Investment Committee

Item number 5 – Open session

Subject: ALM & One Fund Approach Education

Presenter(s): Scott Chan and Josh Diedesch

Item type: Information

Date and time: November 4, 2026 – 40 minutes

Attachment(s): None

PowerPoint presentation(s): ALM & One Fund Approach Education

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Item purpose

The purpose of this item is to provide the Investment Committee with education on two topics: the upcoming Asset-Liability Management (ALM) study and an introduction to the One Fund Approach (OFA).

Executive summary

This report is divided into two parts. The first section is an overview and education on the ALM, including some basic background, the purpose and goals of the ALM, and a high-level timeline. The second section is an introduction to the One Fund Approach describing the challenges and opportunities that the OFA seeks to address and its major elements. The 2027 ALM will begin in February 2027 and conclude with an asset allocation decision in September 2027. In parallel, Staff is introducing the One Fund Approach, a framework to better align investment strategy, governance, and portfolio construction around the total fund.

Background

Deciding on and overseeing a prudent level of long-term risk and return to achieve the CalSTRS mission is the most important role of the Investment Committee and Board as fiduciaries. This role is fulfilled in several ways: setting a long-term level of risk and return through the ALM; deciding appropriate delegation to Staff; adopting policies to support risk management of the fund and delegated authority; deciding on and approving budget for resources – people, technology, data, etc. – to support execution of the investment strategy; and supporting a diverse, collaborative culture.

This item introduces two major areas of work over the next year that support these responsibilities: the 2027 ALM, which will set a prudent long-term level of risk and return to meet the CalSTRS mission, and the One Fund Approach, which seeks to align investment strategy, governance, and portfolio construction around a total fund view. These two areas are closely linked but have distinct differences. The objective of the ALM is for the Investment Committee to set the long-term level of risk and return for the portfolio as part of the well-established ALM framework at CalSTRS. The objective of the OFA is to provide the Committee with education and design choices to better align investment strategy, governance, and portfolio construction around the total fund.

Asset-Liability Management Study

The Investment Committee conducts an ALM every four years to align with Actuarial work and the Board's adoption of the Investment Return Assumption. The main outcome of the ALM is the Investment Committee deciding the long-term level of risk and return through the strategic allocation of the portfolio. Investment returns are expected to contribute approximately two-thirds of ultimate benefit payments paid out to beneficiaries, making this the most important decision the Investment Committee makes.

To support the Investment Committee's decision, Staff works closely with Actuarial Resources and the Committee's General Consultant Meketa to perform extensive analysis of various levels of risk and return, assumptions about future market returns and risk, strategic long-term investment opportunities and risks, evolving market conditions and geopolitics, climate risk and the energy transition, and many others. Based on all this work, Staff provides the Investment Committee with options and a recommendation for the level of long-term risk and return, as well as long-term asset allocation strategy.

The 2027 ALM will begin at the February 2027 Investment Committee meeting with discussion of long-term capital markets assumptions, analysis of different levels of portfolio risk-return and what they mean for the funding plan, and general guidance from the Committee on a target level of risk and return to seek in the asset allocation. In the March and May 2027 Committee meetings, discussion will focus on opportunities to shift the investment strategy, including changes to the asset allocation, geographic diversification, ways to increase portfolio resiliency, and the possible use of leverage. In September of 2027, Staff will present long-term allocation options and a recommendation for Committee approval.

One Fund Approach

CalSTRS invests in a competitive global landscape and has evolved over time to improve diversification, reduce costs, and enhance the long-term success of the fund. Prior Investment Committee meeting discussions on the Shared Vision have highlighted some of these changes: development and expansion of direct and internal management, broadening portfolio diversification into illiquid alternative assets, and enhancements to liquidity management. The OFA is the next step in that evolution.

At its core, the One Fund Approach seeks to better align the investment strategy, delegation and governance, and asset allocation and portfolio construction decisions to a total fund view. A total fund view would better position the fund to meet several challenges and opportunities:

- Global competition for investment opportunities coming from the growth in sophisticated sovereign wealth funds and other asset owners
- Unwinding of decades of relatively free flow of global capital and investment to a world that's more fractured with heavier emphasis on mercantilist industrial policies
- Reversal of trends that favored investment in financial and intangible assets to a much heavier focus on capital-intensive investment in the AI buildout, energy transition, defense spending, and reindustrialization
- A more uncertain long-term inflation outlook with developed market fiscal deficits, heavy demand for capital to support the AI buildout, and significant uncertainty in the timing and effects of AI disruption

The One Fund Approach seeks to build on the history of success and strengths at CalSTRS to meet these challenges and capitalize on the opportunities they present. As a long-term investor, CalSTRS is well positioned to benefit from these trends. But the traditional approach to asset classes and strategic asset allocation limits flexibility to respond to these challenges. The AI buildout, for example, cuts across multiple asset classes and presents new challenges to traditional views of portfolio risk. Building a resilient portfolio for the long-term means diversifying the portfolio for a constantly evolving set of risks. Key goals of the One Fund Approach to help meet these challenges include:

- Improving portfolio diversification and resiliency
- Enhancing risk management and governance
- Enabling dynamic asset allocation at the total fund level and across divisions
- Enhancing liquidity management and the balance sheet
- Capitalizing on scale to add alpha

Achieving these goals could involve increasing allocations that diversify growth risk in the portfolio, increasing allocation to real assets that provide long-term inflation protection and cash flow, greater geographic diversification, and the use of leverage to fund growth-diversifying assets that balance sources of risk without increasing total risk. It includes identifying opportunities to enhance governance by aligning delegation to support more agile and flexible shifts to the portfolio through different market environments. It also involves capitalizing on the scale of relationships that span traditional asset class lines to source superior investment opportunities and deal flow.

Achieving the goals of the OFA would increase the likelihood of superior long-term risk-adjusted returns and ultimately improve the ability to meet the CalSTRS mission. The OFA has similarities to the "Total Portfolio Approach" but reflects the opportunities and challenges specific to CalSTRS.

The goal of the OFA is not to take more risk or reduce oversight but instead improve the way risk is allocated and enhance risk management with clear delegation and accountability at the appropriate levels.

Over the next several Investment Committee meetings, Staff will provide education on these areas and the range of opportunities they present. The ALM involves tradeoffs and choices for risk and return in the portfolio that drive the long-term strategic direction of asset allocation. The OFA presents many design choices for areas like governance, delegation, and organization. Staff will provide education on these choices and, where appropriate and in coordination with Meketa, will bring recommendations on changes that can improve the long-term success of the fund.

Strategic Plan Linkage: Goal 1 of the CalSTRS Strategic Plan. Trusted stewards – Ensuring a well-governed, financially sound trust fund.

Board Policy Linkage: Investment Policy Statement 05-2025

Investment Beliefs - CalSTRS
