



Investment Committee

Item Number 6a – Open Session

Subject: Inflation Sensitive Policy Revision – First Reading

Presenter(s): Paul Shantic & Charles Fitzpatrick

Item Type: Information

Date & Time: July 7, 2022 – 20 minutes

Attachment(s): Attachment 1 – Meketa Concurrence Memo

Attachment 2 – Inflation Sensitive Investment Policy – Redline Version

Attachment 3 – Inflation Sensitive Investment Policy – Clean Version

PowerPoint(s): Inflation Sensitive Investment Policy Revisions – First Reading

POLICY

The [CalSTRS Inflation Sensitive Policy](#) (Page Q-1), which governs the management of the Inflation Sensitive Asset Class, seeks to ensure that a diversified portfolio of Inflation Sensitive assets is developed to meet CalSTRS' objectives, within acceptable risk parameters.

PURPOSE

This is a first reading of these proposed Inflation Sensitive policy revisions.

This is an action item proposing policy changes to the Inflation Sensitive policy language to suggest and incorporate additional modifications in keeping with the evolving market conditions, practices, and opportunities available to the unit.

Staff is proposing policy changes designed to accomplish:

- Clarify that Inflation Sensitive investment approvals will follow the same policies and procedures as those currently utilized by the infrastructure portfolio involving internal recommendations and external consultant review. As procedures around RFP, ASP, and

new external manager assignments are developed, the unit will develop guidelines to handle these potential new manager selection tools.

- Clarify that Infrastructure related loan or debt securities are governed by the Inflation Sensitive policy as they are more akin to floating rate debt and debt-like securities rather than equity. Also extends the debt security description to timberland, agriculture, and energy-based securities that are more debt-like.
- Add language from the Infrastructure policy regarding staff approval levels, single manager investment limits, and the 5% asset limit.
- Slightly modifies the performance objective benchmark to recognize the discontinuation of the Alerian Index.
- Eliminate from the Policy Exhibits 1, 2, and the Glossary to be in line with other policy updates. Those exhibits will be incorporated into the unit's guidelines and procedures, with the exception of the Glossary, which will be retired and are found in the new and larger combined CalSTRS Glossary.

DISCUSSION/SUMMARY

The Inflation Sensitive portfolio is a unique hybrid asset class of multiple asset types that will utilize both internal CalSTRS managers and external managers in order to achieve its long-term goal of exceeding the U.S. CPI – by a weighted performance target. The policy benchmark is a weighted blend of all the strategies undertaken in the portfolio. The goal is always to ensure that the strategy undertaken has the appropriate benchmark in place.

Staff and the Board consultant, Meketa Investment Group (Meketa), have reviewed the Inflation Sensitive Policy and recommend the following revisions:

1. *Page Q1-Q7* – a ministerial revision is made throughout the document. “P” in “Portfolio” stands for the entire CalSTRS Portfolio. The use of “p” in “portfolio” stands for the Inflation Sensitive portfolio only.
2. *Page Q2* - eliminates duplicative language under the **Performance Objectives** regarding “blended and weighted benchmark.” Also, deletes under the **Program Benchmark** the “Alerian MLP daily index” as a benchmark. The strategy has been dropped from the portfolio.

3. *Page Q3* – under the **Program Structure** section a paragraph is inserted which clarifies that Inflation Sensitive investment approvals will follow the same procedures and processes as those currently utilized by the Infrastructure Policy in terms of written recommendations and external consultant review, if necessary, based on the acquisition process of the strategy and manager involved.
4. *Page Q3 & Q4* – under the **Private Inflation Sensitive** section additional clarification is made that infrastructure related loan and debt securities are governed by the Inflation Sensitive policy and not the Infrastructure Policy as they are more akin to floating rate debt securities and have debt-like structures and are not infrastructure equity securities. This definition is also extended to agriculture, timberland, and energy related securities.

Under the **Allocation Ranges** section, ranges are established around the upper limits for the U.S. TIPS portfolio, Commodities, and Private Inflation Sensitive asset sub-asset classes. Ranges are easier to work with in a dynamic market. Also, the section clarifies that sub-asset classes and “investment strategies” that move into the Inflation Sensitive purview will receive a review by the Inflation Sensitive Director, the DCIO, and CIO.

Under **Other Strategies** this section clarifies the involvement of the Deputy Chief Investment Officer in the investment decision matrix.

5. *Page Q5* – under the **Risk Management** section additional ministerial corrections are made using the words “insure” and “ensure.”

Inserts the section **Eligible Investment Vehicles** and refers to investment vehicles available for use under the Infrastructure Policy and makes them and other potential vehicles eligible for use under the Inflation Sensitive Policy.

Inserts the section **Discretionary Authority** under language suggested by CalSTRS’ Compliance unit.

6. *Page Q-6* - under **Discretionary Authority** this section borrows language from the Infrastructure Policy regarding the initial approval level for a staff commitment of \$500 million to a manager or a strategy, limits a single manager to a 25% investment limit (versus the previous 20%) and includes a 5% single asset limit.

Under the **Inflation Sensitive Internal/External Management** section the decision matrix in Exhibit 2 is dropped and incorporated into IS internal guidelines.

7. *Page Q-7* - under the **Policy Monitoring and Modification** this section incorporates suggested Compliance unit language.
8. *Page Q-9, Exhibits 1 & 2 in addition to the Glossary* – have been struck and will be incorporated into the IS unit’s guidelines and procedures. The attached glossary has been replaced by a full on-line glossary covering investment terms across all asset classes.

RECOMMENDATION

Staff recommends and the Board consultant Meketa concur that the Investment Committee consider the proposed revisions to the Inflation Sensitive Investment Policy. Staff will incorporate the Board's feedback into the Policy and bring it back for a second reading, unless the Board decides to approve the recommended changes at this meeting.