CalPERS – the Charted Course Forward for Pensions

2022 CSMFO Annual Conference

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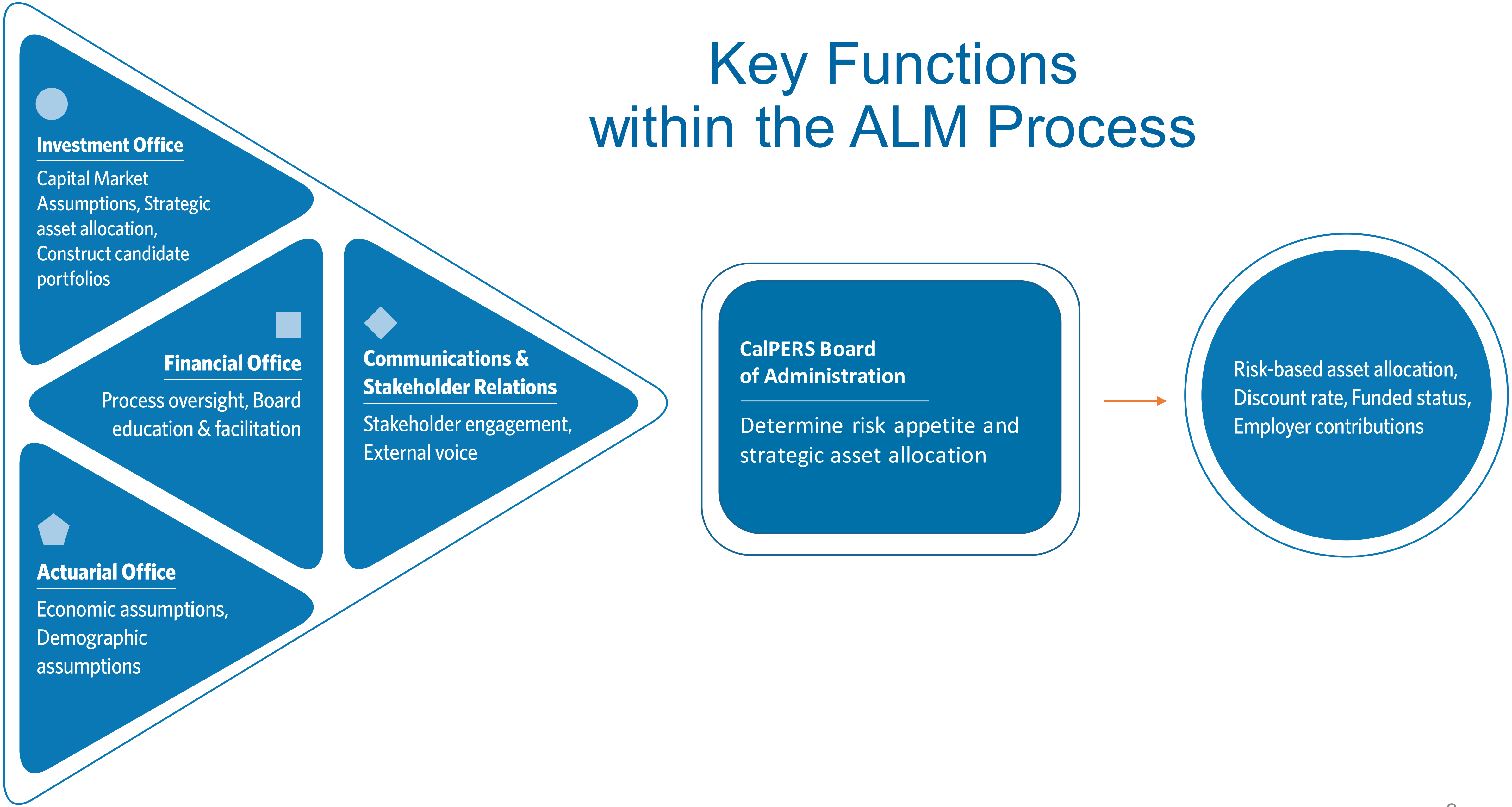
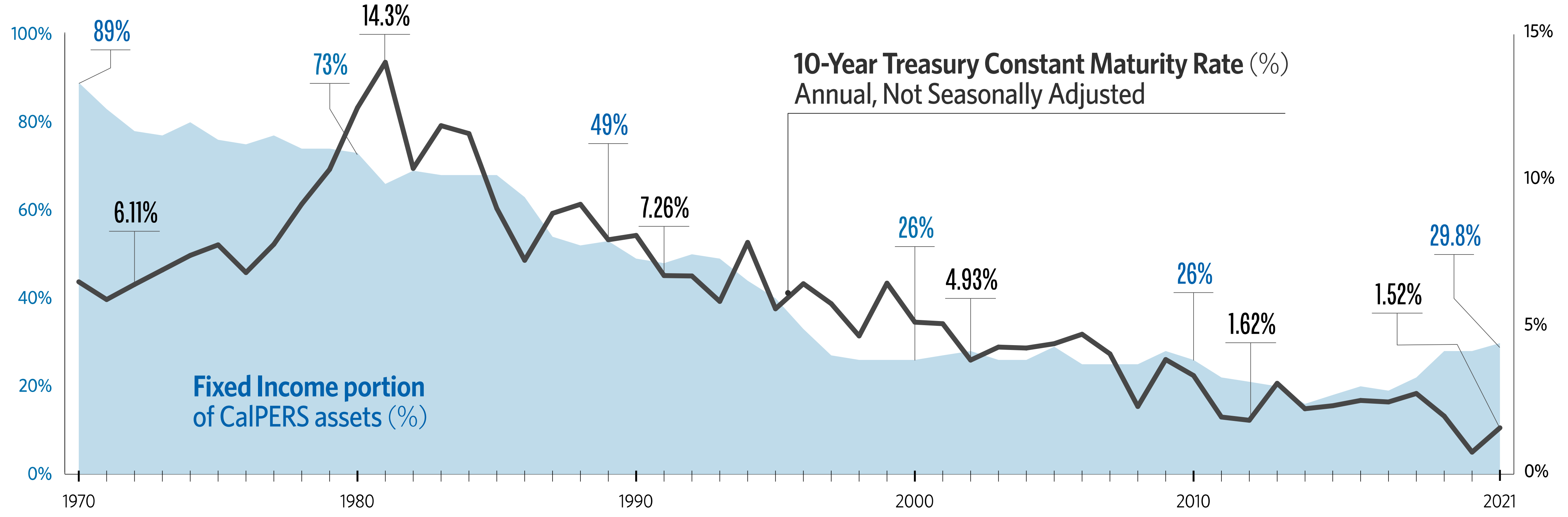
Key Functions within the ALM Process



Challenges to Achieving Target Returns

US Treasury Yields Reduced to Near Zero



Leading Up to the Discount Rate Decision

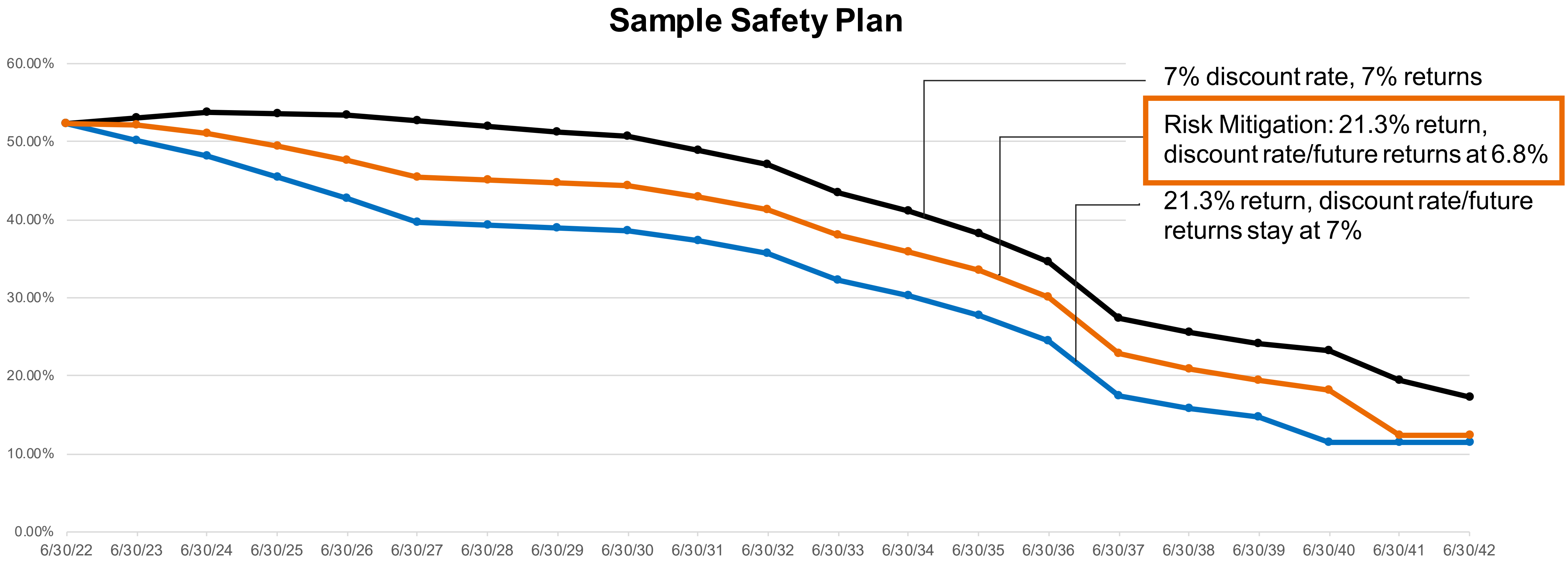
- 2021 – **began the ALM review**, which is conducted every 4 years
- **21.3% return** for fiscal year 2020-21
- Funding Risk Mitigation Policy **triggered**
- Discount rate automatically **lowered to 6.8%** on July 1, 2021
- New **Capital Market Assumptions adopted** – current portfolio has projected returns of 6.2% over the next 20 years
- Board **considered portfolios** with 6.5%, 6.8% and 7.0% discount rates with varying degrees of leverage

Risk Mitigation Policy Had Already Lowered Discount Rate to 6.8%

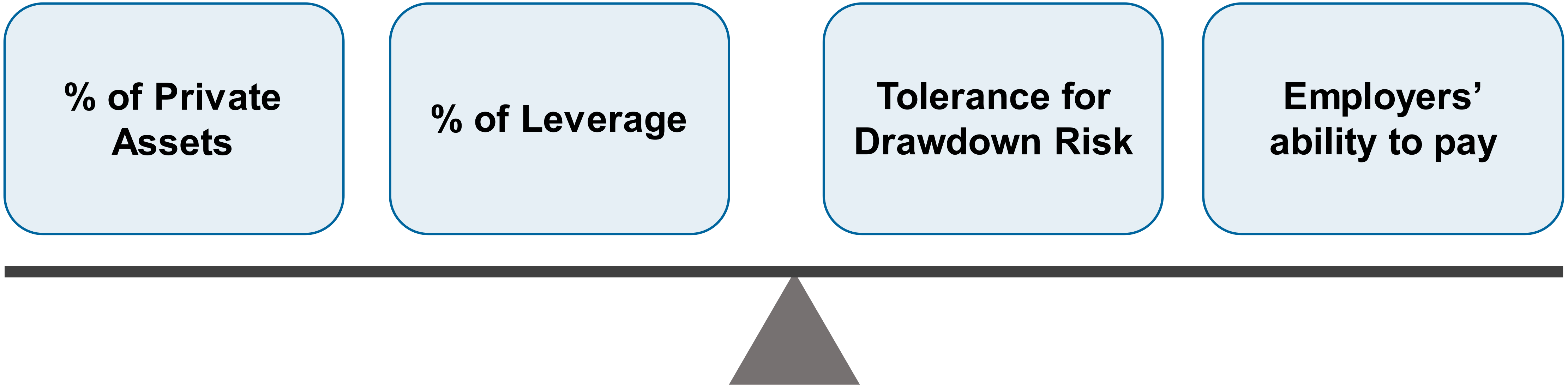
If investment returns outperform discount rate by:	**then** resulting discount rate will be:
+2 pp → 9%	6.95%
+7 pp → 14%	6.90%
+10 pp → 17%	6.85%
+13 pp → 20%	6.80%
+17 pp → 24%	6.75%

From Risk Mitigation Policy triggering

21.3% Return Softened Impact of Discount Rate Reduction for Employers



Balancing Risk & Reward



Discount Rates and Portfolios Considered

Portfolio Characteristics		Years 1-20		
Name	Leverage	Discount Rate	Drawdown	Volatility
Current	0%	6.2%	22.6%	11.2%
A1	0%	6.5%	20.4%	10.9%
A2	3%	6.5%	20.1%	10.8%
B1	0%	6.8%	23.6%	12.1%
B2	5%	6.8%	23.0%	12.0%
C1	5%	7.0%	25.5%	12.9%

ALM Outcome

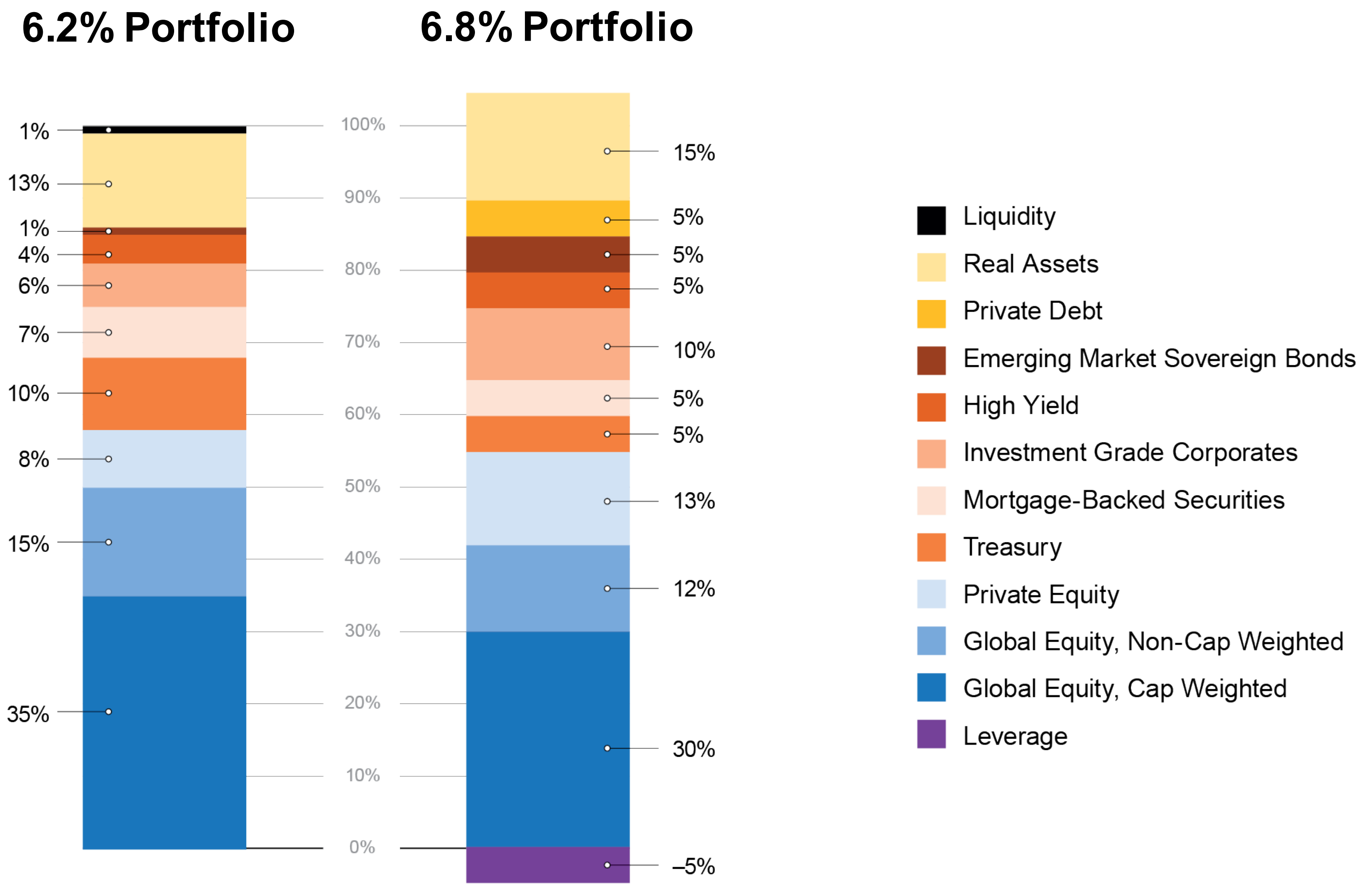
Board selected 6.8% discount rate with 5% leverage (Candidate Portfolio B2)

New strategic asset allocation:

- 5% leverage
- Increased allocation to private assets

New **actuarial assumptions adopted**

Previous Portfolio (6.2%) and New Portfolio (6.8%)



What Leverage Does

CalPERS & Leverage

- Board approved adding 5% leverage as a strategic asset allocation
- Current leverage is mainly in real estate portfolio and is actively managed
- Leverage is borrowing money to buy assets
- Will take several years to fully implement
- Leverage has been used in moderation for years

Why Is CalPERS Using Leverage?

- Reduce percentage of CalPERS Fund allocated to riskier assets, including public stocks
- Increase diversification by investing in less-risky assets, including fixed income, to better withstand economic downturns
- Reduces overall risk and volatility compared with a similar portfolio that contains no leverage
- Not being used to increase private asset investments

What Are the Risks?

- Leverage adds complexity to managing the fund
- Higher losses in some market conditions

Why Are Private Assets Critical to the Asset Allocation?

Highest returning asset class, past and projected

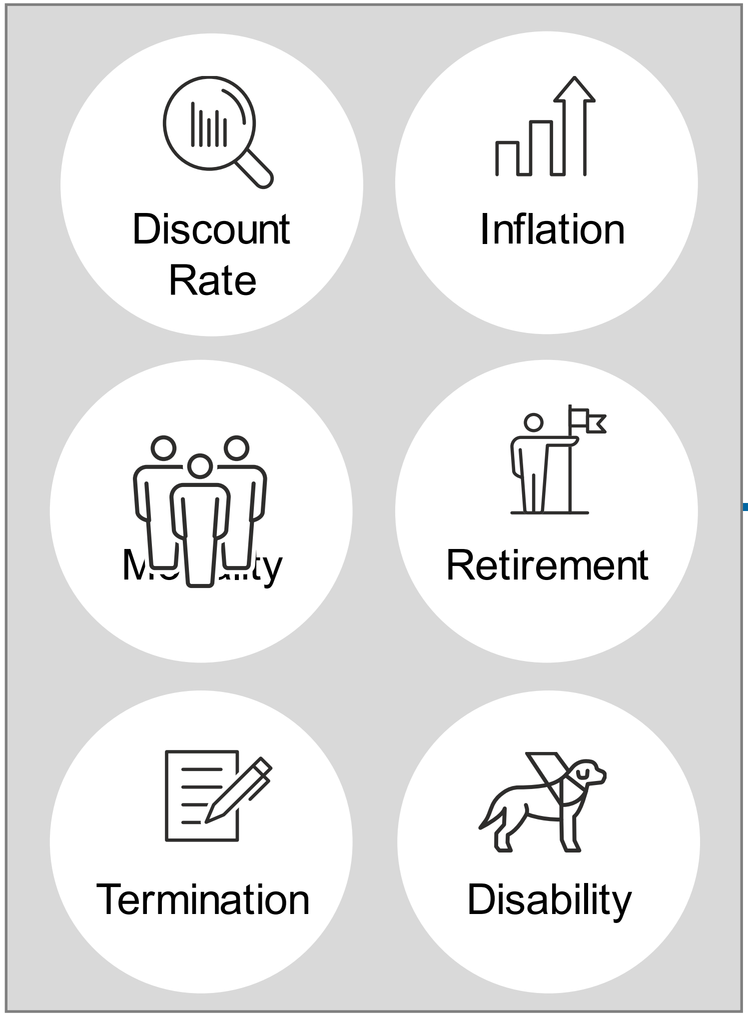
Portfolio diversifier

Access to different parts of the economy not readily available in public markets

Discount Rate

- Discount Rate set by Risk Mitigation Policy affirmed by Board
- Increases normal cost
- Increases UAL (unfunded accrued liability)
- School and State plans – effective 2022–23 fiscal year
- Public agency plans – effective 2023–24 fiscal year

ALM Outcomes for Employers — Year 1



2020–21 Investment Gain

Estimated Employer Contribution Impact*:

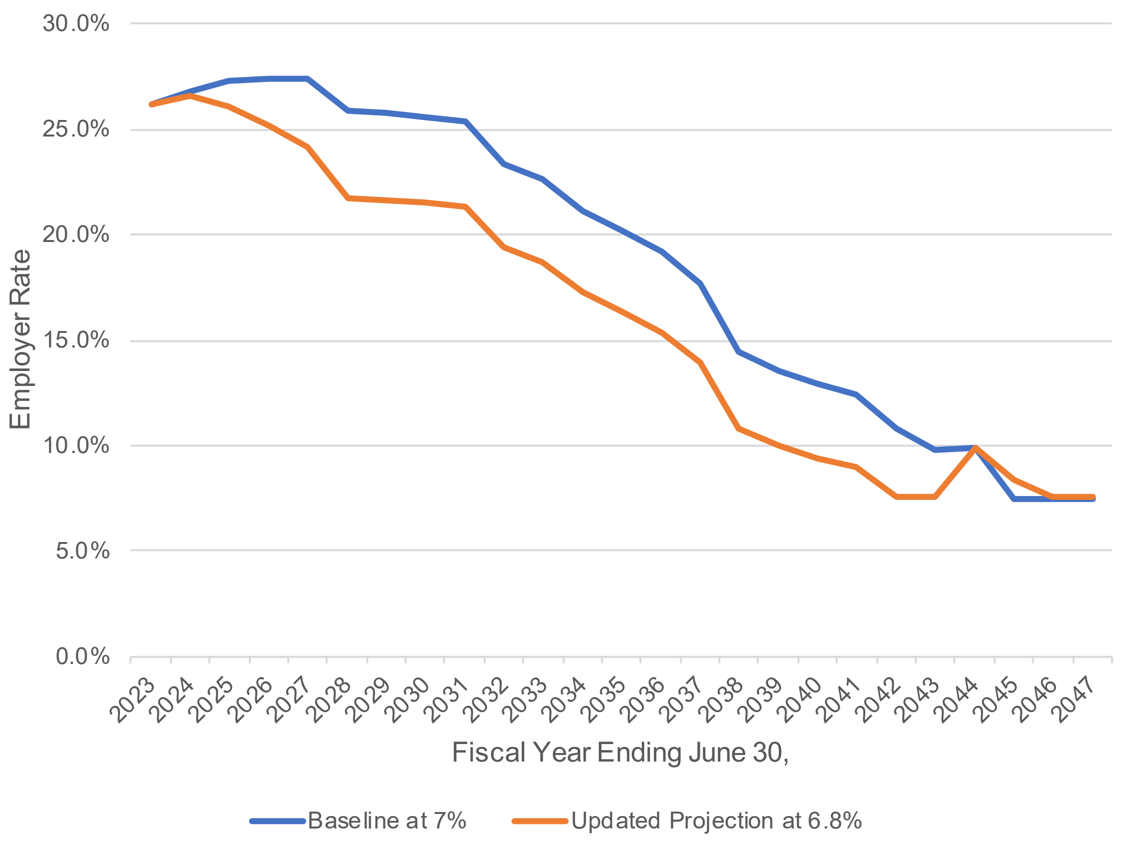
State Misc.	–0.6%
Schools	–0.1%
PA Misc.	0% median**
PA Safety:	0% median**

* *Results are as % of payroll changes*

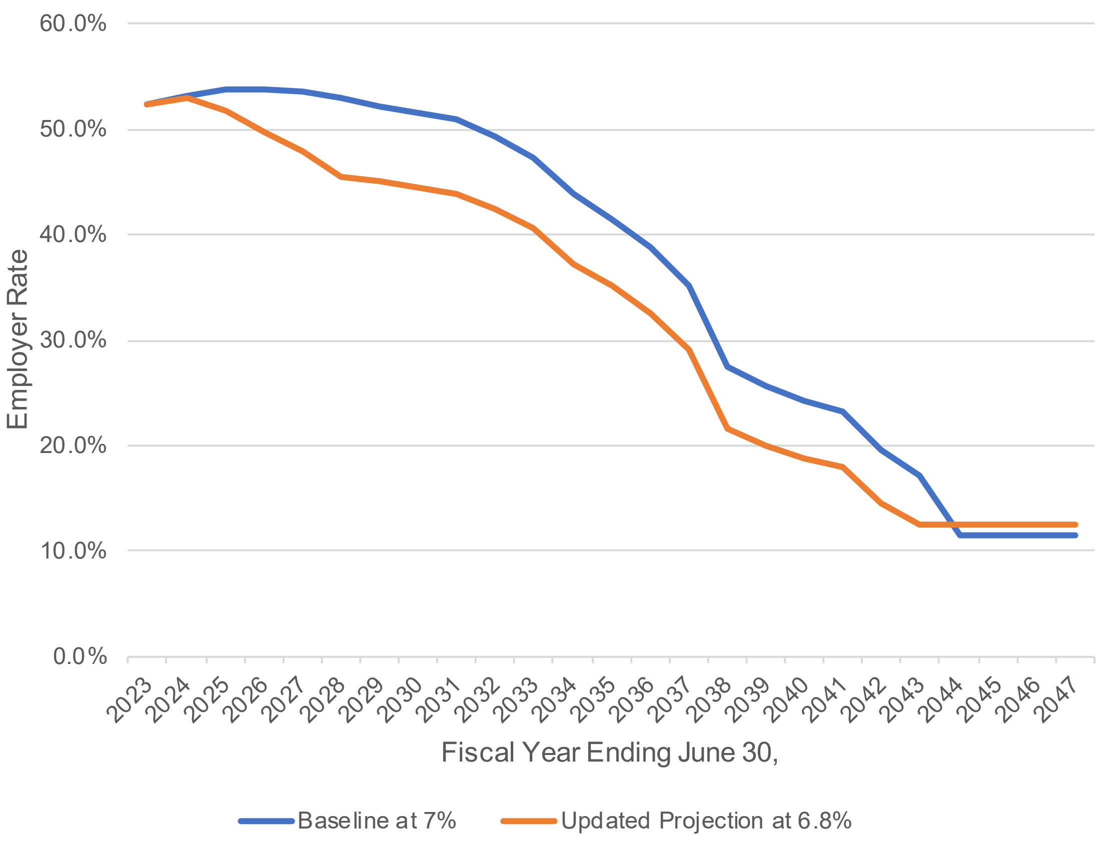
** *Ranges vary based on plan specifics*

Employer Contribution Rate Projections

Sample Public Agency Misc. Plan



Sample Public Agency Safety Plan



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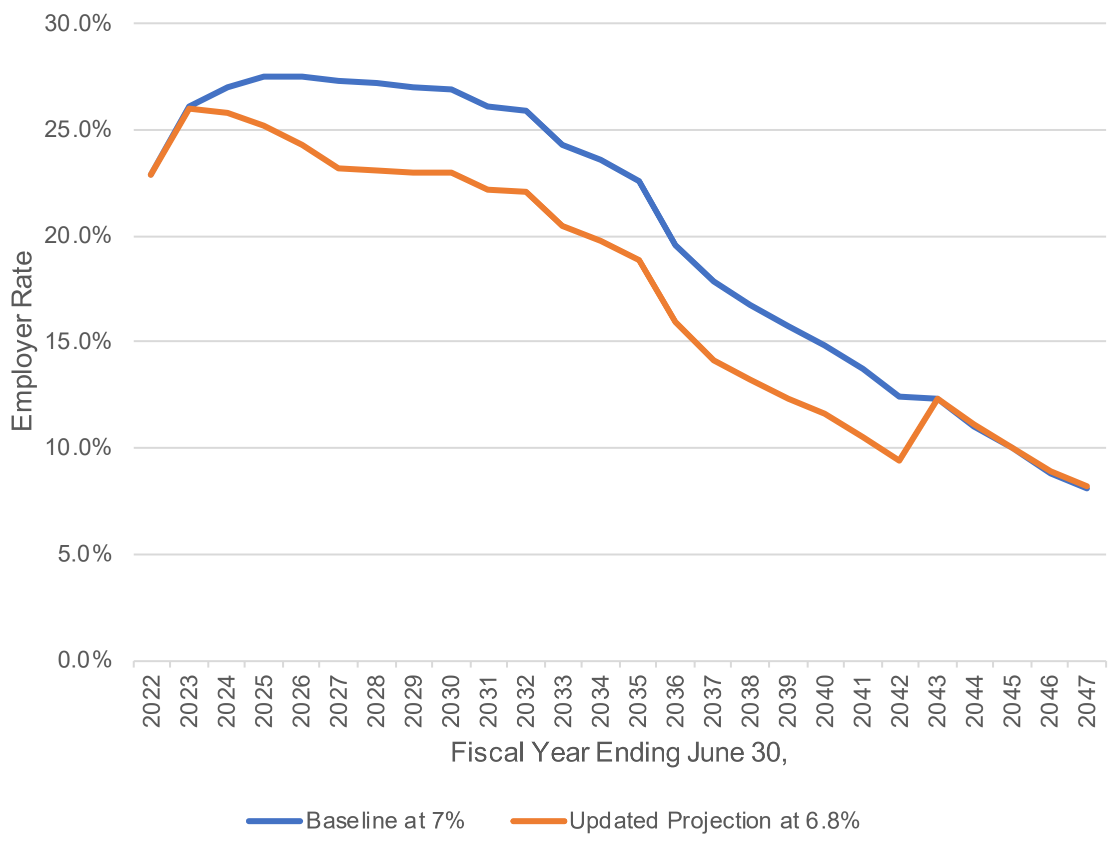
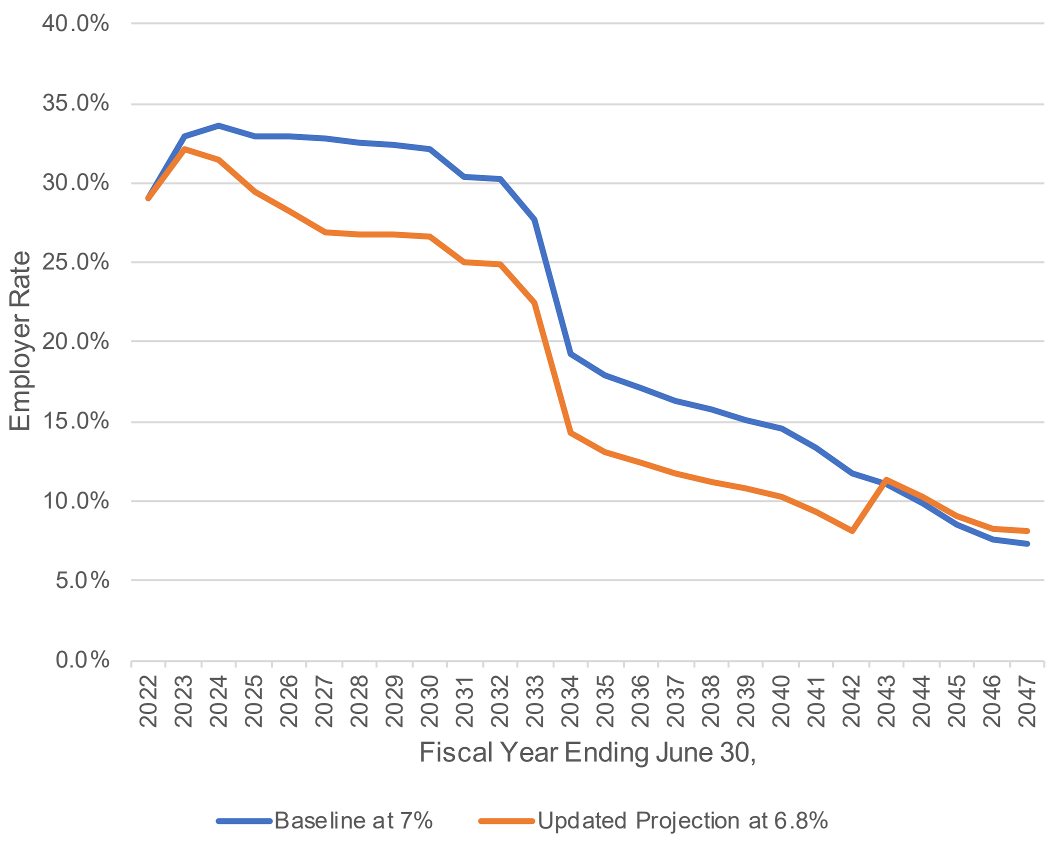
Employer Contribution Rate Projections

School Plan



State Misc. Plan



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Pension Outlook Tool – Model Any Plan's Contribution Rate Projections

Economic Assumptions

Details	Baseline	Model
Discount Rate	7.000%	**6.800%**
Payroll Growth	2.750%	**2.750%**
Inflation Rate	2.500%	**2.500%**

Investment Scenario Chosen

Rate	Period
21.300%	1
6.800%	1
6.800%	1
6.800%	7
6.800%	20

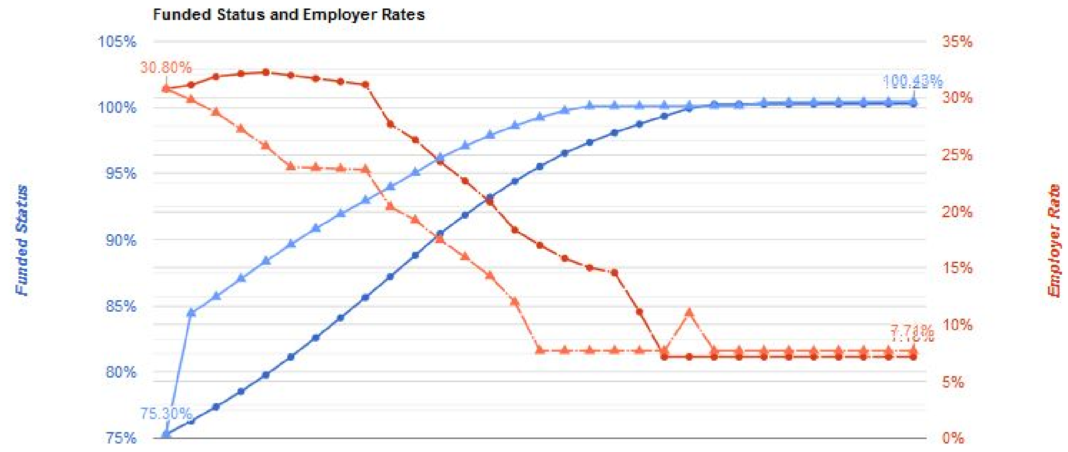
Other Assumptions

Details	Baseline	Model
PEPRA	Yes	**Yes**
Transition Years	15	**15**
ADP	No	**No**

30 Year Budget

Download the Fiscal Year Cost and Annual Relative Increase in Cost (XLSX).

Summary | Funding | Cash Flow | Glossary



How Are CalPERS Members Affected?

All members

Strengthens long-term sustainability of pension plan

Active members

- Minor technical changes to pension calculation based on retirement date
- Slight increase in service credit purchases based on date of request

Active PEPRA members

Increase in contributions in most plans, average of 0.8%

Retired members

No change to pension benefits or COLA

When Do PEPRA Member Rates Increase?

Discount rate lowered, assumptions changed → Normal cost increases → If discount rate increases normal cost base rate **by 1% or more**

- **No** → Employee contribution stays the same
- **Yes** → Employee contribution goes up — shares 50% of increase with employer

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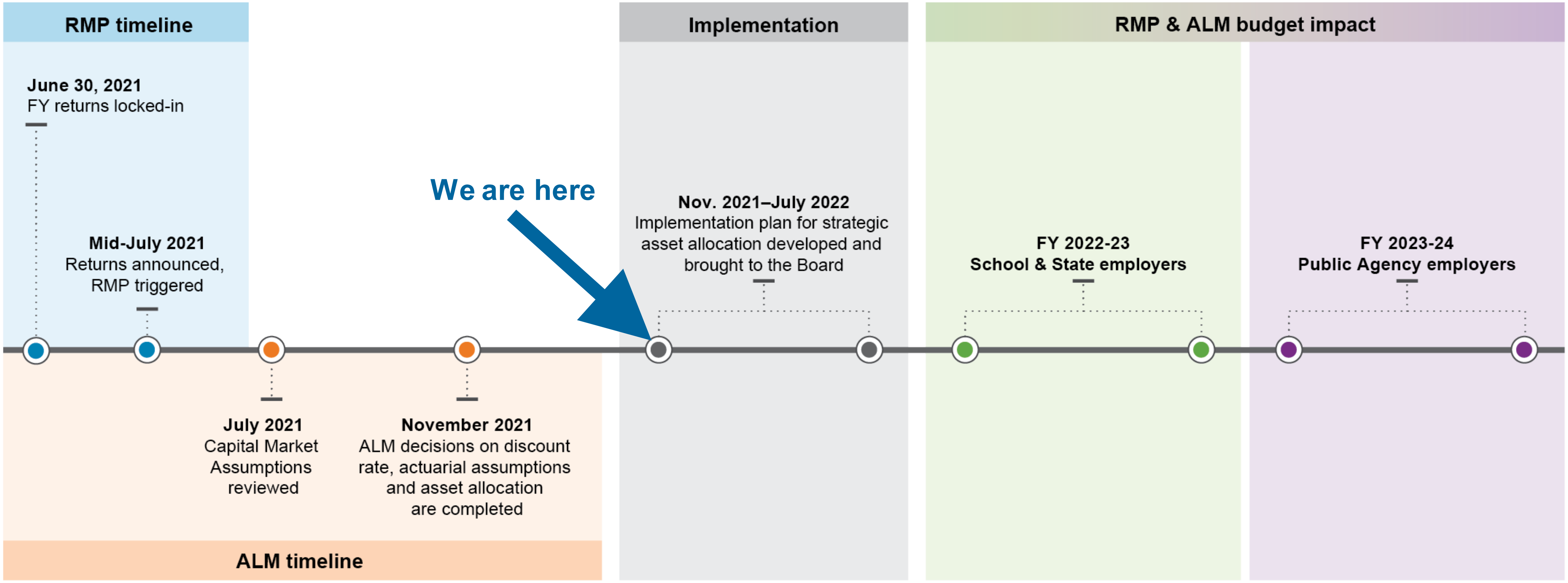
Implementation



Q&A

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