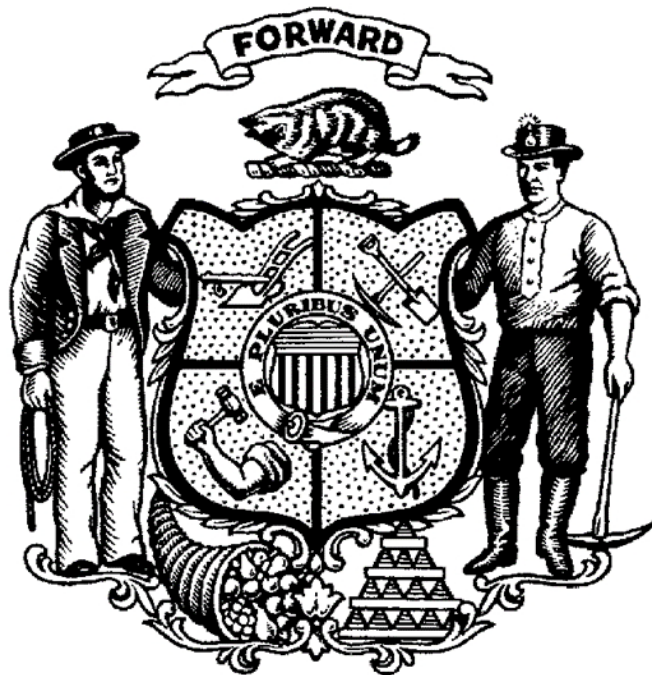


State of Wisconsin

Investment Board



Agency Budget Request

2025 – 2027 Biennium

September 16, 2024

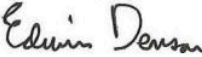
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Date: September 16, 2024

To: Kathy Blumenfeld, Secretary
Brian Pahnke, Administrator, Executive Budget & Finance
Department of Administration

Robert Lang, Director
Legislative Fiscal Bureau

From: Edwin Denson, Executive Director/Chief Investment Officer
Investment Board 

Re: **2025-27 Biennial Budget Request**

Attached is SWIB's budget submission for the 2025-27 biennium. Our budget is funded entirely by charges to the funds under management (program revenue). Our submission includes a \$83,748 increase in budget authority and 8 staff positions. Under Wis. Stats. 25.187(2)(b), the Board of Trustees establishes and monitors SWIB's operating budget each fiscal year. 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

SWIB's performance goals established in our 2023-25 biennial can be seen in the attached Performance Measures. The Core Fund ended December 31, 2023, with a net of all fees and expenses return of 11.40% and a 5-year net of all fees and expenses return of 9.29%. The Core Fund's 10-year net of external manager fees return was 7.09%. SWIB's returns for the Core Fund exceeded its performance benchmarks for all these periods and exceeded the long-term rate of return assumed by the WRS actuary. The Variable Fund had 1- and 5-year net of all fees and expenses returns of 22.24% and 12.76% respectively and a 10-year net of external manager fees return of 9.25% for the period ended December 31, 2023. The Core and Variable Funds comprise the WRS which represents approximately \$137.0 billion, or 86 percent, of the total assets managed by SWIB of \$160.2 billion as of June 30, 2024. From 2013 through 2022, net investment income earned by SWIB approximated 78 percent of total funding for the WRS. The WRS continues to be one of the few fully funded public pension plans in the U.S.

SWIB's performance goal for the next biennium is to increase active return through improved investment strategies. SWIB will consider enhancements to existing investment strategies to provide new opportunities for alpha generation. Additionally, SWIB will explore its requirements for a new strategic order management system to improve investment decision-making processes. Finally, SWIB will continue to explore opportunities for optimizing existing capabilities in setting its strategic asset allocation.

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. Internally managing approximately 37 percent of WRS assets helps keep SWIB's costs lower when compared to the cost of external active management, according to CEM Benchmarking, an independent provider of objective cost benchmarking for public pension plans. In addition to cost savings, SWIB's active management has created billions in additional income for beneficiaries when compared to a simple passively constructed portfolio. Over the last 20 years, SWIB's active management and diversified holdings generated \$18.3 billion for the Core Fund above what SWIB would have earned by investing in a passive portfolio consisting of 60% global equities and 40% domestic bonds.

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 when considering the amount of volatility in investment markets over the past several years. 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, 2023, SWIB held assets of \$635.0 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 Jameson Greenfield, Chief Financial Officer, at 608-266-9857.

AGENCY DESCRIPTION

SWIB is a trusted and skilled investment organization contributing to the strong financial future of the beneficiaries of the funds entrusted to it. An independent state agency governed by Chapter 25 of state statutes, SWIB is responsible for managing the assets of the fully funded Wisconsin Retirement System (WRS), the State Investment Fund (SIF), and other separately managed funds. Other funds managed by SWIB include the State Life Insurance Fund, Historical Society Trust Fund, Injured Patients and Families Compensation Fund, and University of Wisconsin System Trust Funds.

As of June 30, 2024, the board managed approximately \$160.2 billion in assets. The trust funds of the Wisconsin Retirement System (WRS) comprise nearly 86 percent of the funds under management at \$137.0 billion in assets. The WRS is a risk-sharing defined benefit plan. It is a hybrid model in that it contains elements of a defined benefit plan and a defined contribution plan, like a 401(k). SWIB works to protect and grow the assets of the WRS for the benefit of the approximately 677,000 participants who count on the pension for a more secure financial future. The WRS consistently ranks among the 10 largest public pension funds in the U.S.

The SIF invests the commingled cash balances of the state and its agencies, local governments and the WRS. Funds are managed to protect principal, provide liquidity and enhance returns. In addition, the separately managed funds are managed to fulfill specific investment objectives financial needs.

The board comprises 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 WRS from among WRS nonteacher participants, for six-year terms.
- One member is the secretary of the Department of Administration, or his or her designee.

The board has a fiduciary responsibility to invest in the best interest of the trust funds as a prudent expert.

MISSION

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

PROGRAMS, GOALS, OBJECTIVES AND ACTIVITIES

Program 1: Investment of Funds

Goal: Earn a reasonable 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. SWIB's overall objective for each fund it manages is to seek aggregate investment returns in excess of the applicable benchmarks over all cumulative time periods constructed with a prudent level of risk. 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 participants 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 Separately Managed Funds is to meet annual fund cash flow requirements, as established by their governing boards.

PERFORMANCE MEASURES

FY2023 AND FY2024 GOALS AND ACTUALS

| Prog. No. | Performance Measure | Goal FY2023 | Actual FY2023 | Goal FY2024 | Actual FY2024 |
|------------------|---|---|---|---|--|
| 1. | Investment returns for the Wisconsin Retirement System exceed market index returns for the asset classes in which the funds are invested on a net basis. ^{1,2} | Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis | <u>CY2022</u> <u>Core</u> 1 Year: Yes 5 Year: Yes 10 Year: Yes <u>Variable</u> 1 Year: Yes 5 Year: No 10 Year: No | Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis | <u>CY2023</u> <u>Core</u> 1 Year: Yes 5 Year: Yes 10 Year: Yes <u>Variable</u> 1 Year: No 5 Year: No 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. ^{1,2,3} | Net return averages at least 6.8% annually over the long term (five and ten years) | <u>CY2022</u> <u>Core</u> 5 Yr - 6.25% 10 Yr - 7.25% | Net return averages at least 6.8% annually over the long term (five and ten years) | <u>CY2023</u> <u>Core</u> 5 Yr - 9.40% 10 Yr - 7.09% |

¹ Returns reported net of all fees and expenses, except where noted. The 10-year returns are reported net of external manager fees.

² The Wisconsin Retirement System official investment performance and measures are reported on a calendar year basis.

³ The assumed rate of return is established by the Employee Trust Funds (ETF) Board, acting on recommendation of its independent consulting actuary.

FY2025, FY2026 and FY2027 GOALS

| Prog . No. | Performance Measure | Goal FY2025 | Goal FY2026 | Goal FY2027 |
|-------------------|---|---|---|---|
| 1. | Investment returns for the Wisconsin Retirement System exceed market index returns for the asset classes in which the funds are invested on a net basis. ^{1,2} | Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis | Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis | Net investment returns exceed market performance benchmarks on a one-, five- and ten-year basis |
| 1. | Long-term investment returns for the Core Retirement Fund meet or exceed the rate of return assumed by Wisconsin Retirement System actuary. ^{1,2,3} | Net return averages at least 6.8% annually over the long term (five and ten years) | Net return averages at least 6.8% annually over the long term (five and ten years) | Net return averages at least 6.8% annually over the long term (five and ten years) |

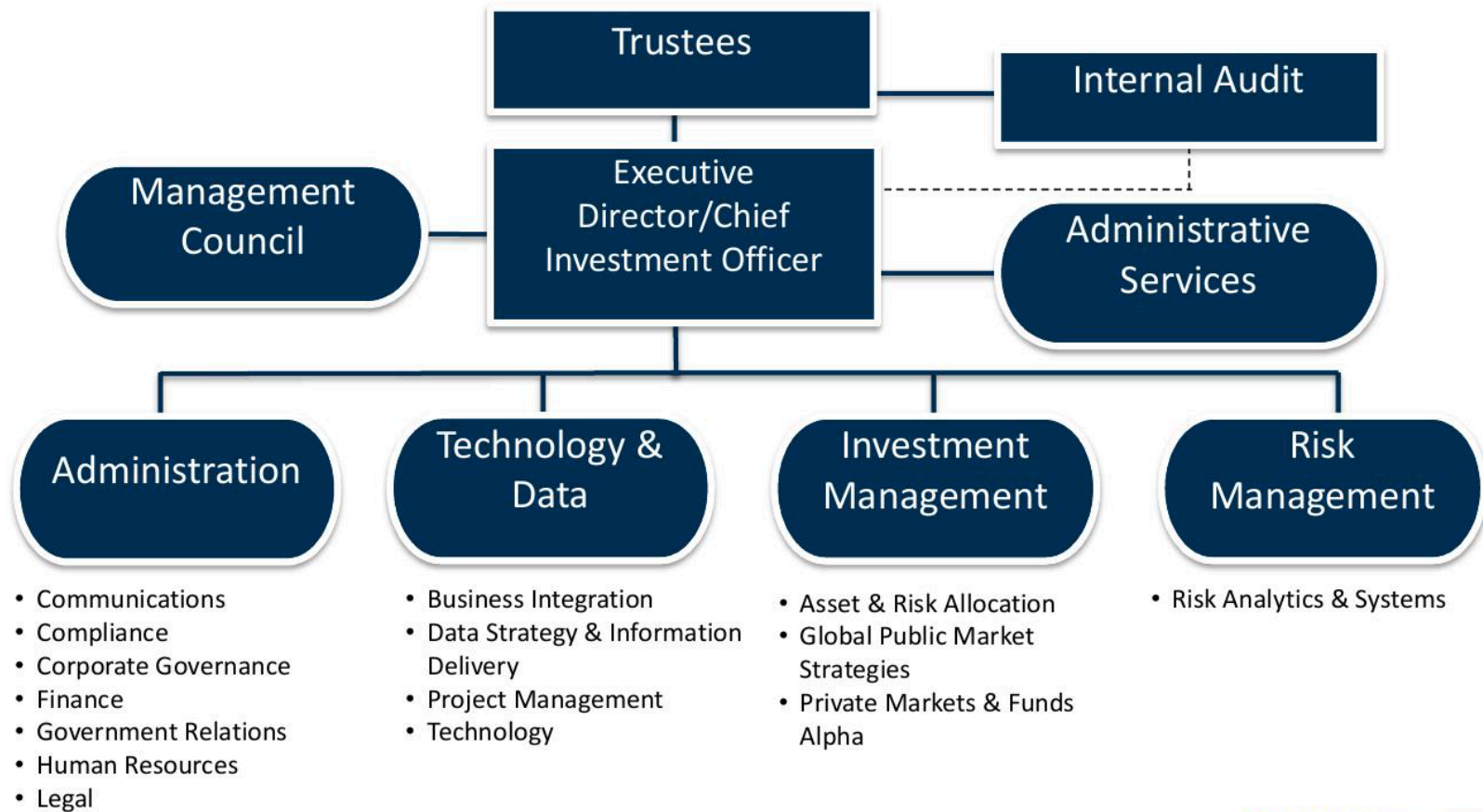
¹ Returns reported net of all fees and expenses, except where noted.

² The Wisconsin Retirement System official investment performance and measures are reported on a calendar year basis.

³ The assumed rate of return is established by the Employee Trust Funds (ETF) Board, acting on recommendation of its independent consulting actuary.

SWIB Organizational Structure

298 FTE as of June 30, 2024



Agency Total by Fund Source

Investment Board

2527 Biennial

| | | 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 | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| Total | | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| Grand Total | | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |

Agency Total by Program

Investment Board

2527 Biennial Budget

| Source of Funds | Prior Year Total | ANNUAL SUMMARY | | | | | BIENNIAL SUMMARY | | | |
|-------------------------------|----------------------|----------------------|----------------------|----------------------|---------------|---------------|-------------------------|----------------------|-------------------|-------------------|
| | | 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 | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| S | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| Total - Non Federal | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| S | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| PGM 01 Total | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| PR | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| S | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| TOTAL 01 | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| S | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |
| AGENCY TOTAL | \$126,335,392 | \$102,814,700 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 | \$205,629,400 | \$205,629,400 | \$0 | 0.00% |

Agency Total by Decision Item

Investment Board

2527 Biennial Budget

| Decision Item | 1st Year Total | 2nd Year Total | 1st Year FTE | 2nd Year FTE |
|----------------------------------|----------------------|----------------------|---------------|---------------|
| 2000 Adjusted Base Funding Level | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| TOTAL | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |

Decision Item (DIN) - 2000

Decision Item (DIN) Title - Adjusted Base Funding Level

NARRATIVE

Adjusted Base Funding Level

Decision Item by Line

2527 Biennial Budget

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

| | Expenditure Items | 1st Year Cost | 2nd Year Cost |
|-----------|-------------------------------------|----------------------|----------------------|
| 01 | Permanent Position Salaries | \$85,108,700 | \$85,108,700 |
| 02 | Turnover | \$0 | \$0 |
| 03 | Project Position Salaries | \$0 | \$0 |
| 04 | LTE/Misc. Salaries | \$345,000 | \$345,000 |
| 05 | Fringe Benefits | \$17,361,000 | \$17,361,000 |
| 06 | Supplies and Services | \$0 | \$0 |
| 07 | Permanent Property | \$0 | \$0 |
| 08 | Unallotted 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 | | \$0 | \$0 |
| 15 | | \$0 | \$0 |
| 16 | | \$0 | \$0 |
| 17 | TOTAL | \$102,814,700 | \$102,814,700 |
| 18 | Project Positions Authorized | 0.00 | 0.00 |
| 19 | Classified Positions Authorized | 0.00 | 0.00 |
| 20 | Unclassified Positions Authorized | 298.00 | 298.00 |

Decision Item by Numeric

2527 Biennial Budget

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 | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| | Investment of funds Sub Total | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| | Adjusted Base Funding Level Sub Total | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| | | | | | |
| | Agency Total | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |

Decision Item by Fund Source

2527 Biennial Budget

Investment Board

| Decision Item/Source of Funds | | 1st Year Total | 2nd Year Total | 1st Year FTE | 2nd Year FTE |
|--|---|----------------------|----------------------|---------------|---------------|
| 2000 Adjusted Base Funding Level | | | | | |
| PR | S | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| Adjusted Base Funding Level Total | | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |
| | | | | | |
| Agency Total | | \$102,814,700 | \$102,814,700 | 298.00 | 298.00 |

ACT 201

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

FY: **FY26 & 27**

Agency: **SWIB - 536**

Exclude: 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 "FY26" TO "FY26 AND 27".

| Agency | Appropriation | | Fund Source | \$ | FTE | (See Note 1) 0% Change Target | Proposed Budget 2025-26 | | Item Ref | Change from Adj Base | | (See Note 2) Remove SBAs | | Change from Adj Base after Removal of SBAs | |
|---------------|---------------|---------|-------------|-------------------------|---------------|-------------------------------------|-------------------------|---------------|----------|----------------------|-------------|-----------------------------|-------------|--|-------------|
| | Alpha | Numeric | | | | | Proposed \$ | Proposed FTE | | \$ | FTE | \$ | FTE | \$ | FTE |
| 536 | 1k | 131 | PR | \$102,814,700.00 | 298.00 | \$0 | \$102,814,700 | 298.00 | | \$0 | 0.00 | \$0 | 0.00 | \$0 | 0.00 |
| Totals | | | | \$102,814,700.00 | 298.00 | \$0 | \$102,814,700 | 298.00 | | \$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): **5% change in each fiscal year**

FY: **FY26 & 27**

Agency: **SWIB - 536**

Exclude: 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 "FY26" TO "FY26 AND 27".

| Agency | Appropriation | | Fund Source | \$ | FTE | (See Note 1) 5% Change Target | Proposed Budget 2025-26 | | Item Ref | Change from Adj Base | | (See Note 2) Remove SBAs | | Change from Adj Base after Removal of SBAs | | |
|---------------|---------------|---------|-------------|-------------------------|---------------|-------------------------------------|-------------------------|---------------|----------|----------------------|----------------------|-----------------------------|--------------|--|----------------------|---------------|
| | Alpha | Numeric | | | | | Proposed \$ | Proposed FTE | | \$ | FTE | \$ | FTE | \$ | FTE | |
| | 536 | 1k | | | | | 131 | PR | | \$102,814,700.00 | 298.00 | (\$5,140,700) | \$97,674,000 | 283.10 | | |
| Totals | | | | \$102,814,700.00 | 298.00 | (\$5,140,700) | \$97,674,000 | 283.10 | | | (\$5,140,700) | -14.90 | \$0 | 0.00 | (\$5,140,700) | -14.90 |

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 = (\$5,140,700)

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

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

1 The targeted \$5.1 million reduction would equate to a staffing reduction of approximately 15 total FTEs (10 investment services staff, 5 investment management staff)

This would require an estimated movement of \$5.1 billion in assets from internal management by SWIB staff to external management by asset management firms.

While costs from internal management would decrease by \$5.1 million, SWIB's total costs would increase an estimated \$9.2 million (net of internal cost savings) due to the higher fee structure for external management.

Particularly since 2007, SWIB has increased internal management when possible to optimize costs without giving up returns. SWIB currently manages approximately 45% of total assets with internal staff. For CY2023, external manager base fees were approximately 3.4 times higher than internal costs. Viewed in this context, an arbitrary 5% cut in the operating budget does not make fiscal sense because it forces SWIB to incur greater external fees or to risk lower returns, or both.