

Private Debt Investment Update

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I. Program Overview

II. Benefits of Private Debt

III. Risks of Private Debt

IV. Current Market in Private Credit

V. ESG Considerations

Program Overview | Private Debt

Role

Private Debt seeks to harvest premiums from the structure complexity and illiquid nature of private loans while generating current income.

Activity

Since inception (2020), Private Debt has committed over \$24Bn with \$8.9Bn in NAV.

Investment Beliefs

- II. A long investment horizon is a responsibility and an advantage.
- VII. CalPERS will take risk only where we have a strong belief we will be rewarded for it.
- VIII. Costs matter and need to be effectively managed.
- X. Strong processes and teamwork and deep resources are needed to achieve CalPERS goals and objectives.



I. Program Overview

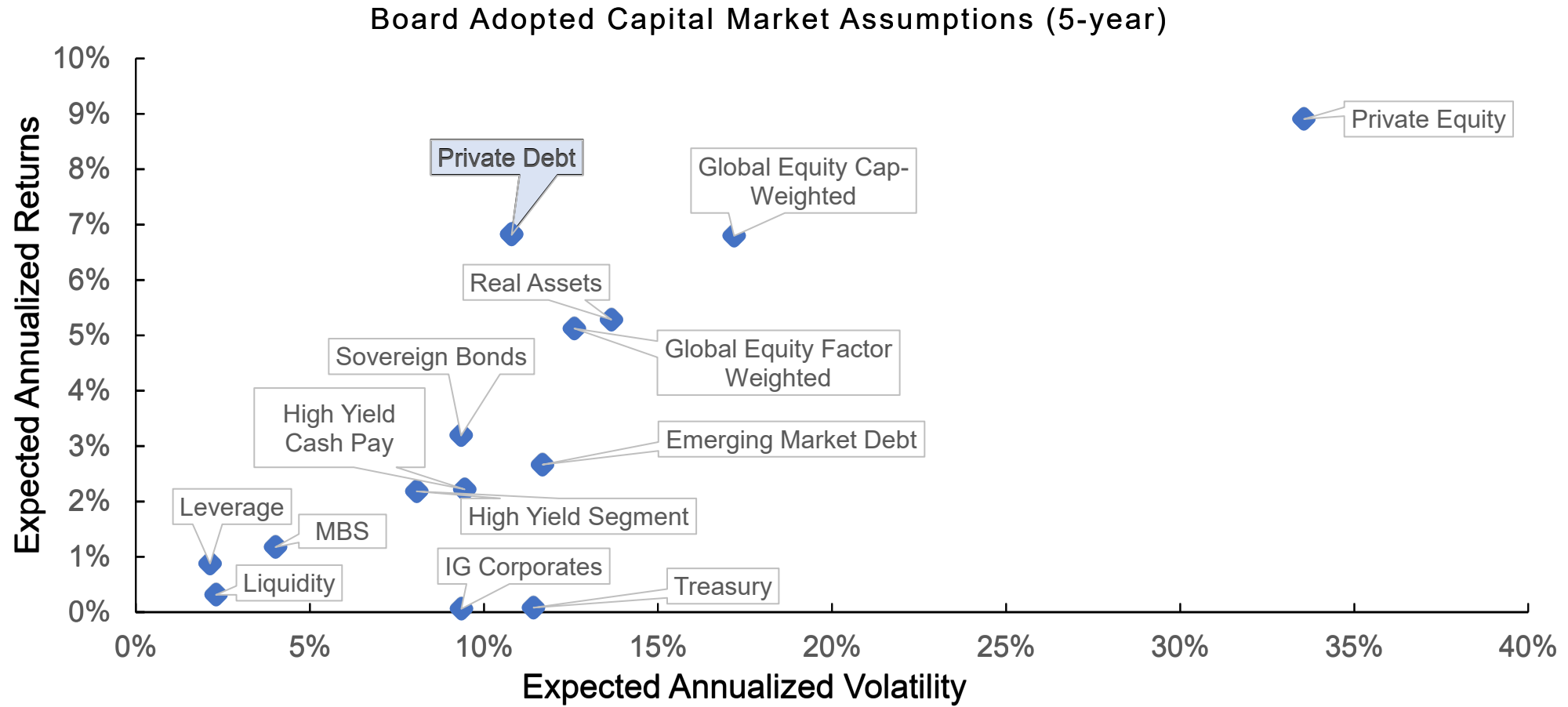
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Attractive Risk- Adjusted Returns



Source: Capital market assumptions adopted as part of the 2021-22 ALM process, September 13, 2021.

Cash Flow Profile Complements Private Equity

Private Debt:

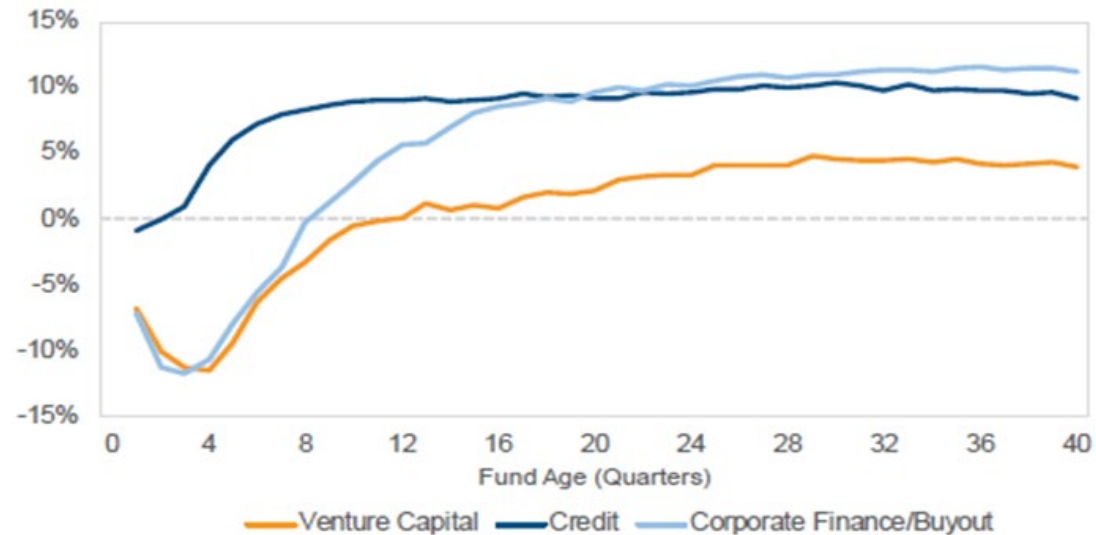
Quarterly interest payments drives a constant cash flow stream throughout the deal life



Private Equity:

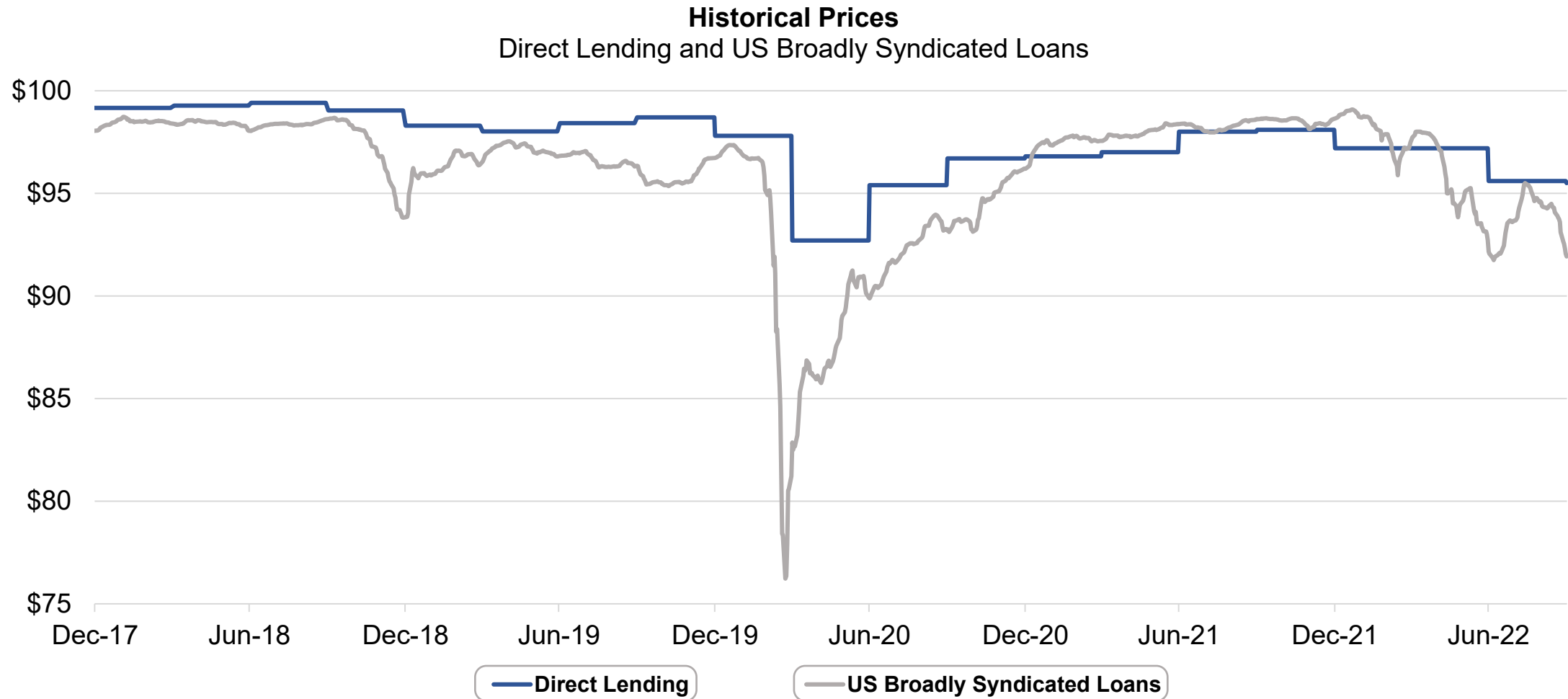
Negative cash flows during initial years of an investment before realizing returns (“J-curve”)

Median IRR J-Curves by Strategy
Vintage Years 1974-2018



Source: Hamilton Lane Fund Investment Database
As of 3/31/2018 (September 2018).

Accounting Diversification

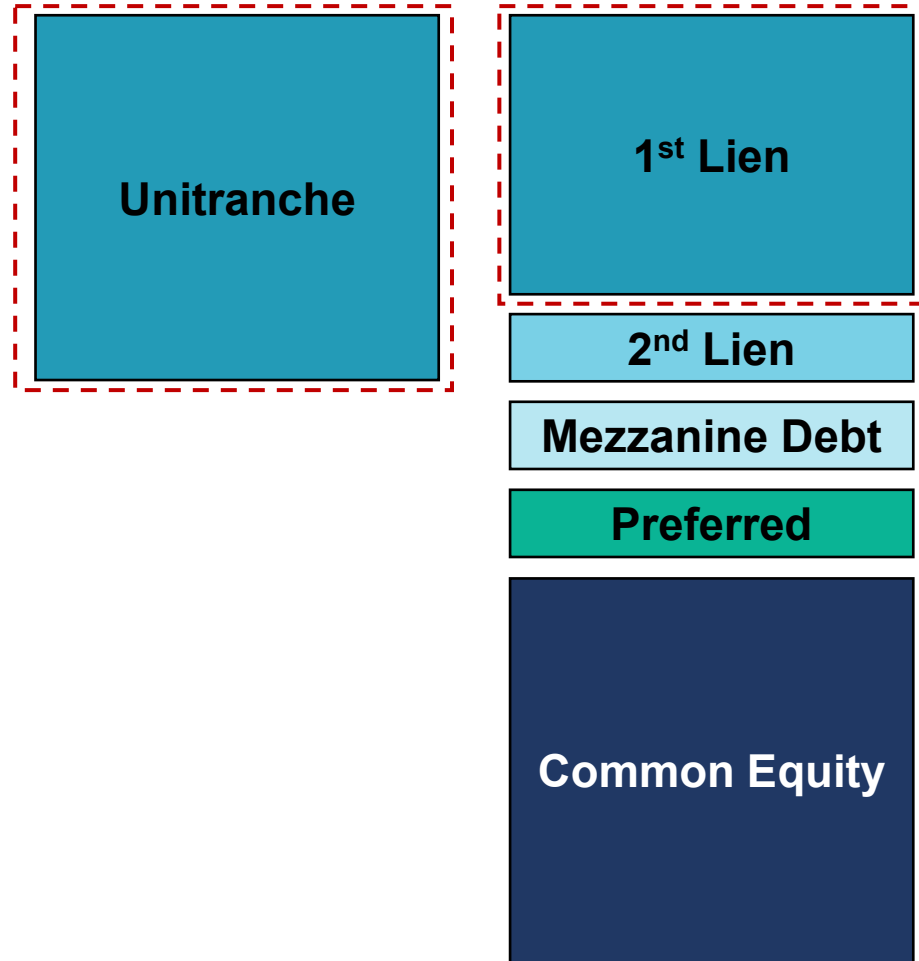


Source: Data for US Broadly Syndicated Loans are prices from Morningstar LSTA US Leveraged Loan index from Morningstar / PitchBook Leveraged Commentary & Data (LCD).



Higher in the Capital Structure

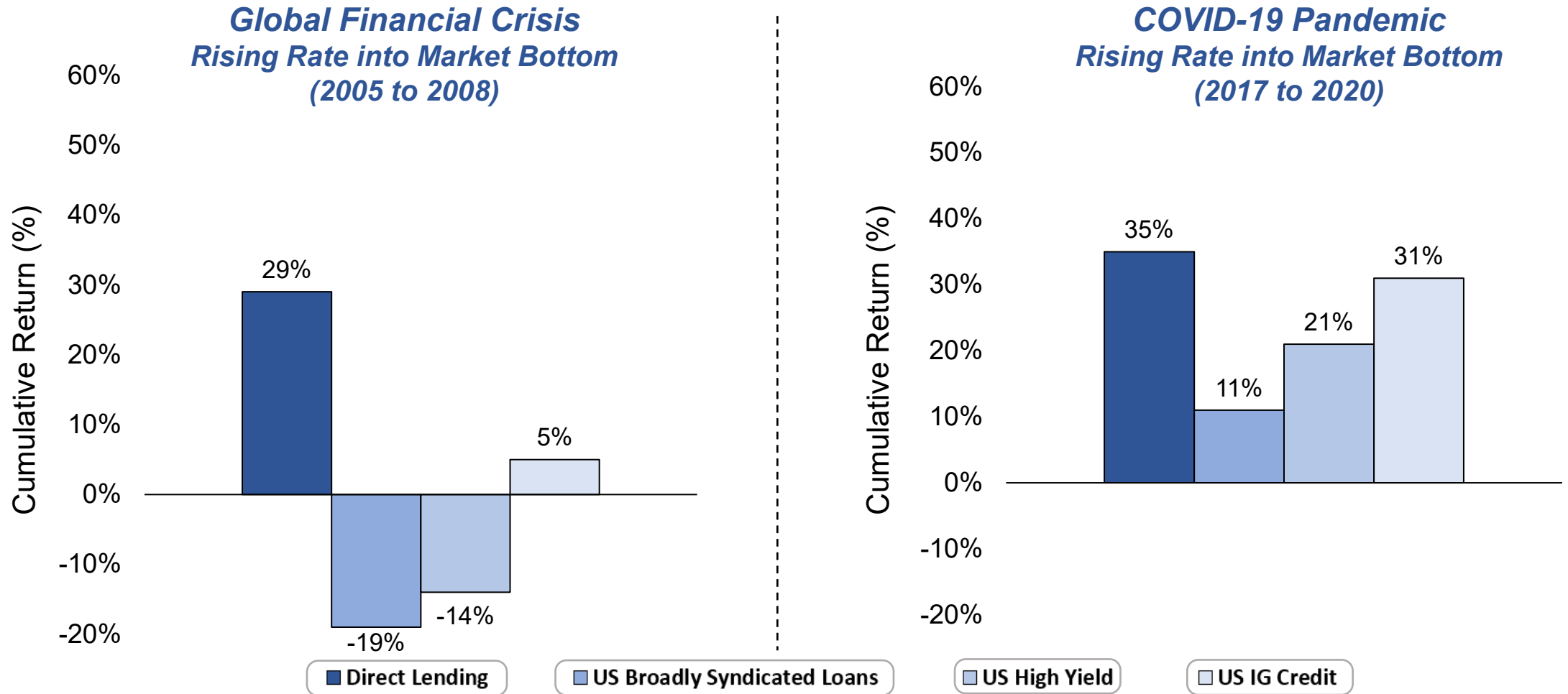
- Private Debt primarily focuses on investing at the top of the capital structure.
- Investing at or near the top of the capital structure reduces risk relative to equity.



Shorter Tenor Compared to Private Equity

	Private Credit	Private Equity
Term of Fund	5 - 8 years ^{(a)(b)}	7 - 10 years ^(c)
Investment Period of Fund	2 - 3 years ^{(a)(b)}	3 - 5 years ^(c)
Est. Holding Period of Investments	~ 2 - 3 years	4 - 6 years ^(d)

Strong Performance Through Economic Cycles



Source: Blue Owl – 2023 *Direct Lending Outlook*. Data as of December 31, 2021. Credit Suisse for US Broadly Syndicated Loans represented by the Credit Suisse Leveraged Loan Index. Bloomberg Barclays Indices for US IG Credit. Cliffwater for Direct Lending represented by the Cliffwater Direct Lending Index (CDLI). ICE, Bank of America for US High Yield represented by the ICE BofA High Yield Index.



I. Program Overview

II. Benefits of Private Debt



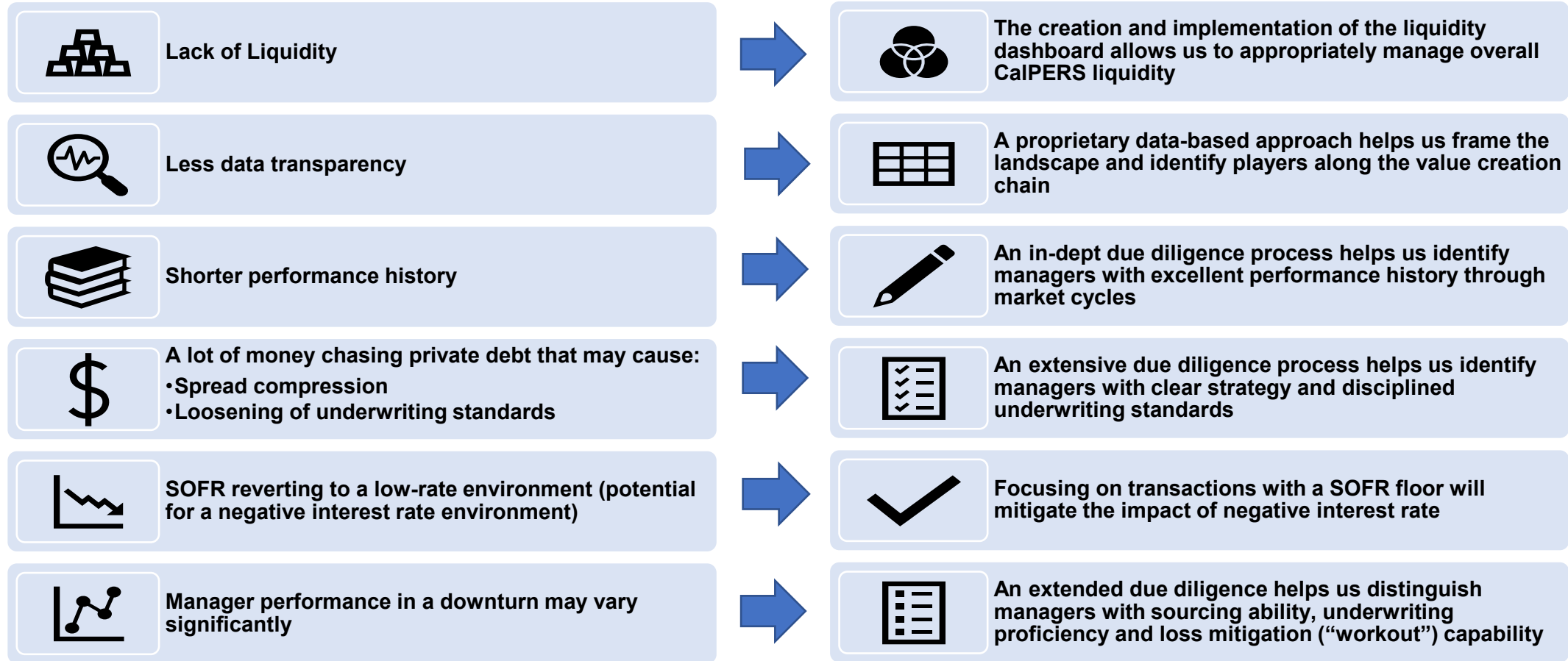
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Potential Risks of Private Debt

How We Invest To Mitigate Risks



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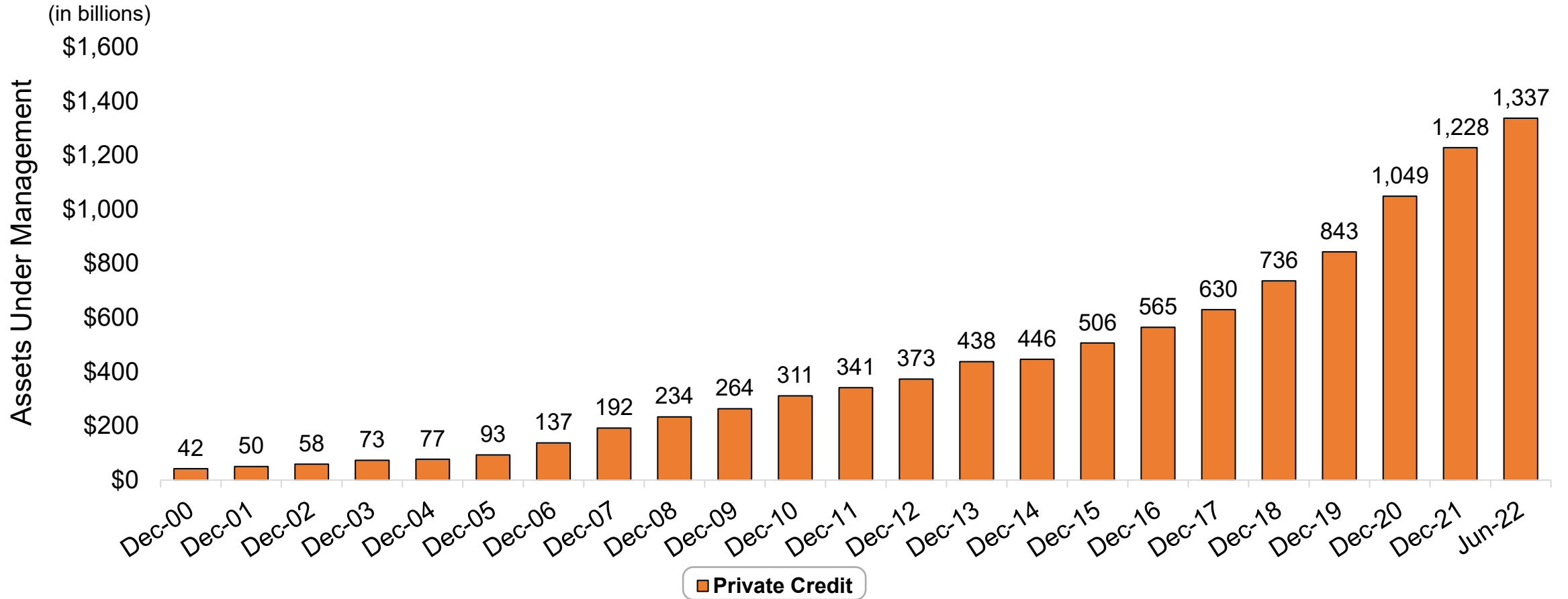


IV. Current Market in Private Credit

V. ESG Considerations

Assets Under Management Has Increased Meaningfully

- The assets under management (AUM) in Private Credit has grown by almost 4x over the past decade.

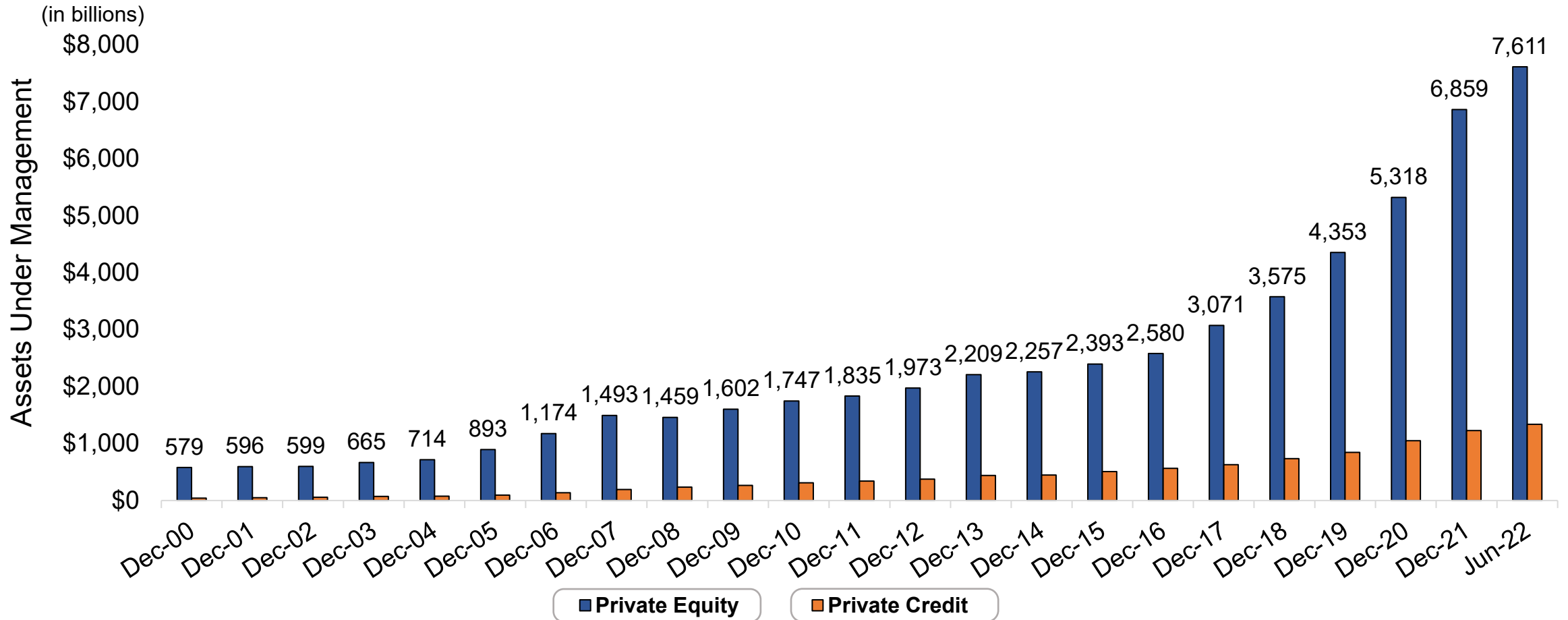


Source: Preqin – “Assets Under Management Breakdown” – as noted by Preqin, to avoid double counting available capital and unrealized value, fund of funds and secondaries are excluded. (Available data as of Jan. 2023).



Assets Under Management Has Increased Meaningfully (cont'd)

- The AUM growth in Private Equity has also been very strong.

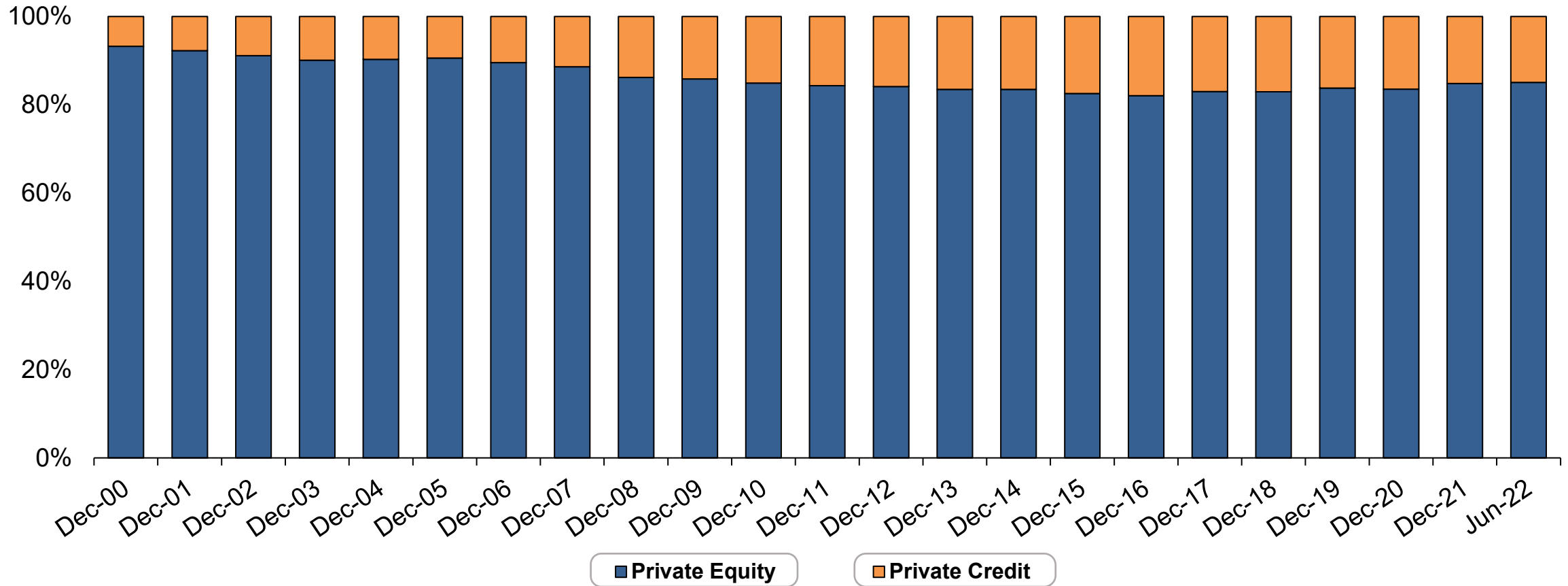


Source: Preqin – “Assets Under Management Breakdown” – as noted by Preqin, to avoid double counting available capital and unrealized value, fund of funds and secondaries are excluded. (Available data as of Jan. 2023).



Assets Under Management Has Increased Meaningfully (cont'd)

- Because the total AUM of both Private Equity and Private Credit exhibited strong growth, the proportion of Private Credit has remained relatively steady for the past decade.

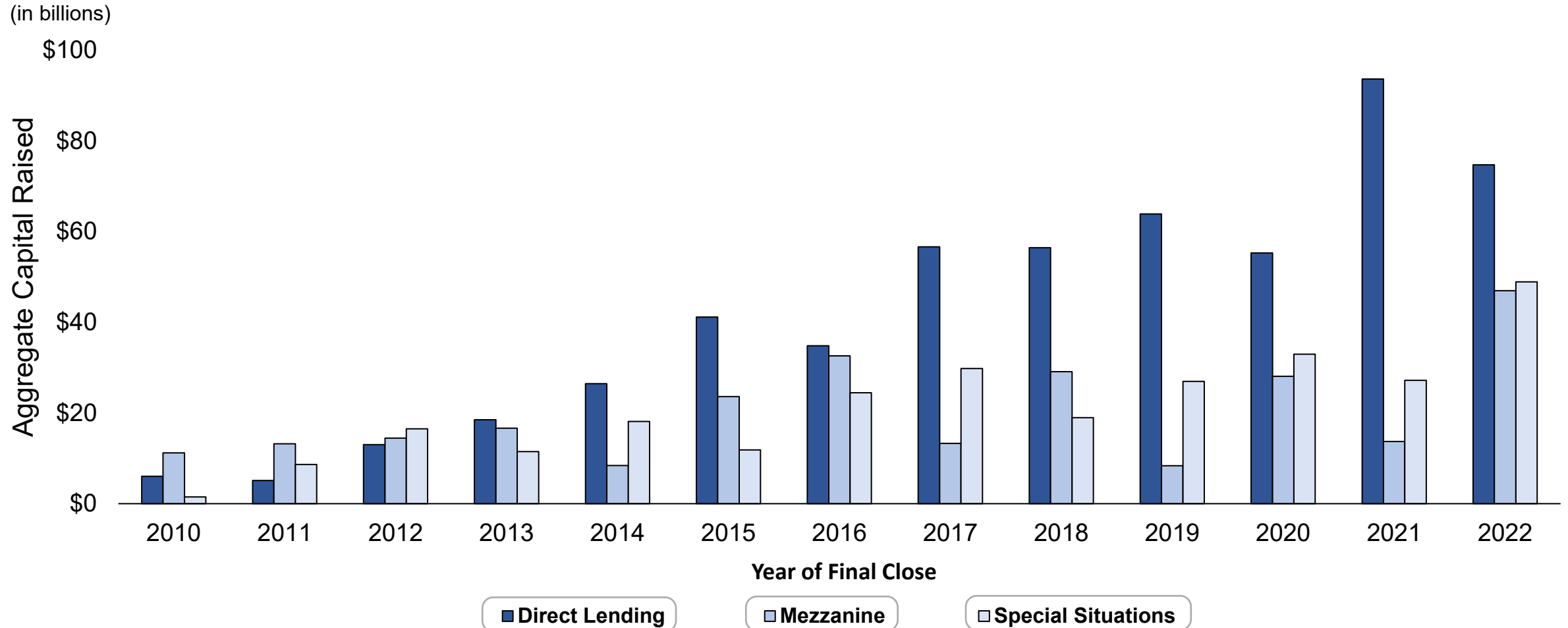


Source: Preqin – “Assets Under Management Breakdown” – as noted by Preqin, to avoid double counting available capital and unrealized value, fund of funds and secondaries are excluded. (Available data as of Jan. 2023).



Fund Raising by Private Credit Strategy

- Within Private Credit, Direct Lending has contributed the most in capital raised.



Source: Preqin. The date represents when the fund officially closed; does not consider when fund raising started. Direct Lending includes Senior Debt and Unitranche Debt. (Available data as of Jan. 2023).



Broadly Syndicated Loans Activity Has Declined Across the Board as of 3Q 2022

New Issuance – Broadly Syndicated Loans Activity			
(\$ billions)	Q3 2022	5-Year Qrtly. Avg.	Historical Comparison
'B' Rated Activity	\$15.8	\$67.5	Lowest since Q3 2011
Refinancing	\$2.6	\$27.5	Lowest since GFC
Dividend Recaps	\$0.0	\$9.9	Lowest since Q1 2016
Sponsored M&A Volume	\$13.1	\$39.9	Lowest since Q1 2012
Sponsored Activity	\$13.6	\$60.2	Lowest since GFC
LBO Activity	\$10.6	\$25.3	Lowest since Q4 2017
M&A Activity	\$16.3	\$54.5	Lowest since Q4 2011
Total	\$21.4	\$96.8	New issuance volumes accounts for ~22% of historical levels

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Integration of Governance & Sustainability

- The Private Debt program is integrating ESG factors into the manager assessment process by:
 - Reviewing how external managers incorporate ESG into their investment decision-making through the Due Diligence Questionnaire and annual review processes.
- Although still in the early stages, Private Debt managers continue to improve on ESG-related engagements.
 - A manager embedded a ratcheting mechanism to lower interest rates as the borrower meets certain criteria, to ensure ongoing ESG engagements.
 - A manager has taken the initiative to have one of their funds to be Article 8^(a) compliant.