Staff shall rely on short- or long-term ratings from authorized nationally recognized statistical rating organizations (NRSROs) only. Staff shall maintain and annually update internal ratings for securities that are not rated by any authorized NRSROs.

Investment Constraints/ Limitations

See Appendix 3 for program investment constraints.

Glossary of CalPERS Specific Terms

Italicized terms appearing in the Program Policy are CalPERS-specific in nature and are defined in the [CalPERS Specific Glossary of Terms](#).

Policy Document History

See Appendix 4 for historical details of Investment Committee adoption of and revisions of this Program Policy.

Appendices

See the [Total Fund Investment Policy](#) appendices for overarching reporting requirements and responsibilities for the Investment Committee, staff, **General Pension Consultant, Private Asset Class Board Investment Consultant**, and **External Manager**.

Appendix 1: Reporting to the Investment Committee

The following tables provide details regarding reporting to the Investment Committee:

- Investment Office staff
- **General Pension Consultant**

Table 1: Investment Office Staff Reporting Responsibilities

Ref #	Report Content	Frequency
1.	Staff shall provide an Annual Program Review that will include a program overview, investment review, and business review in general conformance with the Annual Program Review Template.	No less than annually
2.	Staff shall report concerns, problems, material changes, and all violations of the Policy. These reports shall include explanations of any violations and appropriate recommendations for corrective action.	At the next Committee meeting, or sooner if deemed necessary

Table 2: General Pension Consultant Reporting Responsibilities

Ref #	Report Content	Frequency
1.	The Consultant shall monitor, evaluate, and report on the performance of the Program relative to the benchmark and this <u>Program</u> Policy and other applicable CalPERS Policies.	No less than annually

Appendix 2: Investment Responsibilities

The following ~~tables~~ sections provide details regarding investment related responsibilities for the:

- Investment Office staff
- **General Pension Consultant**
- **External Manager**

Investment Office Staff Responsibilities

1. All aspects of portfolio management, including monitoring, trading, analyzing, evaluating performance relative to the appropriate benchmark, and selecting and contracting with managers.
2. Monitor the internal and external managers in the implementation of, and compliance with, the Program Policy and the Total Fund Policy.
3. Develop and maintain investment procedures, program guidelines, and sub-program guidelines.

General Pension Consultant Responsibilities

1. Provide independent perspective and counsel to the Committee, to include routine communication with the Investment Office staff and periodic reviews of processes and procedures.

External Manager Responsibilities

1. Manage the fund in accordance with each manager's contract with CalPERS, the Total Fund Policy, and the Program Policy.
2. Communicate and cooperate with Investment Office staff and authorized third parties regarding the management of the fund.

Appendix 3: Investment Constraints/Limitations

The following ~~tables provide~~ table provides details regarding investment constraints/limitations related to the following ~~programs~~ Asset Segments:

- ~~Dollar-Denominated Fixed Income~~
- ~~International Fixed Income~~
- ~~Credit Enhancement~~

Ranges for Domestic and International Programs relative to the benchmark are listed below.

- Long Treasury Segment
- Long Spread Segment
- High Yield Segment

Domestic Program <u>Investment Constraints/Limitations by Global Fixed Income Asset Segment</u>
<p>International Program <u>Long Treasury Segment</u></p> <ol style="list-style-type: none"> 1. <u>Interest rate risk will be controlled using duration management. Duration will be maintained at +/-10% of the benchmark.</u> 2. <u>Further restrictions regarding liquidity and use of derivatives are outlined in the Investment Procedures and Guidelines (IPG) <u>Policy-Related Procedures (PRP)</u> for the Global Fixed Income Program.</u> <p><u>Long Spread Segment</u></p> <ol style="list-style-type: none"> 1. <u>Sector Risk will be controlled by sector ranges that specify the degree by which allocations may fluctuate from the benchmark weights. Permitted sector ranges for each strategy will be maintained within +/-10% of the benchmark weight with a minimum weight of 0%.</u> 2. <u>Further restrictions regarding duration, ratings, concentration, currency, geography, and use of derivatives are outlined in the IPG <u>PRP</u> for the Global Fixed Income Program.</u> <p><u>High Yield Segment</u></p> <ol style="list-style-type: none"> 1. <u>Restrictions regarding duration, ratings, concentration, out of index bets and use of derivatives are outlined in the IPG <u>PRP</u> for the Global Fixed Income Program.</u>
Dollar-Denominated Fixed Income Program
<ol style="list-style-type: none"> 1. Interest Rate Risk must be controlled using duration management. Duration shall be maintained at -50% to +10% of the Barclays Capital Long Liabilities (BCLL) Index on an option-adjusted basis. Decisions shall be managed using historical real return relationships and economic analysis. 2. Sector Risk must be controlled using the ranges below. Based on the economic outlook, historical factors, and break-even analysis, staff shall estimate the impact on various sectors' spreads and make allocations accordingly.

~~Sector Ranges—The permitted sector ranges are expressed as a percentage of the total Dollar-Denominated Fixed Income Program portfolio.~~

Total Domestic Program Weightings

Sector	BCLL Index	Permitted Sector Ranges
U.S. Treasury & Government Sponsored	40%	10%—80%
Mortgage	30%	15%—45%
Corporate	24%	10%—40%
Opportunistic	3%	0%—12%
Sovereign	3%	0%—10%
Total	100%	N/A

International Fixed Income Program

1.—Interest Rate Risk must be managed by the Manager within -50% to +10% of the benchmark duration

2.—Sector Risk will be controlled using the ranges below. Managers are responsible for determining appropriate allocations based on market analysis.

~~Sector Ranges—The following table specifies the ranges within which allocations can fluctuate from benchmark weights, with the exception of Governments (ex US), for which the permitted sector range is expressed as a percentage of the total International Fixed Income Program portfolio:~~

Total International Program Weightings

Sector	Benchmark	Permitted Sector Ranges
Governments (ex US)	100%	90%—100%
U.S. Treasury (ex TIPS)	0%	-10%—+10%
Investment Grade Corporate	0%	-10%—+10%
Mortgages	0%	0%—+10%
Non-Investment Grade Corporate	0%	0%—5%
Total	100%	N/A

~~Note: The total of non-government securities cannot exceed 10% of the total International Program.~~

Credit Enhancement Program

1. ~~Credit Rating Portfolio Limits~~ — The average credit quality of the Program's portfolio shall be "single-A" long-term credit rating designation (A by S&P, A2 by Moody's, and A by Fitch).
2. ~~Program Transaction Limits~~ — The maximum holding in any given transaction in California shall be 25% of the issue in order to be in compliance with the Safe Harbor rules established under Section 503(e) of the Internal Revenue Code (IRC).

Additional details regarding investment constraints/limitations and risks are outlined in each Program Segment specific written procedures.

Appendix 4: Policy Document History

Table 3: Global Fixed Income Program Policy History

Date	Detail
2015-11-16	Approved by the Investment Committee Reformatted to incorporate Investment Policy Revision Project and Investment Delegation Restructuring Project revisions. <u>The Credit Enhancement Program Policy was consolidated with the Global Fixed Income Program Policy and was repealed on November 16, 2015.</u>
<u>YYYY-MM-DD</u>	<u>[Approved by the Investment Committee Updates were made to reflect the new asset segments. Administrative changes to migrate policy into an accessible template.]</u>

~~The Credit Enhancement Program Policy was consolidated with the Global Fixed Income Program Policy and was repealed on November 16, 2015.~~