Asset Liability Management
Mid-Cycle Review

Christine Reese & Dianne Sandoval
Trust Level Portfolio Management

Investment Committee
June 15, 2020
Introduction

The Strategic Asset Allocation process is used to build a diversified portfolio for a long-term investment horizon that balances expected risk and return.

CalPERS’ Board adopted the strategic asset allocation for the PERF & Affiliate Funds between December 2017 – June 2018. The next full Asset Liability Management study will begin in 2021.

This mid-cycle review reflects current economic conditions, market valuation, and capital market assumptions as compared to the 2017/18 estimates.

*Strategic Asset Allocation is the primary determinant of portfolio risk and return* – CalPERS’ Investment Belief #6
Economic Overview

Unprecedented economic impact and global response

U.S. Unemployment
- 14.7% - April 2020
- 16.8% - Q2 2020 forecast

U.S. GDP
- -4.8% Q1 2020
- -35% Q2 2020 forecast

U.S. & Global Response
- Monetary & fiscal support
- Timely and unprecedented size
- Several trillion in aid granted

Economic Uncertainty
- Remains extremely elevated
- No close historic parallel

Data as of April - May 2020
Market Valuation

U.S. Equity Real Yields

Max = 8.8%

Min = -1.5%

U.S. Treasury Real Rates

Max = 8.2%

Q1 2020

Q2 2019

Global Financial Crisis

1981 Recession

Data as of April 30, 2020
Capital Market Assumptions
Building Blocks

- Risk Premium
  - Risk premiums vary by each asset class due to their unique attributes and risks

- Risk-Free Real Rate
  - Foundations common to all asset class assumptions

- Inflation
Capital Market Assumptions
10-year Expected Returns 2020 vs. 2017 - PERF

Data Sources:
- 2020 – March 31, 2020 CMA Survey Results from 10+ providers; CalPERS’ CMA models
Capital Market Assumptions
10-year Expected Returns 2020 vs. 2018 - Affiliate Funds

Data Sources:
- 2020 – March 31, 2020 CMA Survey Results from 10+ providers; CalPERS' CMA models
Asset Class Segments
Factor Weighted & High Yield

PERF Implementation - Constraints
• Assessed costs, capacity, market
• Reaffirmed constraints set in 2017
• Review again in full ALM study

Affiliate Funds Analysis
• Adding High Yield (HY) and/or Factor Weighted Equity (FWE) improves the efficient frontier for sample fund
• Product availability and costs to be reviewed
Next Steps

Asset Liability Management Study

• Begin planning and preparation for launch in 2021

Asset Class Research

• PERF
  – Review role of US Treasuries and potential alternatives
  – Revisit segment constraints in ALM study

• Affiliate Funds
  – Review role of US Treasuries and potential alternatives
  – Review role of inflation asset classes and potential alternatives
  – Assess cost/benefit for Factor Weighted Equity & High Yield segments