



Legislative Fiscal Bureau

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November 12, 2014

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Investment Board: Annual Budget, Position, and Performance Report to the Joint Committee on Finance

Under s. 25.17(13r) of the statutes, the Executive Director of the State of Wisconsin Investment Board (SWIB), or his or her designee, is required to appear at the first quarterly meeting of the Joint Committee on Finance under s. 13.10 of the statutes in each fiscal year to provide an update of SWIB's budget changes, position authorization changes, assessment of the funds under management, and performance of the funds under management for the current and next fiscal year. Attached is SWIB's submission to the Committee to satisfy this requirement.

The reason for this report relates to 2011 Act 32 provisions that modified SWIB's authority with respect to the Board's budget and position levels.

Under prior law, the agency's budget for a fiscal year could not exceed the greater of: (a) the amount that the Board could have assessed the trust funds in the second year of the prior fiscal biennium; or (b) 0.0325% of the average market value of the assets of the funds at the end of each month between November 30 and April 30 of the preceding fiscal year. This prior law mechanism for establishing SWIB's operating budget (s. 25.187(2)(c) of the statutes) was repealed in Act 32. In addition, under prior law, changes in the authorized position level for the Board needed to be approved by the Legislature, or by the Committee under s. 16.505 of the statutes.

Under 2011 Act 32, the Investment Board was authorized to establish SWIB's operating budget each year and monitor the fiscal management of the budget. Further, SWIB's Executive Director was authorized to create or abolish staff positions. Under the Act 32 provisions, SWIB's budget was established at \$30 million in 2011-12 (with actual expenditures of \$28.7 million) and \$35.3 million in 2012-13 (with actual expenditures of \$34.2 million). Utilizing its Act 32 authority, the Board approved a budget for SWIB of \$44.6 million in 2013-14 (with actual expenditures of \$41.4 million), and in June, 2014, the Board approved an operating budget for 2014-15 of \$46.9 million.

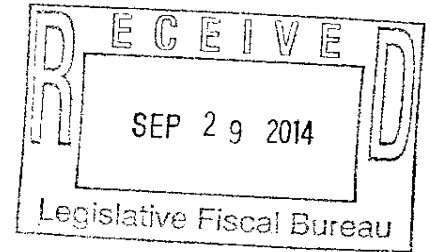
By statute, some of the Board's administrative expenses are not included in the budgeted appropriations for the agency. These types of expenditures include custodial and banking fees, legal fees, investment research and consulting fees and external management fees. For calendar year 2013, these expenditures amounted to approximately \$316.3 million.

Position authority for the agency totaled: (a) 131.75 full-time equivalent (FTE) positions in 2011-12; (b) 145.1 FTE in 2012-13; and (c) 148.1 FTE in 2013-14. During the quarter ending June 30, 2014, the Board approved 159.1 FTE positions and 7.25 temporary project positions for SWIB for 2014-15.

In addition to the required annual report now before the Committee, 2011 Act 32 also requires that SWIB provide quarterly reports to the Department of Administration, the Co-Chairpersons of the Joint Committee on Finance and the Co-Chairpersons of the Joint Committee on Audit, identifying: (a) all operating expenditures and the number of FTE positions created or abolished during that quarter; and (b) all costs and expenses charged to funds during that calendar quarter, including a breakdown of the amount and percentage of assets managed under each type of dedicated and commingled account or partnership, and the change in the amount and percentage from the prior calendar quarter.

The intent of the 2011 Act 32 quarterly reporting requirement is to assure that the executive branch and the Legislature are kept apprised of the status of SWIB's determinations of budget and position authority, given the Board's authority to make these determinations under the Act 32 provisions. The annual appearance of SWIB officials before the Committee also serves this function and, in addition, provides Committee members with the opportunity to ask questions or request additional information from SWIB.

Prepared by: Paul Onsager
Attachment



September 29, 2014

Senator Alberta Darling, Co-Chair
Joint Committee on Finance
P.O. Box 7882
Madison WI 53707-7882

Representative John Nygren, Co-Chair
Joint Committee on Finance
P.O. Box 8953
Madison WI 53708-8953

Dear Senator Darling and Representative Nygren:

Wisconsin Statutes Section 25:17 (13r) requires SWIB's Executive Director to appear before the Joint Committee on Finance each year at a quarterly meeting under s.13.10 to provide an update on SWIB's operating budget changes, position authorization changes, assessment of the funds under management, and performance of the funds under management.

This reporting requirement was imposed together with other provisions of 2011 Wisconsin Act 32 that provided SWIB's Board of Trustees additional flexibility to establish SWIB's operating budget and to approve staff positions.

I have attached copies of slides that I will discuss at the next scheduled s.13.10 meeting. I am submitting them so they can be distributed with other committee materials for this meeting.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael Williamson".

Michael Williamson
Executive Director

Attachments

cc: Bob Lang, Legislative Fiscal Bureau
Dan Subach, DOA Division of Executive Budget and Finance
Joe Malkasian, Committee Clerk, Joint Committee on Finance



State of Wisconsin Investment Board

Annual Update on Investment Operations
Joint Committee on Finance

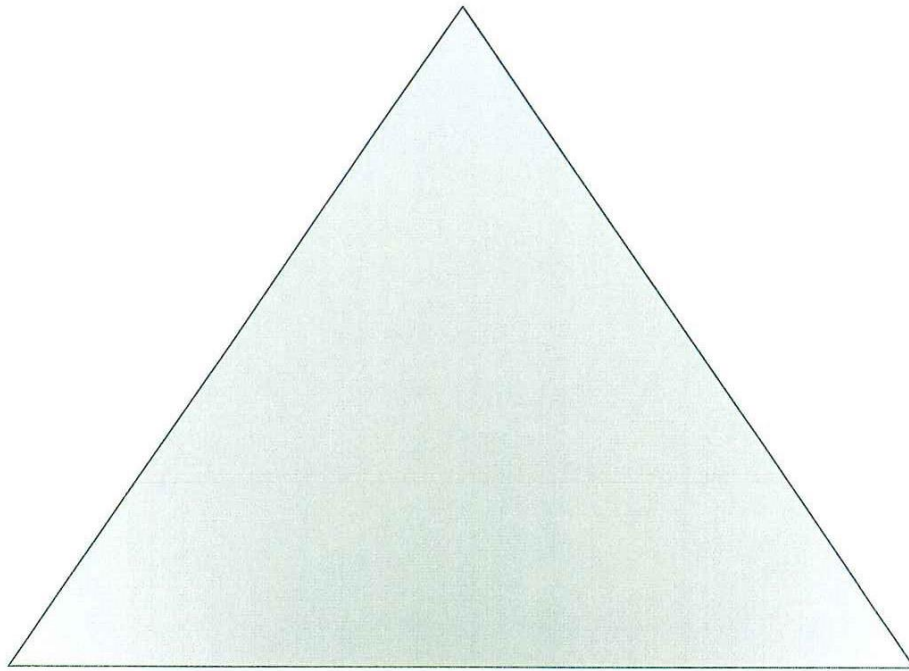
Michael Williamson
Executive Director
September 2014





SWIB's Job

Make Money



Manage Risk

Control Cost



How SWIB's Performance Compares

- **Independent* review:** Core Fund return above peer median for five-year period adjusted for risk
 - Core Fund has less (investment) risk for returns earned relative to peers
- **Performance Benchmark:** Core Fund above one-, three-, five- and ten-year benchmarks ending 12/31/2013

*Callan Associates Inc. report based on Core Fund cumulative performance during five-year period ending June 30, 2014.

Core Fund Investment Performance

	1 – Year Thru 7/31/14	3 – Year Thru 7/31/14	5 - Year Thru 7/31/14	10 – Year Thru 7/31/14
Core Trust Fund	12.5%	9.3%	11.4%	7.9%
Core Trust Fund Benchmark	12.2%	8.9%	10.7%	7.6%
Russell 3000 (U.S. stocks)	16.4%	16.6%	17.1%	8.4%
Barclays Capital Gov't/Credit (U.S. bonds)	3.9%	3.4%	4.7%	4.8%

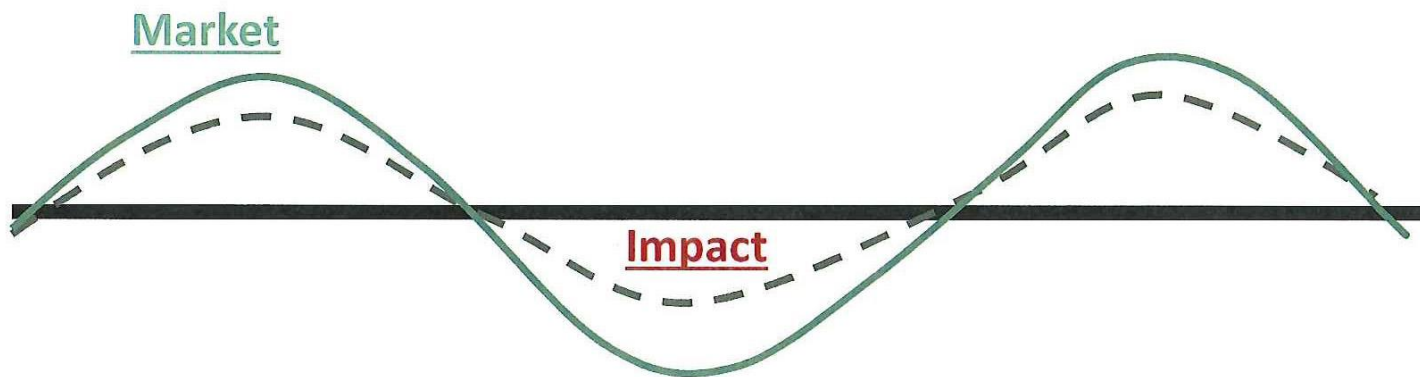


Managing Risk

- Limit fluctuations in market returns year-over-year
 - Contribution rates
 - Benefit adjustments
- Implement new strategies slowly and incrementally
- Protect against inflation
- Positive returns for the Core Fund over the past five years
 - 22.4% in 2009
 - 12.4% in 2010
 - 1.4% in 2011
 - 13.7% in 2012
 - 13.6% in 2013

Reducing Fund Volatility

The goal is to stabilize the effects of returns on the WRS



Slight reduction in performance in times of strong stock markets

Better protection against worst outcomes



How Costs Compare with Peers*

- Independent review: SWIB is low-cost fund compared to other large U.S. public pension funds
 - SWIB's cost of 38¢ per \$100 versus peer median of 59¢ per \$100 under management
 - SWIB has a lower allocation to higher cost assets
 - Applying peer median costs to SWIB's asset allocation would result in an increase of \$79.3 million annually
 - Due to greater use of internal and passive management
 - SWIB pays less for external management it does use
- Over the long term, low-cost pension funds realize greater net returns over investment benchmarks

*Core Fund cost benchmarking results for period ending December 31, 2013.

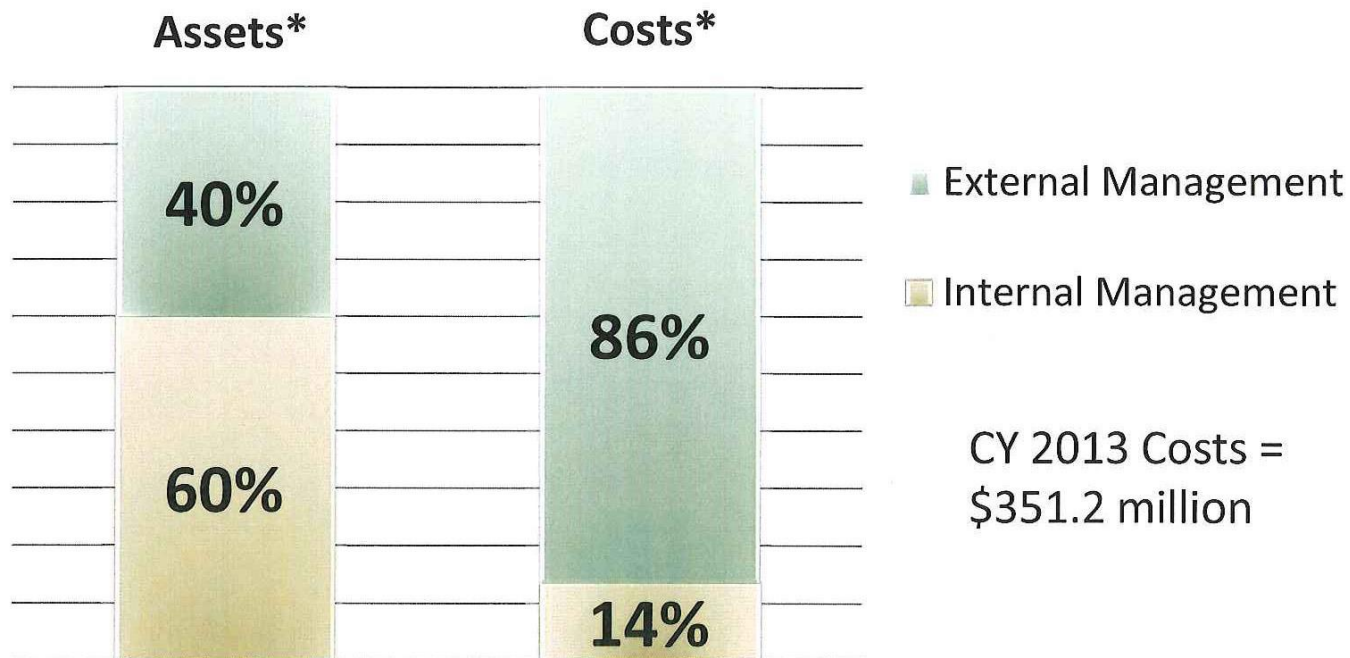
Budget & Staffing

	7/1/2012 FY13	7/1/2013 FY14	7/1/2014 FY15
Internal Asset Management (WRS)	54.2%	56.1%	57.9%
External Asset Management (WRS)	45.8%	43.9%	42.1%
SWIB Staff – FTE	145.10	148.10	159.10
Temporary Project Staff	-	-	7.25
Total Staff - FTE	145.10	148.10	166.35
Budget/Internal Operating Expenses Assessed * (in millions)	\$35.3	\$44.6	\$46.9

*Budget amount is assessed to the funds. Actual amount spent is determined at fiscal year end.
Unspent funds are credited back to the funds during the next billing.

Internal and External Assets & Costs

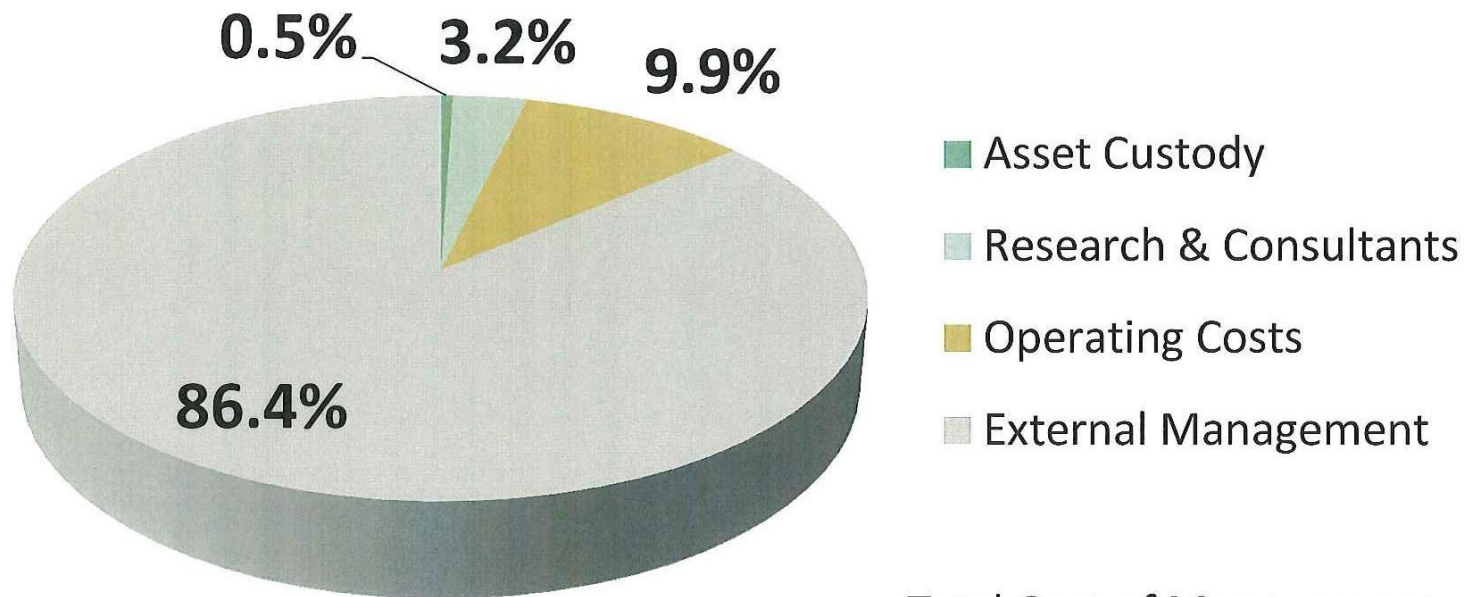
Calendar Year 2013



Cost to externally manage 40% of assets represents 86% of SWIB's total costs. Internal management is less expensive.

* Includes WRS, State Investment Fund & other trust funds

All Funds - Total Cost of Management Calendar Year 2013



Total Cost of Management
for All Trust Funds in CY
2013 = \$351.2 million



Managing Compensation

- Based on performance
- Represents small percentage of earnings over benchmark
- Focused primarily on five-year results
- Compensation consultant advises Trustees
- Compensation benchmarked to banks, insurance companies and in-house managed pension funds (excludes East and West coast financial centers)



Practical Effects

- Added 55 jobs in Wisconsin & significantly reduced assets managed out-of-state since 2007
- WRS assets managed internally increased significantly since shift began
 - 21% in 2007
 - 58% in 2014
- Internal public market asset management saves \$57 million annually
- Economic impact of state and local pensions on Wisconsin in 2012 was \$6.6 billion*

* National Institute on Retirement Security 2014 Pensionomics