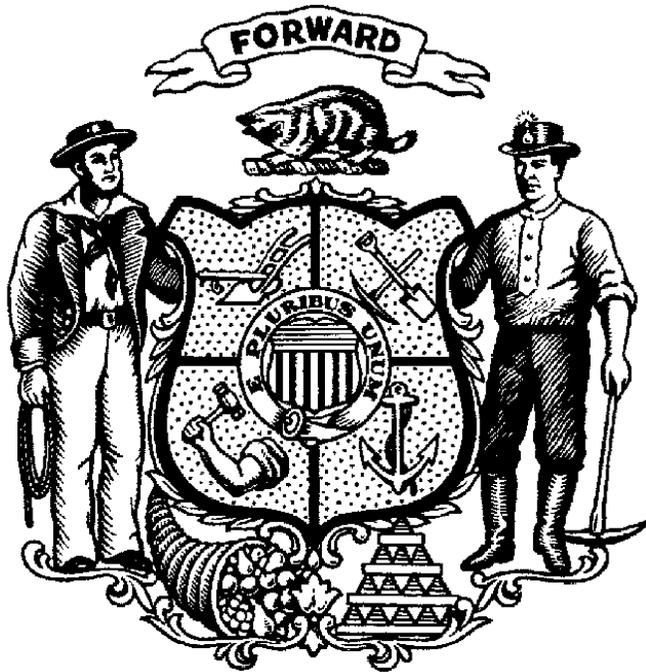


State of Wisconsin

Investment Board



Agency Budget Request

2017 – 2019 Biennium

September 15, 2016

Table of Contents

Cover Letter	3
Description.....	5
Mission.....	6
Goals	7
Performance Measures.....	8
Organization Chart.....	11
Act 201	11
Agency Total by Fund Source.....	12
Agency Total by Program.....	13
Agency Total by Decision Item (DIN)	14
Decision Items.....	15

Date: September 15, 2016

To: Scott Neitzel, Secretary
Michael Heifetz, State Budget Director
Department of Administration

Robert Lang, Director
Legislative Fiscal Bureau

From: Michael Williamson, Executive Director
Investment Board

Re: **2017-19 Biennial Budget Request**

Attached is SWIB's budget submission for the 2017-19 biennium. Our budget is funded entirely by charges to the funds under management (program revenue) and we seek no increase in budget authority or staff positions as part of the biennial budget request. Under Wis. Stats. 25.187(2)(b), the Board of Trustees may establish the operating budget each fiscal year and monitor the fiscal management of the operating budget. The annual operating budget is developed to provide the necessary resources to manage trust fund assets and for the Board to fulfill its fiduciary duty to manage the assets in the best interest of the beneficiaries.

Performance Goals and Achievements

Despite the current low return environment that exists, SWIB has surpassed most of the performance goals established in our 2015-17 biennial budget request. As can be seen in the attached Performance Measures, SWIB has exceeded investment benchmarks after costs for the five-, and ten-year periods ending June 30, 2016, for the Core funds and the five-year for the Variable funds that make up the Wisconsin Retirement System (WRS). The WRS funds represent 92% of assets managed by SWIB or \$94.3 billion as of June 30, 2016, and total assets under management exceed \$102.1 billion. On average, investment returns account for nearly 75% of the income of the WRS. SWIB's strong investment returns are one reason the WRS is, according to the Pew Center on States, one of the best funded public pension plans in the country.

SWIB's goals for the next biennium include continuing to realize external asset manager fee savings by using less expensive internal management where appropriate and to further reduce volatility of assets under management by implementing new, diversified investment strategies.

Budget Flexibility Leads to Net Cost Savings

With the support of the Governor and the Legislature, SWIB has used the budget flexibility granted by the Legislature to build a strong internal investment management program that is providing a significant financial benefit to the WRS. Since SWIB began an initiative to manage more money internally, internal management of WRS assets has increased from 21% in 2007 to nearly 64% in 2016, and SWIB manages nearly 65% of all trust fund assets internally. Net cost savings resulting from internal management are significant. If internally managed public market assets in the WRS were managed by out-of-state external money managers, it would cost approximately \$51 million more annually.

Investment Strategies and Managing Risk

SWIB's asset allocation and investment decisions are based on selecting the best opportunities to meet the long-term investment objectives of the WRS and the other trust funds under management while taking an appropriate level of risk. Having a long-term view of performance and the investment markets is crucial especially when markets become volatile as has been the case over the last decade or more. As a result, SWIB is continuing to explore and implement new investment strategies to help stabilize investment returns and, in turn, contribution rates for active employees and pension adjustments for retirees. Asset allocation and investment diversification are essential components of SWIB's long-term investment strategy.

Investment in Wisconsin Businesses

When economically appropriate, SWIB continues to invest in Wisconsin businesses ranging from small, family-owned companies to billion-dollar manufacturers with worldwide sales. For the fiscal year ending June 30, 2015, SWIB held assets of over \$809.4 million in companies headquartered in Wisconsin or with significant operations in the state. SWIB has also invested in venture capital funds designed to identify and invest in promising young technology businesses in Wisconsin and the region.

SWIB will continue to be diligent in our efforts to keep the WRS system stable and well-funded.

We look forward to working with your staff as the budget progresses. If you have any questions please contact Lori Wersal at 266-2042.

AGENCY DESCRIPTION

As of June 30, 2016, the Board managed approximately \$102.1 billion in assets. The trust funds of the Wisconsin Retirement System (WRS) comprise nearly 92 percent of the funds under management. With assets over \$94.3 billion, the Wisconsin Retirement System is currently the 9th largest public pension fund in the United States and the 24th largest public or private pension fund in the world.

The Board also manages the State Investment Fund which invests the cash balances of state agencies, over 1,300 local governments and the WRS on a commingled basis. Funds are managed to protect principal, provide liquidity and enhance returns. In addition, the Board manages several smaller trust funds. Each has investment objectives to fulfill specific financial needs.

The Board is comprised of nine trustees, selected as follows:

- Five public members appointed by the Governor with the advice and consent of the Senate, to staggered six-year terms. Four of these five members must possess at least ten years of investment experience.
- One member representing a local government that participates in the Local Government Investment Pool. This member is appointed by the Governor with the advice and consent of the Senate to a six-year term and must meet prescribed statutory eligibility criteria.
- Two members must be WRS participants. One member is appointed by the Teachers Retirement Board from among WRS teacher participants and the other is appointed by the Wisconsin Retirement Board from among WRS non-teacher participants, for six-year terms.
- One member is the secretary of the Department of Administration, or his or her designee.

MISSION

To be a trusted and skilled global investment organization contributing to strong financial futures for the beneficiaries of the funds entrusted to us.

PROGRAMS, GOALS, OBJECTIVES AND ACTIVITIES

Program 1: Investment of Funds

Goal: Earn the best rate of investment return, with an appropriate level of risk, for each fund managed.

Objective/Activity: The Board strives to exceed measurable investment goals for each fund. The investment objective for the Wisconsin Retirement System trust funds is to achieve a long-term rate of return that will help the system meet pension obligations to current and future beneficiaries. Successful investment performance reduces the amount that taxpayers contribute to the funding of system benefits and provides for increases in pension benefits. The investment objective for the State Investment Fund is to exceed its established performance benchmark while ensuring the safety of principal and liquidity. The investment objective for the small funds is to meet annual fund cash flow requirements, as established by their governing boards.

PERFORMANCE MEASURES

FY 2015 and FY 2016 Goals and Actuals

Prog. No.	Performance Measure	Goal FY 2015	Actual FY 2015	Goal FY 2016	Actual FY 2016
1.	Investment returns for the Core and Variable Retirement Funds exceed market index returns for the asset classes in which the funds are invested on a net basis.	Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis	<u>Core:</u> 1 Year: Yes 5 Year: Yes 10 Year: Yes <u>Variable:</u> 1 Year: No 5 Year: Yes 10 Year: Yes	Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis	<u>Core:</u> 1 Year: No 5 Year: Yes 10 Year: Yes <u>Variable:</u> 1 Year: No 5 Year: Yes 10 Year: No
1.	Long-term investment returns for the Core Retirement Fund meet or exceed the rate of return assumed by Wisconsin Retirement System actuary.	Return averages at least 7.2% annually over the long term ¹ (ten years)	Did not meet goal. Ten-year net return was 6.4%.	Return averages at least 7.2% annually over the long term ¹ (ten years)	Did not meet goal. Ten-year net return was 5.5%
1.	Total costs to manage the Core Retirement Fund are reasonable when compared to peer funds with a similar asset mix and size. ²	Total costs are at or below the normal cost paid by our peers to manage a similar asset mix	Met goal. CY 2013 cost was 37.6 basis points (37.6 cents per \$100 managed) compared to typical costs of 47.1 basis points. ²	Total costs are at or below the normal cost paid by our peers to manage a similar asset mix	Met goal. CY 2014 cost was 40.1 basis points (40.1 cents per \$100 managed) compared to typical costs of 47.2 basis points. ²
1.	Core Retirement Fund net investment returns are in the top half of its peer group. ^{3,4}	Core Fund's five-year investment return exceeds the peer group median on an absolute and risk adjusted basis	Did not meet return goal on an absolute basis, but met on a risk adjusted basis. Five-year in top 79% and ten-year in top 52% of peer group as of December 31, 2014. ³	Core Fund's five-year investment return exceeds the peer group median on an absolute and risk adjusted basis	Did not meet return goal on an absolute basis, but met on a risk adjusted basis. Five-year in top 81% and ten-year in top 60% of peer group as of December 31, 2015. ³

Prog. No.	Performance Measure	Goal FY 2015	Actual FY 2015	Goal FY 2016	Actual FY 2016
			Five-year risk adjusted return in the top 28% of peer group as of December 31, 2014. ⁴		Five-year risk adjusted return in the top 41% of peer group as of December 31, 2015. ⁴
1.	State Investment Fund returns exceed investment performance benchmarks.	Exceed Benchmark	Exceeded one-, five-, and ten-year investment benchmarks.	Exceed Benchmark	Exceeded one-, five-, and ten-year investment benchmarks.
1.	State Investment Fund returns exceed the median of comparable money market mutual funds. ⁵	Above the median	Exceeded goal. SIF return ranked first out of 163 government funds and 9 th compared to 972 taxable funds as of June 30, 2015.	Above the median	Exceeded goal. SIF return ranked first out of 213 government funds and 28 th compared to 832 taxable funds as of June 30, 2016.
1.	Meet annual fund cash flow requirements as established by the governing boards for the State Historical Society Trust Fund, the Injured Patients and Families Compensation Fund, the State Life Insurance Fund, the Local Government Property Insurance Fund and the EdVest Tuition Trust Fund.	Meet the cash flow needs of the funds	Met goal.	Meet the cash flow needs of the funds	Met goal.

Note: Based on fiscal year, except where noted.

¹As assumed by the actuary.

²As reported by CEM Benchmarking, Inc.

³Trust Universe Comparison Service data for public funds with over \$10 billion in assets (not risk adjusted).

⁴Peer group with over \$10 billion in assets compiled by Callan Associates, Inc. (risk adjusted)

⁵As measured by the iMoneyNet Government Index and All Taxable Money Market Index.

FY 2015, FY 2016 and FY 2017 Goals

Prog. No.	Performance Measure	Goal FY 2017	Goal FY 2018	Goal FY 2019
1.	Investment returns for the Core and Variable Retirement Funds exceed market index returns for the asset classes in which the funds are invested on a net basis.	Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis	Same	Same
1.	Long-term investment returns for the Core Retirement Fund meet or exceed the rate of return assumed by Wisconsin Retirement System actuary.	Net return averages at least 7.2% annually over the long term ¹ (ten years)	Same	Same
1.	Total costs to manage the Core Retirement Fund are reasonable when compared to peer funds with a similar asset mix and size. ²	Total costs are at or below the normal cost paid by our peers to manage a similar asset mix	Same	Same
1.	Core Retirement Fund investment returns are in the top half of its peer group. ³	Core Fund's five-year investment return exceeds the peer group median on a risk adjusted basis	Same	Same
1.	State Investment Fund returns exceed investment performance benchmarks.	Exceed Benchmark	Same	Same
1.	State Investment Fund returns exceed the median of comparable money market mutual funds. ⁴	Above the median	Same	Same
1.	Meet annual fund cash flow requirements as established by the governing boards for the State Historical Society Trust Fund, the Injured Patients and Families Compensation Fund, the State Life Insurance Fund, the Local Government Property Insurance Fund and the EdVest Tuition Trust Fund.	Meet the cash flow needs of the funds	Same	Same

Note: Based on fiscal year, except where noted.

¹ As assumed by the actuary.

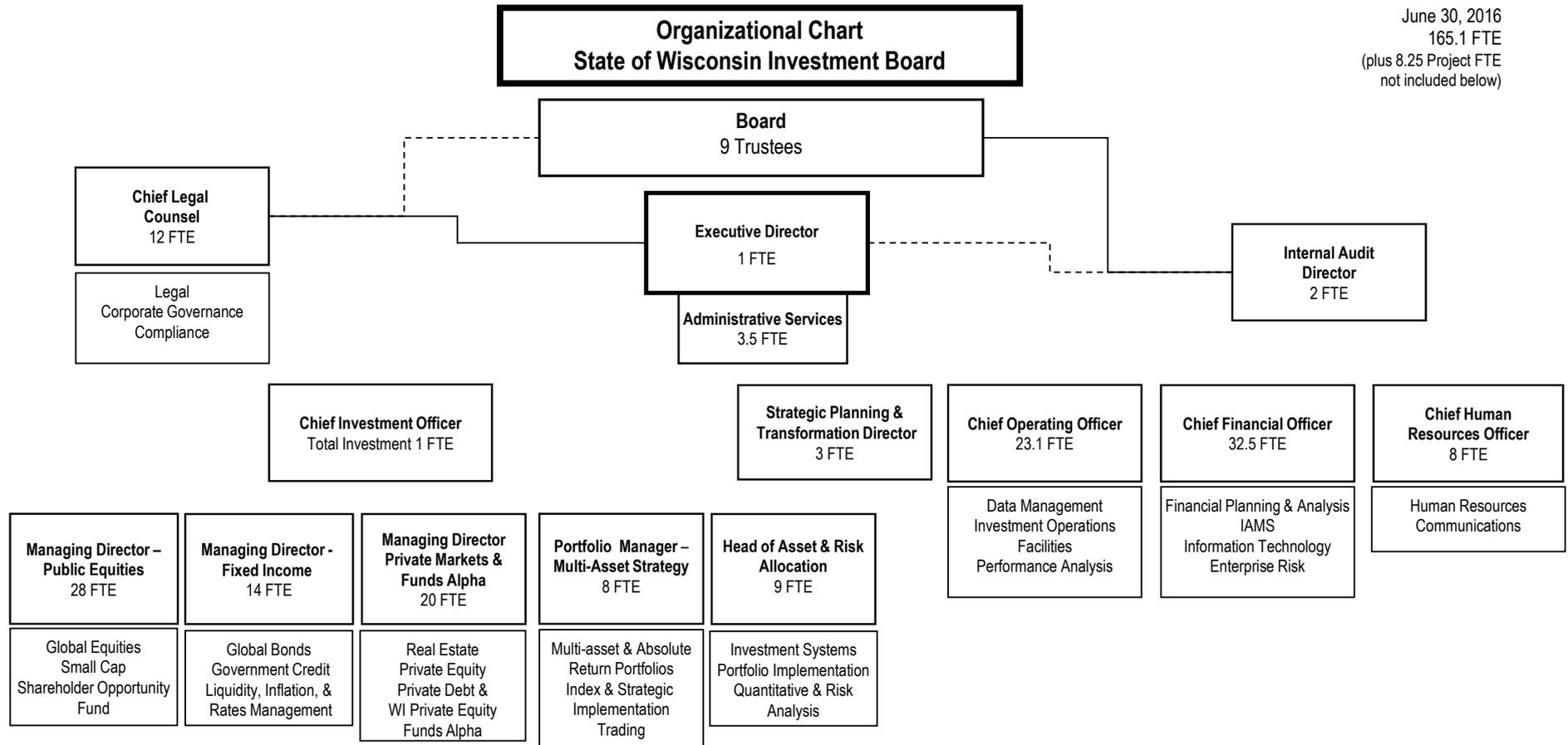
² As reported by CEM Benchmarking, Inc.

³ Peer group with over \$10 billion in assets compiled by Callan Associates, Inc. (risk adjusted)

⁴ As measured by the iMoneyNet Government Index and All Taxable Money Market Index.

**Organizational Chart
State of Wisconsin Investment Board**

June 30, 2016
165.1 FTE
(plus 8.25 Project FTE
not included below)



Agency Total by Fund Source

Investment Board

1719 Biennial Budget

		ANNUAL SUMMARY						BIENNIAL SUMMARY			
Source of Funds		Prior Year Total	Adjusted Base	1st Year Total	2nd Year Total	1st Year FTE	2nd Year FTE	Base Year Doubled (BYD)	Biennial Request	Change From (BYD)	Change From BYD %
PR	S	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.0%
Total		\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.0%
Grand Total		\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.0%

Agency Total by Program

536 Investment Board

1719 Biennial Budget

Source of Funds	ANNUAL SUMMARY						BIENNIAL SUMMARY			
	Prior Year Actual	Adjusted Base	1st Year Total	2nd Year Total	1st Year FTE	2nd Year FTE	Base Year Doubled (BYD)	Biennial Request	Change From (BYD)	Change From BYD %
01 INVESTMENT OF FUNDS										
Non Federal										
PR	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
S	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
Total - Non Federal	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
S	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
PGM 01 Total	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
PR	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
S	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
TOTAL 01	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
S	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%
Agency Total	\$42,797,360	\$53,499,600	\$53,499,600	\$53,499,600	173.35	173.35	\$106,999,200	\$106,999,200	\$0	0.00%

Agency Total by Decision Item

Investment Board

1719 Biennial Budget

Decision Item	1st Year Total	2nd Year Total	1st Year FTE	2nd Year FTE
2000 Adjusted Base Funding Level	\$53,499,600	\$53,499,600	173.35	173.35
TOTAL	\$53,499,600	\$53,499,600	173.35	173.35

Decision Item (DIN) - 2000

Decision Item (DIN) Title - Adjusted Base Funding Level

NARRATIVE

Adjusted Base Funding Level

Decision Item by Line

1719 Biennial Budget

	CODES	TITLES
DEPARTMENT	536	Investment Board
	CODES	TITLES
DECISION ITEM	2000	Adjusted Base Funding Level

Expenditure items		1st Year Cost	2nd Year Cost
01	Permanent Position Salaries	\$38,488,700	\$38,488,700
02	Turnover	\$0	\$0
03	Project Position Salaries	\$364,400	\$364,400
04	LTE/Misc. Salaries	\$389,100	\$389,100
05	Fringe Benefits	\$8,376,100	\$8,376,100
06	Supplies and Services	\$5,881,300	\$5,881,300
07	Permanent Property	\$0	\$0
08	Unalloted Reserve	\$0	\$0
09	Aids to Individuals Organizations	\$0	\$0
10	Local Assistance	\$0	\$0
11	One-time Financing	\$0	\$0
12	Debt Service	\$0	\$0
13		\$0	\$0
14	Total Cost	\$53,499,600	\$53,499,600
15	Project Positions Authorized	8.25	8.25
16	Classified Positions Authorized	0.00	0.00
17	Unclassified Positions Authorized	165.10	165.10

Decision Item by Numeric

Investment Board

Program	Decision Item/Numeric	1st Year Total	2nd Year Total	1st Year FTE	2nd Year FTE
	2000	Adjusted Base Funding Level			
01	Investment of funds				
	31 General program operations	\$53,499,600	\$53,499,600	173.35	173.35
	Investment of funds SubTotal	\$53,499,600	\$53,499,600	173.35	173.35
	Adjusted Base Funding Level SubTotal	\$53,499,600	\$53,499,600	173.35	173.35
	Agency Total	\$53,499,600	\$53,499,600	173.35	173.35

Decision Item by Fund Source

Investment Board

	Source of Funds		1st Year Total	2nd Year Total	1st Year FTE	2nd Year FTE
Decision Item	2000	Adjusted Base Funding Level				
	PR	S	\$53,499,600	\$53,499,600	173.35	173.35
	Total		\$53,499,600	\$53,499,600	173.35	173.35
Agency Total			\$53,499,600	\$53,499,600	173.35	173.35

ACT 201

Proposal under s. 16.42(4)(b)2.: **0% change in each fiscal year**

FY: **FY18 & 19**

Agency: **SWIB - 536**

Exclusions: Federal
Debt Service

Columns A-G were prepopulated for agencies to reflect state operations adjusted base and reductions agreed to by DOA and LFB. See Appendix H for instructions on how to complete these templates.

Proposed \$ and Proposed FTE columns reflect total agency proposed spending and positions for indicated fiscal year. These amounts should include standard budget adjustments (SBAs), any proposed reallocations or reductions to meet the target, and any other requests that the agency would want considered under this proposal.

Appropriations with zero dollars and zero FTEs are not loaded into the template. If you have any questions, contact your SBO analyst.

IF YOUR AGENCY PLANS TO TAKE THE SAME CUTS OVER BOTH YEARS, YOU SHOULD ONLY FILL OUT ONE GRID FOR 0% GROWTH AND ONE GRID FOR 5% REDUCTION, THEN CHANGE FY18 TO FY18 AND 19.

Agency	Appropriation		Fund Source	Adjusted Base		(See Note 1)	Proposed Budget 2017-18		Item Ref.	Change from Adj Base		(See Note 2)	Change from Adjusted Base after Removal of SBAs		
	Alpha	Numeric		\$	FTE	0% Change Target	Proposed \$	Proposed FTE		\$	FTE	\$	FTE		
536	1k	131	PR	53,499,600	173.35	0	53,499,600	173.35		0	0.00	0	0.00	0	0.00
Totals				53,499,600	173.35	0	53,499,600	173.35		0	0.00	0	0.00	0	0.00

Note 1: Reduction target must be met within state operations appropriations, but may be allocated across those appropriations and fund sources.

Note 2: Amounts should be SBAs (DINs 3001 - 3011) from agency request multiplied by -1.

Target Reduction = 0

Difference = **0**
Should equal \$0

Items - Describe proposed changes (excl. SBAs) to reach target or other priorities of agency

- 1
- 2
- 3

ACT 201

Proposal under s. 16.42(4)(b)1.: 5% change in each fiscal year

FY: **FY18 & 19**

Agency: **SWIB - 536**

Exclusions: Federal
Debt Service

Columns A-G were repopulated for agencies to reflect state operations adjusted base and reductions agreed to by DOA and LFB. See Appendix H for instructions on how to complete these templates.

Proposed \$ and Proposed FTE columns reflect total agency proposed spending and positions for indicated fiscal year. These amounts should include standard budget adjustments (SBAs), any proposed reallocations or reductions to meet the target, and any other requests that the agency would want considered under this proposal.

Appropriations with zero dollars and zero FTEs are not loaded into the template. If you have any questions, contact your SBO analyst.

IF YOUR AGENCY PLANS TO TAKE THE SAME CUTS OVER BOTH YEARS, YOU SHOULD ONLY FILL OUT ONE GRID FOR 0% GROWTH AND ONE GRID FOR 5% REDUCTION, THEN CHANGE FY18 TO FY18 AND 19.

Agency	Appropriation		Fund Source	Adjusted Base		(See Note 1)	Proposed Budget 2017-18		Item Ref.	Change from Adj Base		(See Note 2)	Change from Adjusted Base after Removal of SBAs	
	Alpha	Numeric		\$	FTE	5% Reduction Target	Proposed \$	Proposed FTE		\$	FTE	Remove SBAs	\$	FTE
536	1k	131	PR	53,499,600	173.35	(2,675,000)	50,824,600	163.35		(2,675,000)	(10.00)	0	0.00	(2,675,000) (10.00)
Totals				53,499,600	173.35	(2,675,000)	50,824,600	163.35		(2,675,000)	(10.00)	0	0.00	(2,675,000) (10.00)

Note 1: Reduction target must be met within state operations appropriations, but may be allocated across those appropriations and fund sources.

Note 2: Amounts should be SBAs (DINs 3001 - 3011) from agency request multiplied by -1.

Target Reduction = (2,675,000)

Difference = **0**
Should equal \$0

Items - Describe proposed changes (excl. SBAs) to reach target or other priorities of agency

- 1 The targeted \$2.7 million reduction would equate to a staffing reduction of 10 FTEs, including 4.6 investment FTEs.
- 2 This would require the movement of \$ 5.5 billion in assets from internal management by SWIB staff to external management by asset management firms.
- 3 While costs for internal management would decrease by \$2.7 million, SWIB's total costs would increase by \$ 6 million (net of internal cost savings) due to the higher fee structure for external management.
- 4 Particularly since 2007, we have followed a policy of increasing internal management because we can do so at lower cost without giving up returns. SWIB currently manages 67% of the assets with internal staff for 22% of the total costs of management. Viewed in this context, an arbitrary 5% cut in our operating budget makes no fiscal sense because it forces us to incur greater external fees or to risk lower returns, or both.
- 5
- 6