



Budget Activity & Performance Assessment

State Investment Board

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Office of Financial Management

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Table of contents:

Executive Summary	Page 2
Measure Qualitative Evaluation Summary	3
Budget History by Activity	4
Specific Opportunities for Improvement	5
Agency Comments	6
Budget Activity and Measure Critique	7-8
Alignment Overview – Budget Activity Structure	9
Alignment Overview – Strategic Plan Structure	10
Appendix A – Median and mean, performance measures	11

Executive Summary

The Washington State Investment Board (WSIB) should be commended for the amount of historic data provided in the performance measure system. Although the five existing measures are fine, they are all variation of a single dimension of performance: investment return compared to a benchmark.

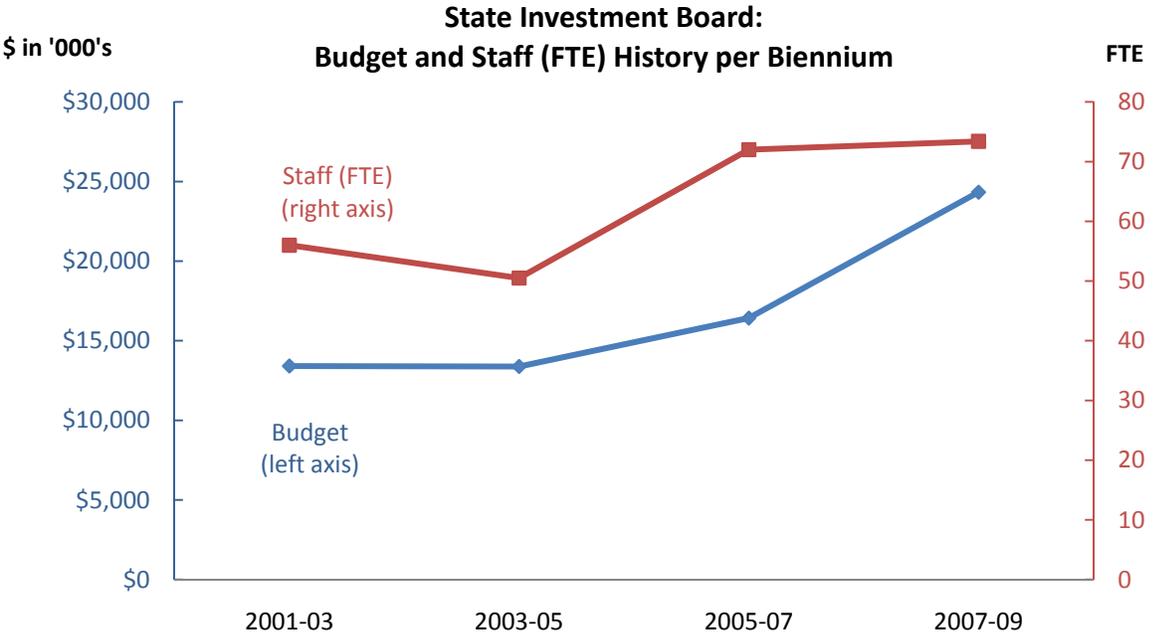
Providing additional measures might allow the WSIB to tell a better story about its performance. The Board staff may want to consider adding additional measures to show performance in dimensions such as investment cost, risk or portfolio diversity.

Activity – Measure Qualitative Evaluation Summary

Budget Activity	Performance Measure Evaluation Criteria *						
	Relevance	Understand-ability	Comparability	Timeliness	Consistency	Reliability	Performance
A001 Investment Activities	Fair: Although there are five measures, there's only one dimension of performance: investment return versus a benchmark.	Good	Good	Good	Good - measure detail includes definitions of benchmarks, when data is available, etc.	Good	Good overall, although recent performance for some measures indicates volatile performance

* Evaluation Criteria Definitions	
Relevance	The performance measure is useful to a budget/policy development audience in assessing the level of accomplishment
Understandability	Clear, concise, and easy for a non-expert to understand
Comparability	Do the data, targets, and footnotes provide the reader with enough context to tell whether performance is getting better, worse, or staying the same?
Timeliness	Is the data current and reported frequently enough to be of value in assessing accountability and making decisions?
Consistency	Is the data collection method standardized and is the operational definition for data calculations adhered to?
Reliability	Is the information verifiable, free from bias, and a faithful representation of what it purports to represent?
Performance	Is actual performance in reference to the stated targets getting better, worse, or staying the same over time?

Budget History by Activity



Specific Opportunities for Improvement

Budget Activity Number and Title	Measures	Improvement Suggestions
A001 – Investment Activities	Existing measures are fine, but all measure the same thing	<p>The Washington State Investment Board should consider adding additional measures to show performance in dimensions other than investment return compared to a benchmark. Options might include:</p> <ul style="list-style-type: none"> • Investment cost • Degree to which investments achieve specific fund objectives (e.g. ability to cover obligations) • Portfolio diversity • Risk • Return on investment in additional staff

Agency Comments and Reactions

The Washington State Investment Board appreciates this budget activity and performance assessment.

Our mission is to invest with integrity, prudence, and skill to meet or exceed the financial objectives of those we serve. We have a clear and measurable purpose. Ours is a strong performance culture that aspires to make the WSIB a superior institutional investor organization. This means our pursuit of excellence must be professionally, ethically, and legally impeccable at all levels.

The WSIB has one service: investment management. Our service performance results are investment returns. These results are described in Financial Performance. The WSIB most likely has one of the most robust performance measurement programs in state government due to the nature of the investment management business. Each portfolio managed has established external benchmarks, based on common and recognized industry standards that allow our beneficiaries to directly compare the WSIB performance to other investors. We not only track market data on a daily basis, we track it over longer time periods as well. It is often the measurements of longer period performance which are more relevant and informative both with respect on how the agency is performing as well as indicating what problems or issues may be developing in the portfolio. It's also important to understand that when the agency undertakes investment decisions, it may take more than a decade for the effective performance of that investment decision to be revealed. In other words, it's not always possible or desirable to track performance on a daily basis. In fact, daily performance may bias the agency away from making important strategic decisions in making hasty decisions.

The WSIB is entrusted with an incredible amount of money to manage and invest. As such, it is absolutely essential that we be as transparent, accessible, and informative about how we do what we do and why to the greatest extent possible. Therefore, the WSIB at OFM's recommendation will add additional measures to show performance in Portfolio diversity: Comingled Trust Fund (CTF) Asset Allocation - WSIB invests based on the risk and return objectives and policy constraints of each client we serve. For its largest asset pool, the CTF, the WSIB invests across a range of asset classes in order to achieve the twin objectives of return diversification and risk reduction for plan beneficiaries over the long term. The WSIB develops its asset allocation policy weight ranges and long-term targets for the CTF on an annual basis, and reviews its allocation on a quarterly basis. In the event that an asset class falls outside the policy weight objective, a rebalancing exercise is undertaken if appropriate.

We appreciate and value the time and assistance provided by Jeffrey Showman and Jane Sakson in the thoughtful review and recommendations of our budget activity measures.

Budget Activity and Measure Critique

Budget Activity Number, Title and Summary: A001 - Investment Activities The Washington State Investment Board (WSIB) manages approximately \$81.9 billion in investments for retirement, industrial insurance, permanent and other trust funds, including the defined benefit and defined contribution pension plans for teachers, school employees, law enforcement officers, firefighters, and public employees. The WSIB also manages investments for the Deferred Compensation Plan, Guaranteed Education Tuition (GET) program, Budget Stabilization Fund, Developmental Disabilities Endowment Trust, Judges Supplemental Retirement Fund, and the Basic Health Fund. The duty of the Board is to diversify investments and maximize returns, at a prudent level of risk, for the exclusive benefit of fund beneficiaries.

Related performance measures:

Number and title:	Type	Analysis comments	Performance chart
1100 Retirement Funds – Median rate of return compared to a pension fund benchmark: TUCS Public Funds over \$1 billion)	Outcome	Mean performance over the six year period is .76% above the benchmark, but performance in the most recent two quarters is outside expected process limits (see Appendix A, p. 11.)	
1200 Permanent Funds	Outcome	Median and average performance are both very close to the benchmark. However, this measure shows volatile performance during recessions due to a “flight to quality” by investors seeking safety of fixed income investments. Investor demand creates volatile prices for bonds, producing the large swings shown on the chart.	

<p>1300 Other Trust Funds</p>	<p>Outcome</p>	<p>Similar to measure 1200, this process shows volatility during recessions at both ends of the eight year period due to a benchmark based on fixed income securities, but median performance is just about equal to benchmark.</p>	
<p>1400 Retirement Funds Value Added Benchmark</p>	<p>Outcome</p>	<p>This is the only one of these measures that appears to be stable and predictable. However, the average and median performance are below the benchmark.</p>	
<p>1500 Other Trust Funds & Guaranteed Education Tuition (GET)</p>	<p>Outcome</p>	<p>Median and average performance are both positive, but performance in the most recent period is outside expected process limits as well as below zero. However, this measure has only been in pace for one biennium.</p>	

OFM Assessor Comments: All five measures are essentially the same measure: comparing investment return against the return of a comparable benchmark. The only difference is among the type of funds being invested, and hence the choice of benchmark. Rate of return is an important objective of investment success, but is not the only one. Private sector investment options, such as mutual funds, report standard metrics such as normalized investment costs or risk. The Washington State Investment Board’s strategic plan mentions several other objectives, including meeting financial objectives of each fund; diversifying portfolios and choices; and expenses that compare favorably to similar organizations (see p. 10). Providing additional measures might allow the WSIB to tell a well-rounded story about its performance.

Agency comments:

Alignment Overview – Budget Activity Structure

Statewide Result Area	Strategy	Activity
Strengthen government's ability to achieve results efficiently and effectively	Safeguard and manage public funds	A001 Investment Activities

Alignment Overview – Strategic Plan Structure

Mission: To invest with integrity, prudence, and skill to meet or exceed the financial objectives of those we serve.

Strategic Goal	Objective	Performance measure
Total investment portfolio is diversified	Expand diversity of portfolio by both sector and global expansion	[Develop precise performance measurement methodology based on selected risk strategy]
Value: Design portfolio to meet the unique investment objectives of each fund	Retirement funds: Maximize return at a prudent level of risk	Implementation value added Performance against benchmark
	Defined contribution: Offer members a comprehensive range of options	
	Deferred Compensation: Offer participants well-managed options at low cost	Each option has its own benchmark
	Insurance funds: Meet the reserve and duration targets set by Labor and Industries	Comparable Market Indices duration targets
	Permanent funds: emphasize stable income	Barclay Capital Aggregate Index
	Common School Fund: maximize growth of assets and maintain a targeted level of income	Barclays Capital Aggregate and Dow Jones U.S. TSMI , based on asset allocation
	GET Program: generate a 4.5% real rate of return	Custom benchmark
	Other trust funds: exceed the return of respective benchmarks	Custom benchmark
Capacity: Broaden reach and deepen insights and oversight	Sustain excellent investment performance	
	Enhance risk management and control	
	Strengthen technology infrastructure	
	Align organizational capacity	
Support: Conduct selves in marketplace and with stakeholders to receive support to fulfill mission	Take advantage of inefficient markets in key sectors (real estate, private equity)	
	Contract for specialized services (external money managers, custodial banking, accounting)	
	Investment earnings cover expenses that compare favorably to comparable pension plans	
	Increase intervention in corporate governance (exercise proxy voting; regulatory initiatives of SEC, etc.)	

Appendix A - State Investment Board performance measure midpoints, based on the median and mean of all data during the period. Positive number indicates the fund outperformed the benchmark.

No.	Measure description	Median	Mean	Period
1100	Retirement Funds: The variance from the median rate of return in comparison to a nationally recognized public pension fund benchmark (TUCS Public Fund > \$1 Billion Median)	0.40	0.27	FY 2001-2009
1200	Permanent Funds: The variance from the average rate of return in comparison to a nationally recognized bond fund benchmark (Barclay Capital Aggregate)	0.01	0.02	FY 2001-2009
1300	Other Trust Funds: The variance from the average rate of return in comparison to a nationally recognized fund benchmark 90 day Treasury Bill)	(0.01)	0.01	FY 2001-2009
1400	Retirement Funds - Measure the variance from the median rate of return in comparison to an implementation value added benchmark.	(0.57)	(0.50)	FY 2007-2009
1500	Other Trust Funds & GET - Measure the variance from the average rate of return in comparison to a custom benchmark.	0.31	0.12	FY 2007-2009