

# ATRS Board Policy 6

## REAL ASSETS INVESTMENT POLICIES

A.C.A. § 24-7-305

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### I. Board - Investment Policies and Procedures

#### A. Real Assets Investment Policies

##### 1. Scope

This policy applies to the Real Asset category ("Real Assets") of the Arkansas Teacher Retirement System's ("ATRS") investment portfolio. This policy governs the private market investments and not the public real asset securities exposure within the Total Equity asset class.

##### 2. Purpose and Objectives

The purpose of this statement of investment policy is to formalize the ATRS' Board of Trustees' (the "Board") investment objectives, policies, and procedures, with respect to Real Assets, and to define the duties and responsibilities of the various entities involved in the Real Assets investment process. This statement is to be considered an extension of ATRS' general Statement of Investment Policy.

#### B. Investment Philosophy

##### 1. ATRS allocates a portion of its total assets to Real Assets. ATRS defines Real Assets as investments relating to the ownership, financing, or operation of real estate, timber, agriculture, and infrastructure assets. ATRS allocates capital to Real Assets with the following goals:

###### a. *Diversification with Other Asset Classes*

Real Asset returns have historically performed differently than the returns of other asset classes in which ATRS invests. ATRS believes that Real Asset returns will continue to perform differently than those of other asset classes, allowing ATRS to lower the risk of its overall portfolio through diversification by allocating to the asset class.

###### b. *Potential Inflation Hedge*

Real Asset returns have historically shown the ability to provide a hedge against rising inflation. By allocating a portion of its investments to an asset class with these characteristics the overall risk of rising inflation to the ATRS portfolio is reduced.

#### C. Allocation

1. ATRS controls allocation risk at the total fund level. The allocation establishes a 14% target for the Real Asset class. As provided in ATRS' general Statement of Investment Policy, a range of minimum and maximum relative to the target has not been set as it is not prudent to set rebalancing ranges for the real asset classes due to their illiquid nature. This target allocation is to be reached and maintained over a reasonable period of time using a pacing schedule established by the joint effort of the Executive Director and Real Asset Consultant. There will be no fixed targets for the Real Assets subasset classes but the following general parameters have been identified for the Real Asset subasset classes:

- 7% Real Estate
- 2% Timber
- 1% Agriculture
- 4% Infrastructure

#### D. Performance Benchmark

1. ATRS' Real Asset portfolio is benchmarked on a net of fee basis against the following sub-asset class benchmarks over rolling five year periods.
  - a. Real Estate Benchmark: The net return for ATRS' real estate investments is expected to meet or exceed the net NCREIF Fund Index Open-end Diversified Core Equity Index ("NFI-ODCE") over five year rolling period.
  - b. Timber Benchmark: The net return for ATRS' timber investments is expected to meet or exceed the NCREIF Timberland Property Index ("NTPI") over a five year rolling period.
    - Given the highly concentrated nature of the NTPI, it is advised that an additional performance measurement tool be utilized in order to gauge the timber portfolio's performance compared to the opportunity cost of investing in timber. The Consumer Price Index plus 300 basis points will be used for measurement.
  - c. Agriculture Benchmark: The net return for ATRS' agriculture investments is expected to meet or exceed the NCREIF Farmland Index ("NFI") over a five year rolling period.
    - Much like NTPI, NFI also has a concentrated nature and it is advised that an additional performance measurement tool be utilized in order to gauge the agriculture portfolio's performance compared to the opportunity cost of investing in agriculture. The

Consumer Price Index plus 300 basis points will be used for measurement.

- d. Infrastructure Benchmark: Over the long term (10 years or longer), the infrastructure portfolio is expected to generate a minimum internal rate of return ("IRR") equal to the Consumer Price Index plus 500 basis points, net of all investment management fees and expenses. The Consumer Price Index plus 500 basis points will be used as the benchmark to reflect the opportunity cost of investing in infrastructure.
2. The ATRS Total Real Asset Benchmark is weighted by the allocations based on Net Asset Values across the various sub-categories, and thus defined as Real Estate benchmark, Timber benchmark, Agriculture benchmark, and Infrastructure benchmark. The net of fee return for ATRS' Total Real Asset Portfolio is expected to meet or exceed the Total Real Asset Benchmark over rolling five year periods.

#### E. Portfolio Composition

1. The majority of the Real Asset class investments should consist of equity ownership of privately-held institutional real estate, timber, agriculture, and infrastructure investments.
2. This policy authorizes the use of all types of investment structures including, but not limited to:
  - Separate Accounts
  - Co-investments
  - Joint ventures
  - Open and closed-end funds
  - Partnerships
  - Private and public Real Estate Investment Trusts ("REITs") and Real Estate Operating Companies ("REOCs")
  - Listed or publicly traded infrastructure

#### F. Risk Management

1. For ATRS' Real Asset investments, the following sections identify the most significant risks and the method of control. Compliance with the following risk parameters shall be based on the percentage of ATRS' Real Asset portfolio's Net Asset Value at Fair Value at the end of each quarter.

a. *Investment Manager Diversification*

Investment manager risk consists of two elements: the exposure to an investment manager and the number of investment managers in ATRS' Real Asset portfolio. To control investment manager exposure, the allocation to a single Real Asset manager is typically limited to 30% of ATRS' Real Asset target allocation.

b. *Individual Investment Diversification*

In order to mitigate the risk of large losses, ATRS will diversify its Real Asset investments across many different individual investments. Individual investments, measured by gross asset value, shall generally not exceed 10% of the overall Real Asset target allocation. For Real Estate, the 10% individual investment limitation will apply to Core properties, but Non-Core properties will be generally limited to 5%. Core properties are generally defined as industrial, apartment, retail, and office portfolios that are at least 80% leased, located in major metropolitan areas, and typically use no more than 50% leverage. Non-core is generally defined as the remainder of the Real Estate property opportunity set.

c. *Liquidity*

The majority of Real Assets are illiquid. As such, ATRS understands and recognizes that the Real Asset class will not be structured in a way to provide liquidity. Should market values for the Real Asset class change such that the asset class falls outside of these and the below risk management parameters, the Executive Director and Real Asset Consultant will determine the most effective solution and timeframe to bring the Real Asset exposure into compliance.

2. Additional risk parameters at the subasset class level are defined below and compliance shall be based on the percentage of each subasset class' Net Asset Value at Fair Value at the end of each quarter:

a. Real Estate:

*Property Diversification* - ATRS seeks to minimize the risk of its Real Estate portfolio by allocating its assets across the spectrum of property types, with the majority of its investments allocated to the primary sectors of the NFI-ODCE. No single traditional property type shall account for greater than 50% of the portfolio. In addition, the general range of property type allocations will be 0.5x - 1.5x the NFI-ODCE's weight in each property type. Other property types, as

defined by NFI-ODCE, are allowed but (on a combined basis) should not exceed 20% of the real estate portfolio.

*Geographic Diversification* - The Plan seeks to minimize the risk of its real estate portfolio by allocating its investments across the geographic spectrum. Within the United States, the general range of geographic allocations will be 0.5x - 1.5x the NFI-ODCE weight in each region. With respect to non-U.S. investing, no more than 40% of the portfolio may be invested outside of the U.S. ATRS may initiate Arkansas-related mortgage loans and direct Real Estate investments to meet the goal of investing in quality Arkansas related investments. The Executive Director and Real Estate Consultant will monitor the Arkansas-related Real Estate holdings to protect against excessive risk due to sector or geographic exposure. The goal of Arkansas-related investments shall be to achieve a total rate of return, net of all fees and costs that will exceed the real estate performance benchmark over time.

*Leverage* - ATRS allows some of its investment managers the ability to use modest amounts of leverage in their investment strategy as a means of enhancing the overall risk-adjusted returns available to ATRS. In keeping with its goal of risk mitigation, leverage at the total asset class level should be kept below a 50% loan-to-value ratio.

*Life Cycle* - ATRS will endeavor to invest the majority of its assets in fully established, income-producing Real Estate, commonly referred to as Core Real Estate. As defined above, the ATRS goal will be to have between 50% and 70% of its Real Estate asset class in Core investments. Non-Core opportunities, such as Value Added and Opportunistic real estate strategies, may provide better alpha generation but will be viewed tactically and have an operating allocation range of 30% to 50% of the real estate portfolio.

b. Timber:

*Geographic Diversification* - The Plan seeks to minimize the risk of its timber portfolio by allocating its investments across the geographic spectrum. Within the United States, the allowable range of geographic allocations will fall within the following target ranges as defined by the NCREIF timberland index.

<u>Region</u>	<u>Range</u>
South	40% to 80%
Northwest	0% to 50%
Northeast	0% to 20%

<u>Lake States</u>	<u>0% to 20%</u>
<u>Other</u>	<u>0% to 20%</u>

c. Agriculture:

*Crop Diversification* - The majority of the portfolio will be comprised of existing crop properties. With the exception of the portfolio creation stage, no crop shall comprise in excess of 40% of the agriculture portfolio.

*Geographic Diversification* - Investments will be primarily located within the continental United States. Properties located within the state of Arkansas are preferred within a prudent range of exposure for the total portfolio. It is desired that the investments will have attractive locations with good market access. No region, as defined by the NCREIF Farm Index regional definitions, will comprise more than 40% of the agriculture portfolio.

*Leverage* - In keeping with its goal of risk mitigation, leverage at the total asset class level should be kept below a 20% loan-to-value ratio.

d. Infrastructure: ATRS will use diversification of its infrastructure portfolio as a risk mitigation tactic. Relevant risk factors considered are strategy, manager, firm, vintage year, asset type, geographic and liquidity issues. However, initial allocations during early implementation may result in temporary variances.

*Strategy* - The portfolio should be appropriately diversified across infrastructure asset classes and vehicles due to various risk/return characteristics.

*Manager* - Manager risk consists of two elements, the exposure within an investment vehicle, and the number of managers (general partners) in a given infrastructure fund. The exposure to a specific manager within an investment vehicle is controlled by limiting its commitment size. The cohesion of the general partners and the vesting rights to interest carry are important elements of insuring a successfully performing general partnership as are the past success of the business model employed and the length of time the team has remained stable.

*Vintage* - Vintage reflects the year of first capital draw and vintage risk refers to the variability of infrastructure commitments over time. Commitments to partnership investments will be staged over time such that the infrastructure portfolio invests over business cycles and insulates the portfolio from event risk.

*Asset Type* - Typically, infrastructure partnerships are permitted to invest in assets in a wide variety of industries (Transportation, Energy/Utility and Other) with limited controls. Risk from investing in assets with different return characteristics is controlled primarily through appropriate diversification across business sectors and sub-sectors. No infrastructure asset class shall account for more than 70% of the portfolio.

*Geographic* - Over the long-term, the infrastructure portfolio should seek diversification with regard to major regional areas both domestically and internationally. The infrastructure portfolio will accept the currency risks consistent with the geographic constraints. Infrastructure partnerships generally do not hedge currency risk, though with increasing globalization, one can see this practice increasing. With respect to U.S. investing, the portfolio should generally target at least 40%.

#### G. Distinction of Responsibilities

1. The Board, as Trustees, is responsible for approving the Real Asset Statement of Investment Policy.
2. ATRS' Board of Trustees is responsible for selecting the investment managers used to implement the Real Asset Statement of Investment Policy.
3. ATRS' Investment Staff and the Real Asset Consultant are jointly responsible for recommending the Investment Managers to the Board, as well as managing the Real Asset class, as described by the Real Asset Statement of Investment Policy, on an on-going basis, including monitoring the investment managers.
4. The Real Asset Consultant will assist ATRS' Investment Staff in recommending investment managers to the Board, monitoring investment managers, presenting Real Asset class performance to the Board, and will assist Investment Staff in developing and recommending the Real Asset Statement of Investment Policy and any changes to this document.
5. Investment Managers are utilized by ATRS to implement the specific investment strategies selected by ATRS.

#### H. Reporting and Monitoring

1. The Investment Staff and the Real Asset Consultant will monitor performance on a quarterly basis, providing a quarterly report to the Board. The report will provide a comprehensive review of the Real Asset portfolio in a form approved by ATRS' Investment Staff and the Real Asset Consultant.

## **HISTORY**

Adopted October 7, 2013

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Amended December 2, 2024

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