



Agenda Item 6b

November 17, 2014

ITEM NAME: Annual Report to the California Legislature – CalPERS
Emerging Manager Five-Year Plan

PROGRAM: Targeted Investment Programs

ITEM TYPE: Total Fund – Action

RECOMMENDATION

Approve transmission of CalPERS Emerging Manager Five-Year Plan annual report to the California Legislature pursuant to statutory requirements of Chapter 701 of the Statutes of 2011 (SB 294 Price).

EXECUTIVE SUMMARY

This agenda item seeks approval to submit the Emerging Manager Five-Year Plan, CalPERS Year Two Report to the State Legislature.

STRATEGIC PLAN

This item directly supports the CalPERS Strategic Plan goal to improve long-term pension and health benefit sustainability.

INVESTMENT BELIEFS

This item supports Investment Belief 3 that CalPERS investment decisions may reflect wider stakeholder views, provided they are consistent with its fiduciary duty to members and beneficiaries.

BACKGROUND

Chapter 701 of the Statutes of 2011 (SB 294 Price) requires CalPERS to complete and deliver a Five-Year Plan that describes our efforts in emerging manager investing. CalPERS shall submit a report to the Legislature, commencing March 1, 2014, and thereafter in compliance with Government Code § 9795.

ANALYSIS

In August 2012, CalPERS began implementing the Emerging Manager Five-Year Plan concentrating on Portfolio Management and External Outreach work streams. This Year Two report describes progress against the work streams over the 12-month period from July 1, 2013 through June 30, 2014.

BUDGET AND FISCAL IMPACTS

Not Applicable

BENEFITS/RISKS

The benefit of compiling the Emerging Manager Five-Year Plan is to provide a framework and single source of transparency into the CalPERS practices and engagement with emerging investment managers. Failure to comply with the reporting requirements of Chapter 701 of the Statutes of 2011 (SB 294 Price) could result in legal and reputational risk for CalPERS.

ATTACHMENTS

Attachment 1 – Emerging Manager Five-Year Plan, CalPERS Year Two Report to the State Legislature

LAURIE WEIR
Senior Portfolio Manager
Targeted Investment Programs

THEODORE ELIOPOULOS
Chief Investment Officer

CalPERS
EMERGING MANAGER FIVE-YEAR PLAN

Pathway to the Future

Year Two Annual Report to the State Legislature

March 1, 2015

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Insert a cover letter transmitting the report to the Legislature from Stausboll.

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Section 1

EXECUTIVE SUMMARY

In 2012, CalPERS' Board of Administration adopted the *Emerging Manager Five-Year Plan – Pathway to the Future* (Five-Year Plan or the Plan), which provides a strategic framework to guide CalPERS' investments and engagement with emerging investment managers. Under this plan, CalPERS will deliver annual updates to the California State Legislature, reporting on progress and accomplishments toward achieving plan goals.

The Five-Year Plan includes ten work streams, organized under two areas: (1) Portfolio Management and (2) External Outreach. CalPERS made notable progress on nine of the ten work streams during Year Two of the Plan, covering the period from July 1, 2013 through June 30, 2014. Information about the accomplishments under each of the work streams is detailed in this Year Two Annual Report, including these notable accomplishments.

Portfolio Management Work Streams

- Published the *Emerging Manager Exposure and Cost Report* in June 2014 which for the first time provides information on the exposure to, and cost of, the \$12 billion emerging manager initiatives in the CalPERS investment portfolio.
- Launched the restructured Global Equity Emerging Manager Program, increasing the market value of emerging managers to approximately \$3.0 billion, which represents approximately 10% of externally managed assets.
- Completed the Private Equity Emerging Manager Program Review. The purpose of this review was to identify lessons learned and adopt best practices for evaluating Private Equity investment managers and potential commitment of new capital to emerging managers.
- Presented results of the *CalPERS Emerging Manager Programs Benchmark Survey* in March 2014, which gathered information from U.S. public fund peers on their investment exposures with emerging managers and the goals, governance, and operations of their programs.

External Outreach

- Created the Targeted Investment Programs page on the CalPERS internet website, which now provides public access to a compendium of information of interest to the emerging and diverse investment manager community.
- Enhanced the internet based Investment Proposal Tracking System to improve the investment proposal submittal process, as well as improve Board reporting and communications related to emerging and diverse managers.
- Convened 400 attendees at the CalPERS *Emerging and Diverse Manager Forum* on April 1, 2014.
- Attended and participated as a featured speaker at 18 emerging and diverse investment manager events and meetings, connecting with key stakeholders and shared information about CalPERS' Emerging Manager programs.

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- Hosted the CalPERS Legislative Roundtable Workshop in August 2013, which provided information about CalPERS' Emerging Manager Programs to key legislative staff.

Also included in this report is information about CalPERS' Diversity and Inclusion Initiatives which are intertwined and related to the work being done under the Five-Year Plan. Diversity and Inclusion accomplishments include:

- Published in January 2014, *CalPERS' Commitment to Diversity and Inclusion Report for Fiscal Year 2012-13*. The report highlighted CalPERS' recent accomplishments and continued commitment to diversity and inclusion.
- Presented in June 2014, the results of the *CalPERS Peer Benchmark Survey: Women and Minority Owned Managers* to the CalPERS Board of Administration, Investment Committee. The results of this survey allowed staff to compare CalPERS' Emerging Manager Programs with those of similar U.S. public fund peers.
- The results of the *CalPERS Investment Manager and Consultant Diversity and Inclusion Survey* were presented to the Investment Committee in June 2014. The results of this survey allowed staff to compare the diversity of our external managers with the broader financial services industry.

Looking ahead, staff anticipates reporting the following accomplishments in Year Three of the Five-Year Plan, covering the period from July 1, 2014 through June 30, 2015.

- Commitment of an additional \$200 million to the Private Equity Emerging Manager Program to be deployed over the next four years.
- Commitment of an additional \$100 million to the continuation of a Real Estate emerging manager strategy.
- Examination of current processes for transitioning emerging managers to direct relationships and work to develop more formal processes and criteria for evaluating emerging managers and transitioning to direct investment mandates.
- Development of information sharing workshops for key stakeholders.

INTRODUCTION

For more than 20 years, CalPERS has developed and implemented emerging manager programs, as well as invested with emerging managers. For purposes of its programs, emerging managers are generally defined as newly formed or relatively small firms. Each CalPERS asset class has emerging manager definitions based on assets under management and/or length of track record. Attachment 1 details the current CalPERS Emerging Manager Programs and definitions across asset classes.

CalPERS has a fiduciary duty which requires the Board of Administration and staff to work at all times in the best interest of our 1.7 million members. As such, our objective for investing in emerging manager programs is to generate appropriate risk adjusted investment returns by identifying early stage funds with strong potential for success; accessing unique investment opportunities that may otherwise be overlooked; and cultivating the next generation of external investment management talent.

California law prohibits State agencies from discriminating against or granting preferential treatment to any individual or group on the basis of race, sex, color, ethnicity or national origin in the operation of public contracting. Therefore, CalPERS may not grant preferential treatment to emerging managers based on the above characteristics. Data shows, however, that women and minority managers make up a higher proportion of emerging managers than of all external managers; therefore, emerging manager strategies can result in greater ethnic and gender diversity among CalPERS' external investment managers.

CalPERS' investments with emerging managers are not limited to dedicated emerging manager programs. CalPERS is also committed to equal access and opportunity for all investment managers, who may submit an investment proposal to CalPERS at any time. To facilitate equality of access and opportunity for these managers, we have established an internet-based investment proposal submittal process and apply a consistent review process and decision-making criteria in evaluating all investment proposals received. In addition, CalPERS has made significant efforts to communicate our investment strategies and criteria for making investment decisions to the manager community, including emerging managers, to help ensure that investment proposals are aligned with CalPERS' objectives.

In 2012, CalPERS' Board of Administration adopted the *Emerging Manager Five-Year Plan – Pathway to the Future* (Five-Year Plan or the Plan), which provides a strategic framework to guide CalPERS' investments and engagement with emerging investment managers. Under this plan, CalPERS will deliver annual updates to the California State Legislature, reporting on progress and accomplishments toward achieving plan goals. The Five-Year Plan includes ten work streams, organized under two areas: (1) Portfolio Management and (2) External Outreach.

CalPERS' dedication to investing with emerging managers is also demonstrated by the integration of our Five-Year Plan into the *CalPERS Fiscal Year 2014-16 Business Plan*

and the *Investment Office Fiscal Year 2013-15 Roadmap*, which are the strategic plans that detail the key priorities and initiatives of both the CalPERS enterprise broadly and the Investment Office.

CalPERS adopted 10 *Investment Beliefs* (Attachment 2) in September 2013, which are intended to provide a basis for strategic management of the investment portfolio, inform organizational priorities, and ensure alignment between the Board and CalPERS staff. In particular, the following Investment Beliefs underpin the work in the Five-Year Plan:

- *Investment Belief 3: CalPERS' investment decisions may reflect wider stakeholder views, provided they are consistent with its fiduciary duty to members and beneficiaries.*
 - As a public agency, CalPERS has many stakeholders who express opinions on investment strategy or ask CalPERS to engage on an issue. CalPERS preferred means of responding to issues raised by stakeholders is engagement.
- *Investment Belief 8: Costs matter and need to be effectively managed.*
 - CalPERS will balance risk, return and cost when choosing and evaluating investment managers and investment strategies.
- *Investment Belief 10: Strong processes, teamwork and deep resources are needed to achieve CalPERS' goals and objectives.*
 - Diversity of talent (including a broad range of education, experience, perspectives and skills) at all levels (Board, staff, external managers, corporate boards) is important.

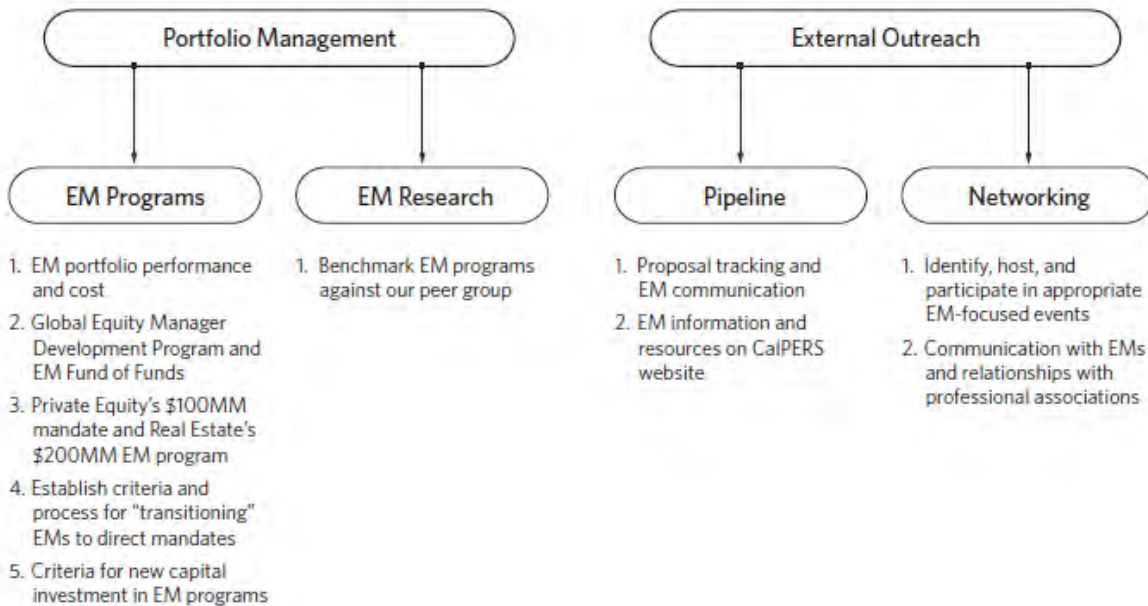
About the Five-Year Plan and CalPERS Year Two Annual Report

Chapter 701 of the Statutes of 2011 (SB 294 Price) requires the California Public Employees' Retirement System (CalPERS) to develop and implement a strategic plan for emerging investment manager participation across all asset classes. In August 2012, CalPERS adopted the *Emerging Manager Five-Year Plan – Pathway to the Future*, as its emerging manager strategic plan (Attachment 3). The Five-Year Plan was delivered to the State Legislature in August 2012, as directed by statute. The statute requires CalPERS to submit a progress report to the State Legislature by March 1 each year, from 2014 through 2017, with the last report due on January 1, 2018.

The Five-Year Plan details CalPERS' strategic efforts related to emerging manager investment strategies in two areas: (1) Portfolio Management and (2) External Outreach. These two strategic areas are further organized into 10 distinct work streams which are detailed below in Exhibit 1.

Exhibit 1

Emerging Manager Five-Year Plan Work Streams



Development of the Five-Year Plan, implementation of the work streams, monitoring and providing progress reports are the responsibility of the CalPERS Investment Office, specifically through the Targeted Investment Programs unit.

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During Year One of the Plan, staff fast-tracked its efforts and made notable progress on nine of the ten work streams. Many of the work streams are inter-related, or require feedback from other work streams that are underway or are set to be completed. As CalPERS implements the work streams over the remaining years of the Plan, there may be a need to make adjustments to the work streams or undertake efforts that are not specifically outlined in the Plan. Staff will include these efforts in the annual reporting under the Five-Year Plan. The Year One Annual Report is available online at <http://www.calpers.ca.gov/eip-docs/about/pubs/year-one-annual-report.pdf>.

As directed by statute, this Year Two Report details the progress made on the work streams of the Five-Year Plan from July 1, 2013 through June 30, 2014. To ensure CalPERS is providing the State Legislature the most current and comprehensive understanding of our efforts under the Plan, activities that have been initiated since June 2014 have also been noted in each section as “Looking Ahead”. These activities will be captured, in detail, in the Year Three Report.

During Year Two of the Plan, staff completed or made notable progress on all but one of the work streams in the Plan. In this report, CalPERS updates the State Legislature and other interested parties about the deliverables under the Portfolio Management work streams (*Emerging Manager Exposure and Cost Report, CalPERS’ Peer Survey: Emerging Manager Programs*, Global Equity Emerging Manager Restructure, internet-based investment proposal submission system enhancements, and new emerging manager commitments). This report also provides a progress update on the External Outreach work streams (*April 2014 Emerging and Diverse Manager Forum*, Legislative workshops, stakeholder meetings and events, CalPERS’ Targeted Investment Programs internet page improvements, and communications plans).

Section 2

FIVE-YEAR PLAN: YEAR TWO ANNUAL REPORT

The following details CalPERS' progress on the Five-Year Plan work streams related to Portfolio Management and External Outreach. Staff is reporting on six work streams under Portfolio Management and four work streams under External Outreach. Each work stream is provided with its desired outcomes, followed by accomplishments in the reporting period of July 1, 2013 through June 30, 2014, efforts initiated after the reporting period, and next steps.

A. Portfolio Management Initiatives

EMERGING MANAGER PROGRAMS

Emerging Manager Programs Work Stream 1:

Establish performance, cost, and diversity of existing emerging manager portfolio

Investment performance of CalPERS' emerging manager programs has been mixed. To better understand specific issues related to performance, the first Portfolio Management work stream outlined in the Plan requires CalPERS to identify performance, cost, and diversity of the existing emerging manager investment portfolio.

Desired outcomes within years 1-3 of the Five-Year Plan:

- Identify and implement a consistent and clear set of metrics to assess emerging manager program performance and cost
- Track information regarding the diversity of our investment managers
- Institute a process for evaluating emerging manager program metrics to facilitate appropriate benchmark comparisons and guide program strategy
- Develop appropriate reporting approaches for each asset class and aggregate asset class reports into a Total Fund report

Summary of Accomplishments

In the Year One Report, covering the period of August 1, 2012 through June 30, 2013, staff reported the release of the *Emerging and Diverse Manager Data Report* in March 2013. This work stream was completed with the release of the *Emerging Manager Exposure and Cost Report* in June 2014.

❖ Emerging Manager Exposure and Cost Initiative

The *Emerging Manager Exposure and Cost Report* (Attachment 4) was presented to the Investment Committee in June 2014. This Report provides information on the exposure to, and cost of, emerging manager investment initiatives in the CalPERS' investment portfolio. The information regarding

emerging managers encompasses CalPERS' investments made through direct relationships and fund of fund advisors, including underlying funds in fund of funds. The Report shows CalPERS invested a total net asset value of \$12 billion with 393 emerging managers. Costs were reported in three major expenditure categories: 1) investment management fees, 2) personnel costs, and 3) other expenses such as consultants and travel. Highlights from the Report include:

- Costs associated with emerging manager program investments totaled \$201.6 million or 15.6%.
- Across the relevant asset classes consisting of Absolute Return Strategies (ARS), Global Equity, Private Equity and Real Estate, as well as Targeted Investment Programs, emerging manager programs accounted for approximately 8.2% of staff time.

Looking Ahead:

- ❖ Establish consistent emerging manager performance reporting into the Total Fund Report

In addition to completing the work stream, staff has undertaken additional work to establish regular performance reporting for emerging manager exposures across the investment portfolio. Staff will identify the necessary improvements to streamline emerging manager program data collection processes in each of the asset classes. Staff expects to complete this effort in Year Three of the Plan.

Emerging Manager Programs Work Stream 2:

Review Global Equity Manager Development Program and Emerging Manager Fund of Funds Program

In 2010, the Global Equity Unit initiated portfolio restructuring to transition the traditional capital allocation model to a risk-adjusted return model. CalPERS also reviewed the Manager Development Program and Emerging Manager Fund of Funds programs with three key goals: to achieve superior risk-adjusted investment returns; to continue providing opportunities for new and emerging investment managers; and to incorporate emerging managers into the broader Global Equity Unit capital allocation model. CalPERS engaged its fund-of-fund partners to better identify highly qualified managers, provide capability development guidance, and establish the process and criteria for determining whether to transition an emerging manager to a larger, direct investment mandate.

Desired outcomes within years 1-3 of the Five-Year Plan:

- Conduct a strategic review of Global Equity Emerging Manager Programs
- Identify a core set of high-performing emerging managers

Summary of Accomplishments

❖ Global Equity Emerging Manager Program Restructure

CalPERS, working in conjunction with its external advisors in Global Equity, substantially completed and launched a restructured emerging manager program. The restructure increased the capital to emerging managers in the Global Equity asset class to approximately \$3.0 billion, representing approximately 10% of externally managed assets. The restructuring was intended to better leverage the skills and resources of CalPERS' advisors in identifying, selecting, and creating more meaningful relationships with emerging managers. As a result, emerging managers became: 1) better aligned with CalPERS' overall investment strategy for Global Equity, 2) better positioned to deliver impact to the total Global Equity portfolio, and 3) in closer contact with CalPERS staff.

❖ Global Equity Emerging Manager Restructure Communication Plan

Staff engaged in significant outreach and communication efforts with representatives of emerging managers and stakeholders in the Global Equity asset class. Outreach efforts on the Global Equity restructure included a webinar on February 25, 2014 to communicate the process and desired outcome of restructuring of the Global Equity emerging manager program.

Looking Ahead:

Staff will finalize all efforts to complete the restructure and report completion to the Investment Committee.

Emerging Manager Programs Work Stream 3:***Manage, track, and report progress of Private Equity's \$100 million and Real Estate's \$200 million Emerging Manager programs***

Since August 2011, CalPERS has committed an additional \$100 million to its Private Equity Emerging Manager Program and \$200 million to its Real Estate Emerging Manager Program. This work stream focuses on ensuring appropriate management and tracking of these investments so investment performance, cost, and other relevant factors can be evaluated and used for investment decision making.

Desired outcomes within years 1-5 of the Five-Year Plan:

- Develop appropriate metrics and approach for monitoring performance and assessing the success of Private Equity and Real Estate Emerging Manager Programs

- Manage, track and report progress on an ongoing basis to guide future investments
- Identify key success factors and lessons learned, to inform best practices and Emerging Manager program development across asset classes

Summary of Accomplishments

❖ Private Equity

Since the Year One Report, three new investments have been made in Private Equity's EM Program managed by Grosvenor Capital Management (formerly the Customized Fund Investment Group).

- Maranon Mezzanine II: Maranon Capital provides senior financing, mezzanine debt and equity co-investments for both private equity-backed as well as entrepreneur-owned middle market transactions.
- Valor Equity III: Valor Equity is an operationally active private equity firm focused on making expansion, growth and buyout investments and is the third minority owned firm selected for the Private Equity EM Program.
- New Heritage Capital Fund LP: New Heritage specializes in growth capital investments and acquisitions.

❖ Real Estate

In January 2014, the Canyon Catalyst Fund (CCF), a California-only program, increased its initial \$30 million commitment to Rubicon Point Partners to \$50 million. Rubicon Point Partners is a San Francisco based woman-owned firm focusing on investment strategies in office and datacenter property sectors primarily in Northern California.

In May 2014, CCF increased its initial \$30 million commitment to Sack Properties to \$50 million. Sack Properties is a San Francisco based woman-owned firm specializing in multifamily properties in California.

As of June 30, 2014, CCF invested \$87 million of its \$200 million commitment in multifamily, office, and retail properties in California.

Looking Ahead:

- ❖ New Private Equity emerging manager commitment of \$200 million effective October 2014. The \$200 million will be invested through an emerging manager fund of funds manager dedicated to private equities.
- ❖ A commitment of \$100 million was made to a co-investment partnership in Real Estate in September 2014. The co-investment partnership is comprised of an

emerging manager and a Real Estate investment partner who will serve as advisor and mentor in the relationship.

- ❖ Continued monitoring and management of Private Equity and Real Estate's Emerging Manager Programs investments. There are potential emerging manager investments pending due diligence and execution during Year Three of the Plan.

Emerging Manager Programs Work Stream 4:

Establish criteria for “transitioning” emerging managers to direct mandates

The goal of this work stream is to establish criteria to evaluate emerging managers' potential for direct investment mandates. This will be done by building on demonstrated performance and capabilities, actively managing risks, and providing a clear understanding of what is required of emerging managers to compete for additional capital.

Desired outcomes within years 1-3 of the Five-Year Plan:

- Develop criteria for evaluating emerging manager “transition” to direct mandates
- Through fund of fund partnerships and internal managers, engage with existing emerging managers to communicate the criteria for evaluation
- Track and report the number of emerging managers transitioned
- Create appropriate forums and mechanisms for sharing information on transitioning criteria with emerging managers and appropriate stakeholder groups

Looking Ahead:

CalPERS has in the past, and will continue to identify emerging managers in fund of funds for transition to direct investment relationships. The purpose of this work stream is to document the current process by which emerging managers transition to direct mandates, to seek to identify best practices centered on those processes, and share this information with our stakeholders.

Emerging Manager Programs Work Stream 5:

Evaluate and establish criteria for new capital to Emerging Manager programs

The information and lessons learned from CalPERS' research, analysis, outreach, and strategic reviews will assist CalPERS in determining prudent targets for emerging manager participation. In developing the emerging manager program strategies, factors to be considered include availability of new capital for investment, capital allocation among asset classes, percent of assets managed externally, emerging manager performance and costs, and the size of the viable universe of emerging managers, while also ensuring alignment with CalPERS' investment strategy.

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Desired outcomes within years 1-5 of the Five-Year Plan:

- Source and review data regarding emerging manager program performance, cost and growth potential
- Design and execute targeted research and analysis efforts to develop a deeper understanding of emerging manager performance
- Leverage internal and external insights to assess CalPERS' Emerging Manager programs and to inform the evolution of CalPERS' Emerging Manager commitment
- Establish criteria for success of emerging manager programs
- Evaluate potential for new capital to be invested through emerging manager programs

Summary of Accomplishments

❖ CalPERS Private Equity Emerging Manager Program Review

The review identified lessons learned and adopted best practices for evaluating Private Equity investment managers and potential commitment of new capital to emerging managers.

In-depth reviews were performed on 12 emerging managers in the CalPERS Private Equity portfolio with varying features and investment return results. The reviews identified characteristics and attributes contributed to an emerging manager's success. Findings were presented to a panel of industry experts in a workshop environment, allowing panel members to discuss and challenge the findings and, ultimately, seek consensus on best practices.

The results of this initiative were reported to the Investment Committee in March 2014 and during the CalPERS' Emerging and Diverse Manager Forum, that took place on April 1, 2014.

Looking Ahead:

Staff will finalize this work stream in Years Four and Five of the Five-Year Plan.

Emerging Manager Research

Emerging Manager Research Work Stream 1:

Benchmark Emerging Manager program against our peer group

CalPERS is committed to maintaining leadership in emerging manager programs. This work stream directed staff to compare CalPERS' Emerging Manager programs against our peers in the institutional investor community.

Desired outcomes within years 2-5 of the Five-Year Plan:

- Create and implement benchmarking analysis by asset class for emerging manager program design and implementation

Summary of Accomplishments

❖ Emerging Manager Peer Benchmark Project

In March 2014, staff and consultant Callan Associates, presented the results of the *CalPERS Emerging Manager Programs Benchmark Survey* (Attachment 5). This peer survey was executed to understand investment exposures with emerging managers, and the goals, governance, and operations of each emerging manager program in order to learn how other programs are implemented. The survey was intended to provide CalPERS with insight into the best practices of similar U.S. public fund peers.

- CalPERS had the highest exposure to emerging managers at the total fund level among the seven funds that responded out of the 11 institutional funds targeted as peers.
- CalPERS' percentage allocations to emerging managers in private equity and public equity meet or exceed the peer fund averages.
- Three peer funds explicitly include minority and/or women owned firms in their definition and two peers include disabled and/or disabled veteran owned firms.

As a result of this survey, Callan was engaged to conduct a follow-on survey to examine peer exposure to women and minority owned investment managers. Presented to the Investment Committee in June 2014, this follow-on survey is detailed on page 22 in the Diversity and Inclusion section of this report.

B. External Outreach Initiatives

PIPELINE

Pipeline Work Stream 1:

Improve emerging manager proposal tracking and communication

CalPERS is committed to providing equal access and opportunity for submittal and consistent review of emerging manager investment proposals. This work stream aims to improve and enhance the centralized internet-based portal system through which all investment proposals are received and routed to the appropriate asset classes for evaluation. The goal of this work stream is also to educate and improve communication with potential emerging manager partners about the investment proposal submittal

process, the decision criteria and process for evaluating investment proposals, and range of potential outcomes.

Desired outcomes within years 1-3 of the Five-Year Plan:

- Develop educational materials and a more robust communication strategy regarding the process and decision making criteria related to the submittal of investment proposals.

Summary of Accomplishments

❖ Investment Proposal Tracking System (IPTS) Improvement

Significant improvements to IPTS have been made, including:

- Ease of use for managers
- Capturing emerging and diverse manager data
- New response guidelines for more constructive feedback
- Ability to enter and save data and return in 90 days

❖ Emerging Manager Communications Initiative

The Emerging Manager Communications Initiative strived to strengthen communications with emerging and diverse managers and stakeholder groups, as well as facilitate a better understanding of the IPTS submittal and review process. This work encompassed:

- Review and update procedures and communication strategies
- Improve overall outputs and documentation from IPTS
- Establish improved communications and feedback regarding emerging and diverse managers on the evaluation and decision process
- Improve communications to facilitate stronger working relationships with emerging and diverse managers

Looking Ahead:

- ❖ This work stream is complete. However, staff will continue to work to evaluate, enhance and improve the IPTS system to meet the information and program needs of CalPERS and the emerging manager investment community.

Pipeline Work Stream 2:

Improve emerging manager information and resources on CalPERS' website

The goal of this work stream is to review and identify enhancements to CalPERS' website to provide better and improved access to information about the CalPERS Investment Office, its strategies and processes, and other information important to our external stakeholders.

Desired outcomes within years 3-5 of the Five-Year Plan:

- Conduct research and analysis to evaluate relevant portions of CalPERS' website:
 - Outreach and analysis to understand user needs
 - Current tool capability, usability, and utilization assessment
- Define and implement required improvements for the use of the CalPERS website as a critical tool for communication and engagement with emerging managers

Summary of Accomplishments

❖ Targeted Investment Programs Internet Page

In late December 2013, staff launched the Targeted Investment Programs internet page and worked with stakeholder groups to publicize the internet page. The internet page provides information about initiatives and activities in the emerging and diverse manager areas, as well as engagement with labor stakeholders and administration of the Responsible Contractor Program Policy, and coordination and reporting of California Investment Programs. In support of the Five-Year Plan, the Internet page provides:

- A calendar of events (meetings, forums, and events)
- Emerging Manager Five-Year Plan and deliverables
- Targeted Investment Programs updates to the Investment Committee
- Centralized location for Targeted Investment Programs publications
- Links to asset class information and strategies
- Links to the web based Investment Proposal Tracking System

Looking Ahead:

This work stream is complete. As processes and programs change, staff will continue to work to evaluate, enhance and improve the web page to meet the information and program needs of CalPERS and the emerging manager investment community.

NETWORKING

Networking Work Stream 1:

Identify, host, and/or participate in emerging manager-focused events

CalPERS has a long history of hosting and participating in industry association events focused on emerging and diverse managers. This work stream focuses on staff's outreach efforts via conferences, webinars, workshops, and meetings to strengthen CalPERS' relationships and improve communications with our stakeholders.

Desired outcomes within years 1-5 of the Five-Year Plan:

- Further strengthen CalPERS' presence in emerging manager networks through industry associations
- Co-host four emerging manager investment workshops with the Legislature and CalSTRS over a two year period
- Host webinars focused on emerging managers and/or stakeholder groups
- Continue to participate in conferences and events featuring emerging manager investment programs

Summary of Accomplishments

❖ CalPERS Emerging and Diverse Manager Forum

On April 1, 2014, CalPERS hosted its second *Emerging and Diverse Manager Forum*. The theme of the event focused on California public pension funds and their emerging manager initiatives. Senior investment officials throughout pensions in California were gathered to discuss their views on emerging and diverse managers, as well as to provide information on the opportunities available to managers. Representatives from CalPERS' asset classes hosted panels and roundtable discussions during which staff answered questions from emerging managers. The Forum materials, including event videos, are available online and can be found on the Targeted Investment Programs web page. Feedback from the event was positive, including 98% of post-event participants rating the overall event above average or excellent.

California public pensions that participated in the event program include:

- California State Teachers' Retirement System
- Los Angeles City Employees' Retirement System
- Los Angeles Fire and Police Pensions
- San Joaquin County Employees' Retirement System
- Oakland Fire and Police Pensions

❖ CalPERS Legislative Roundtable Workshop

The August 8, 2013 workshop provided an opportunity to educate key legislative staff about Investment Office issues, procedures and policies. The workshop also provided an opportunity to communicate Investment Office efforts related to Emerging and Diverse Manager Programs.

❖ Global Equity Emerging Manager Webinar

CalPERS Investment Office hosted a webinar focused on Global Equity's restructured Emerging Manager Program on February 25, 2014. The webinar discussed the restructuring of the emerging manager program that resulted in an

increase of capital to emerging manager strategies for the asset class. The restructuring is intended to better leverage the skills and resources of CalPERS' advisors in identifying, selecting and creating more meaningful relationships with high-performing emerging managers.

- ❖ CalPERS hosted the New American Alliance (NAA) 2014 National Tour on April 2, 2014 at CalPERS headquarters in Sacramento.

Looking Ahead:

- ❖ This work stream is on-going throughout the Five-Year Plan. Staff will continue to reach out to external stakeholders to strengthen CalPERS' presence in emerging manager networks through industry associations.

Networking Work Stream 2:

Improve communication with emerging managers and professional associations

CalPERS believes that constructive engagement with the emerging manager community is a critical element to continuing our commitment to emerging managers. As such, CalPERS is focused on strengthening efforts in 1) outreach, 2) education and messaging, 3) technology networking tools, and 4) ongoing communications.

Desired outcomes within years 1-3 of the Five-Year Plan

- Improve messaging materials and website to communicate with emerging managers
- Engage directly with the emerging manager community via workshops and interactions with trade and professional associations

Summary of Accomplishments

- ❖ Engagement with Emerging and Diverse Emerging Manager Industry Organizations

CalPERS had multiple engagements and communications with the following major emerging manager investment community stakeholders.

- Association of Asian American Investment Managers (AAAIM)
- National Association of Investment Companies (NAIC)
- National Association of Securities Professionals (NASP)
- New America Alliance (NAA)

- ❖ CalPERS' participation in emerging and diverse manager conferences and events.

During the reporting period, July 1, 2013 through June 30, 2014, staff attended and/or participated as a featured speaker in the following emerging and diverse manager events detailed below.

- AAAIM National Conference
- Annual Emerging Manager Conference hosted by the Teachers Retirement System of Texas and the Employee Retirement System of Texas
- Consortium hosted by RG & Associates
- Credit Suisse Conference on Small & Emerging Managers in Private Equity, Real Estate and In-State Investments
- Invesco Tools for Success Forum
- NAA Wall Street Summit
- NAIC Annual Meeting and Convention
- NASP Annual Conference
- Networking Event hosted by Bank of America Merrill Lynch Capital Access Funds Event
- NY Controllers Annual Investment & Emerging Manager Conference
- Toigo Annual Conference
- Toigo 25th Anniversary Celebration Los Angeles and New York City
- SEO Alternative Investments Conference

Looking Ahead:

- ❖ This work stream is on-going throughout the Five-Year Plan. CalPERS will continue to engage with stakeholder groups and participate in their organizations' meetings, conferences, and events related to emerging and diverse managers in the investment area.

Section 3

DIVERSITY AND INCLUSION EFFORTS

As the nation's largest public pension fund, within the nation's most ethnically and culturally diverse state, we recognize diversity is a competitive advantage. CalPERS broadly interprets diversity to mean differences such as age, ethnicity, culture, or gender that result in diversity of thinking. CalPERS seeks diversity of internal staff, corporate boards, and external investment managers in an effort to secure high functioning teams that incorporate different ways of seeing and solving problems.

CalPERS is committed to provide equality of access for investment managers and is committed to open communication of our exposures, investment strategies, and criteria for investment decision making.

The projects detailed below are directly related to CalPERS Diversity and Inclusion initiatives, and as such, are intertwined with our Emerging Manager program efforts.

❖ CalPERS Peer Benchmark Survey: Women and Minority Owned Managers

CalPERS Peer Benchmark Survey: Women and Minority Owned Managers (Attachment 6) was presented to the Investment Committee in June 2014. This peer survey examined investment manager diversity, specifically exposures to women and minority owned managers amongst CalPERS and U.S. public fund peers.

- CalPERS invests \$4.5 billion in women and minority owned firms, ranking third among its peer funds and employs 89 women and minority managers, more than twice the number of the next highest peer fund.
- CalPERS' largest exposure to women and minority owned firms by total assets is in Public Equity (\$1.6 billion), followed by Real Estate (\$1.4 billion), Private Equity (\$1.2 billion) and Absolute Return Strategies (\$256 million).

❖ CalPERS Investment Manager and Consultant Diversity and Inclusion Survey

In June 2014, staff presented the results of the *CalPERS Investment Manager and Consultant Diversity and Inclusion Survey* (Attachment 7) to the Investment Committee. This survey asked CalPERS' current investment managers and consultants to share information about firm workforce and key position diversity, firm governance diversity, and firm diversity and inclusion practices. This survey was voluntary and is likely to contain a bias with more diverse firms responding and less diverse firms not responding. Additionally, there is a large firm bias as six firms provided 69.7% of the total investment workforce in this survey. Highlights of the survey include:

- Over 63% (147 of 232) of CalPERS' current investment managers and consultants responded to the survey which represents a total of 51,466 employees. Throughout the survey, results were compared to the Equal Employment Opportunity Commission (EEOC) investment industry data.
- The percentage of women and minorities in key positions decreases as seniority increases. When percentages of women and minorities in key positions in CalPERS' firms are compared to the investment industry data, the percentages are similar.
- Larger firms are more likely to have written diversity and inclusion policies and practices.

❖ Diversity and Inclusion in CalPERS Investment Office Recruitments

In the fall of 2013, the Investment Office, working with CalPERS' Human Resources Office and the Diversity Office, initiated various activities designed to strengthen its talent strategy as it relates to diversity and inclusion. These efforts were designed to attract, develop, and retain a highly-skilled, diverse, and motivated team. These activities included expanded recruitment and outreach efforts through contracting with LinkedIn and Professional Diversity Network. In addition, the Investment Office now posts job advertisements to other diversity and financial websites and approximately seven college MBA and/or alumni websites.

Other diversity and inclusion initiatives include engagement with external consultants on projects to enhance the Investment Office's talent sourcing and acquisition. Key components include:

- Analysis of best practices across institutions with leading diversity practices to identify and understand leading edge strategies and tactics
- Identification of networks for strategic alliances and recruitment advertising venues for facilitation of a diverse candidate pool

Looking Ahead:

- ❖ Staff will continue to look at the diversity pipeline of talent through MBA programs and external stakeholder organizations for meaningful ways to engage with the investment industry. In the coming year, staff intends to engage investment managers and consultants on diversity by presenting the results of the survey in a webinar and in a report for all managers and consultants to review.

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Section 4

CONCLUSION

Our objective for investing in emerging manager programs is to generate appropriate risk adjusted investment returns by identifying early stage funds with strong potential for success; accessing unique investment opportunities that may otherwise be overlooked; and cultivating the next generation of external investment management talent.

CalPERS will continue its efforts to examine and improve its emerging managers programs and to communicate with emerging managers and other interested stakeholders about the goals of our investment programs.

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Section 5

REFERENCES

1. CalPERS Emerging Manager Programs and Definitions
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2. CalPERS Investment Beliefs
<http://www.calpers.ca.gov/eip-docs/investments/policies/invo-policy-statement/investment-beliefs.pdf>
3. Emerging Manager Five-Year Plan
<http://www.calpers.ca.gov/eip-docs/about/pubs/emerging-manager-five-year-plan.pdf>
4. Emerging Manager Exposure and Cost Report
<http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/invest/201406/item07b-02.pdf>
5. CalPERS Emerging Manager Programs Benchmark Survey
<http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/invest/201403/ite-02.pdf>
6. CalPERS Peer Benchmark Survey: Women and Minority Owned Managers
<http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/invest/201406/item07c-01.pdf>
7. CalPERS Investment Managers and Consultant Diversity and Inclusion Survey
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