



STATE OF WASHINGTON
STATE INVESTMENT BOARD

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May 27, 2020

David Schumacher, Director
Office of Financial Management
PO Box 43113
Olympia, WA 98504-3113

Dear Director Schumacher:

Thank you for the opportunity to respond to your May 13, 2020, memo regarding identification of budget savings options due to the extraordinary economic hardship created by COVID 19. While the Washington State Investment Board (WSIB) was not directed to achieve a specific reduction target because we are a non-General Fund agency, we recognize our need to be prudent stewards.

This letter outlines the WSIB's budget savings strategy for making immediate one-time reductions and the case for continued fulfillment of long-term investment capabilities. The WSIB will generate the savings from Fund 031 - State Investment Board Investment Account.

The WSIB manages investments in 76 different countries, across 6 continents, 49 currencies, and more than 1,4000 investment holdings. The WSIB delivers strong returns for 17 pension funds for public employees, teachers, school employees, law enforcement officers, firefighters and judges. This also includes the Deferred Compensation Program as a supplement to other retirement benefits. In addition, we manage investments for 17 other public funds that support or benefit industrial insurance, colleges and universities, and developmental disabilities. The management of these funds requires an investment discipline with the highest standards of integrity, commitment to working for the best interests of our beneficiaries, and dedication to continuous improvement.

With this plan, we have been careful to protect the more than \$138 billion in funds under our management and to comply with our statutory fiduciary responsibilities.

Budget Savings of \$3.6 million for the 2019-21 biennium

To address immediate state-level budget constraints for FY 2020 and FY2021, the WSIB will engage three primary sources of one-time savings to achieve a \$2.1 million, or 7 percent, budget savings for FY 2020 and a \$1.5 million, or 5 percent, budget savings for FY 2021. These one-time savings are mainly achieved by:

- Accruing savings from existing vacancies
- Restricting travel
- Implementing savings by withholding budgeted investment officer salary increases that would have been effective July 1, 2020

These savings are described in the narrative below and are further detailed in the attached spreadsheet.

Savings Strategy: Constrain near-term spending; sustain long-term capabilities

The WSIB will make a series of significant one-time savings, while proposing nominal reductions on an ongoing basis, in order to balance responsible budget constraints with prudent preservation of vital investment capability.

In many ways, the 2020 market environment is even more challenging and more systemic than the Great Recession of 2008-2009. The previous event required full restoration of our financial services institutions. This event will require full restoration of broader economies and a holistic rebuilding of many fundamental supply/demand systems. The reopened retail, manufacturing, real estate, and technology sectors will undergo some degree of permanent change. This comes at a time when the WSIB has increased its liquidity allowances and is building out the rigor of its investment analytics and risk management skills. All of this makes for sharpened insights, a deeper talent pool, and the ability to pursue opportunity amid a shocked landscape of risk and volatility. This is not a time to recoil from a challenge; it is a time for prudent investment selection and deeper due diligence.

In the last financial crisis, our focus was primarily on building and maintaining a diverse, storm-resistant set of portfolios. Today, we have enhanced that discipline by adding architects to the building process, so we can better monitor risk and more fully understand how to respond to market stresses within our portfolios. The most vital pillars of these ongoing enhancement are:

- Build-out of best-in-class risk/return analytics
- Tailored development of investment data management
- Professionals who possess depth of experience and investment insights
- Innovative investment tools and structures meant for putting large amounts of capital to work for long-term outperformance at global scale

By making near-term cuts and preserving long-term capabilities, our enhanced resources remain available to help us navigate the unprecedented economic fallout of the pandemic. Our Board has made a strategic decision to build out the capabilities of our organization so that we can be more responsive, more resilient. We want to adhere to responsible budget necessities while stopping short of compromises that would harmfully erode what we have deliberately built for just these types of situations.

One-Time Savings

Vacancy Rate Accruals – \$1,735,000

We have adjusted our hiring pace for two reasons: the delay of some projects that would be difficult to execute under shelter-in-place restrictions and the challenge of recruiting and onboarding new staff when we are all working remotely. While most of our ongoing work can be done from home, final due diligence on new investment managers and new asset acquisition require on-site inspection. Hiring staff for many positions also requires face-to-face interviews in the final selection stages.

	Effective Date	Hire Date	2020 Months Of Savings	2021 Months Of Savings	Total Months of Savings
Real Estate CTF – ASIO	Jan 2020	Aug 2020	6	1	7
RMAA – ASIO	Jul 2020	Sep 2020	0	2	2
Real Estate CTF – IO	Jan 2020	Nov 2020	6	4	10
Innovation Portfolio – IO	Jan 2020	Dec 2020	6	5	11
IT Investment Data Engineer – AIO	Jan 2020	Jan 2021	6	6	12
IT Investment Data Analyst – AIO	Jul 2019	Apr 2021	0	9	9
COO - ASIO	Dec 2019	Apr 2021	12	9	21
Risk and Compliance Officer – IO	Jul 2020	May 2021	9	11	20

Out of State Travel Reductions – \$753,000

We began sharply reducing travel in early February and implemented a complete travel ban effective February 27, 2020. We anticipate resuming some of only the most essential travel in late 2020, but we do not expect travel to resume at anything resembling pre-COVID 19 levels until perhaps mid-2021. These restrictions will allow us to continue to accrue one-time savings through the biennium, with a current assumption that we will resume at-historic levels in the 2021-2023 biennium. We are expecting that the increased adoption of virtual technologies will replace some discretionary travel in the future, but it is simply not possible today to precisely project how much; therefore, it would be short-sighted for us to propose ongoing or permanent travel savings.

Investment Officer Salary Savings – \$469,000

The WSIB was granted by the legislature \$1.4 million for a 3 percent pay increase for investment officers effective July 1, 2019, and another 3 percent increase effective July 1, 2020. We will not be giving the 3 percent budgeted annual raises to our investment staff in July 2020; the only compensation changes for our staff in 2020 would be a statewide COLA, if implemented. Based on this decision, we will be offering up a significant one-time savings. While all of the WSIB expenses come from investment earnings and the WSIB would have the budgeted resources to grant pay increases, we want to show solidarity with the rest of state government and demonstrate common respect for the financial situation of many of our beneficiaries.

Under-Expenditures – \$438,000

We achieved one-time savings associated with under-expenditures on office supplies, employee development, and other goods and services. These one-time savings are in part due to the delay in hiring new investment officer positions and in the filling of other existing vacancies.

Ongoing Savings

Personal Services Contracts Reduction – \$46,000

We eliminated the use of Legislative and Managerial Training services consultants. We assigned all legislative duties to agency staff and will utilize state contracted managerial training services.

Discretionary Travel Reductions – \$156,000

We reduced discretionary out of state travel for staff to attend conference and seminars. Staff will attend virtual conferences, trainings, and seminars.

Conclusion

In summary, our proposed approach does not shelter our investments from dramatic market dislocations or a pandemic-induced economic stall. However, our approach does allow us to be resilient and opportunistic in the face of a storm. We've learned from past economic shocks that investment deals made during high-stress environments often generate superior performance, but only if we rely on quality deal sourcing, painstaking research, and unyielding due diligence.

Our hope is that careful, immediate cuts can be combined with preservation of our strategic strengths in order to ensure a sensitive and smart budget path for the future of the WSIB and its beneficiaries. We welcome additional thoughts and questions along with your ongoing partnership in tackling these budget planning challenges.

David Schumacher, Director
Office of Financial Management
May 27, 2020
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If you have questions, please do not hesitate to contact me or Celina Verme. I can be reached at (360) 704-8709 or Theresa.Whitmarsh@sib.wa.gov. Celina can be reached at (360) 956-4740 or Celina.Verme@sib.wa.gov.

Respectfully,

A handwritten signature in blue ink, appearing to read 'T. Whitmarsh', with a long horizontal flourish extending to the right.

Theresa Whitmarsh
Executive Director

Cc: Nona Snell, Assistant Director Budget, Office of Financial Management
Jane Sakson, Senior Budget Assistant, Office of Financial Management
Celina Verme, Budget and Government Operations Officer, WSIB

Budget Savings Options 2020

Dollars in Thousands

Agency: 126 State Investment Board (SIB)

Agency Priority H, M, L	Impact 1-5	Program/Activity	GF-S				Other Funds				FTE Change		Brief Description and Rationale	Effective Date (MM/YY)	Impacts of Reductions and Other Considerations	Law/Reg. Change Required	
			FY 20	FY 21	FY 22	FY 23	Fund	FY 20	FY 21	FY 22	FY 23	FY 20					FY 21
H	1	Real Estate Assistant Senior Investment Officer - Commingled Trust Fund (CTF)					031	155	26			0.5	0.1	Delay hiring of an Assistant Senior Investment Officer for Real Estate - CTF to 08/20	01/20	One-time savings. The Board increased its target allocation to Real Estate in the last asset allocation study, and as a result additional FTEs were requested; essential position for the WSIB.	
H	1	Risk Management and Asset Allocation (RMAA) Assistant Senior Investment Officer					031		51			0.0	0.2	Delay hiring of an Assistant Senior Investment Officer for RMAA to 09/20	07/20	One-time savings. This position oversees the research function and is increasingly critical due to the market dislocation given the current global health crisis. It is instrumental to help the WSIB deliver on its mission to maximize returns at a prudent level of risk.	
H	1	Real Estate Investment Officer - CTF					031	117	78			0.5	0.3	Delay hiring of an Investment Officer for Real Estate - CTF to 11/20	01/20	One-time savings. The Board increased its target allocation to Real Estate in the last asset allocation study, and as a result additional FTEs were requested; essential position for the WSIB.	
H	1	Innovation Portfolio Investment Officer					031	117	98			0.5	0.4	Delay hiring of an Investment Officer for Innovation Portfolio to 12/20	01/20	One-time savings. This position is critical to build out the Innovation Portfolio of the CTF, designed to take advantage of market opportunities and strategies that are not currently addressed by existing staff expertise.	
H	1	Information Technology Investment Data Engineer					031	84	84			0.5	0.5	Delay the hiring of an Information Technology Investment Data Engineer until 01/21	01/20	One-time savings. This positions was requested for the 2019-21 biennium to develop financial models, and visualize investment data sets for routine and complex customized reporting.	
H	1	Chief Operating Officer					031	302	232			1.0	0.8	Delay the hiring of the Chief Operating Officer until 04/21	07/19	One-time savings. This position is a crucial component of the Board's management succession plan.	
H	1	Information Technology Investment Data Analyst					031		87			0.0	0.8	Delay the hiring of an Information Technology Investment Data Analyst until 04/21	12/19	One-time savings. This positions supports the agency's increasing use of investment-related data analytics.	
H	1	Legal Services Risk and Compliance Officer					031	137	167			0.8	0.8	Delay hiring of the Risk and Compliance Officer to 05/21	07/20	One-time savings. This positions supports agency compliance with legal and regulatory best practices.	
H	4	Investment Officer Compensation					031		469					Compensation increase for investment officers will not be granted on 07/20	07/20	One-time savings. WSIB is dependent on its ability to attract and retain high-quality investment professionals. Adequate compensation is critical to WSIB's success. Lower turnover enables investment staff to develop a deep understanding of WSIB's long-term investment strategies and investment portfolio construction.	
L	1	Legislative Services Contract					031	12	12	12	12			Eliminates Legislative services contract	07/19	Assistance with legislative services issues was assigned to agency staff.	
L	1	Managerial Training Services Contract					031	11	11	11	11			Eliminates in-house customized managerial training for staff	07/19	Staff will attend lower cost contracted managerial training courses.	
M	1	Discretionary Out of State Travel					031	78	78	78	78			Reduces discretionary out of state travel for staff to attend out of state conferences and seminars	07/19	When available staff will attend virtual conferences and seminars. The value of the insights developed through in-person peer interactions and industry experts may be negatively impacted over time.	
M	1	Employee Development - Conference/Seminars					031	168						Under-expenditure due to early implementation of conference attendance restrictions due to COVID-19	02/20	One-time savings. Under-expenditure, no ongoing impact.	
H	1	Out of State Travel					031	753						Under-expenditure due to delay in hiring new Investment Officer positions and early implementation of travel restrictions due to COVID-19	01/20	One-time savings. Under-expenditure, no ongoing impact.	
L	1	Goods and Services - Office supplies, communications and telecommunication services					031	65						Under-expenditure due in part to staff vacancies, as well as delay in hiring new investment Officer positions	07/19	One-time savings. Under-expenditure, no ongoing impact.	
L	1	Certificate of Participation - Lease/purchase agreement with the Office of State Treasurer					031		113					Under-expenditure due to savings from IT refresh financing	07/20	One-time savings. Under-expenditure, no ongoing impact.	
L	1	Rent - Delay Olympia office expansion					031	50	42					Under-expenditure due to delay the Olympia office expansion (space currently occupied by LEOFF Board) to 05/21	07/19	One-time savings. Under-expenditure, no ongoing impact.	
Total								2,049	1,548	101	101	3.8	3.9				

Total Allotment 031 29,261 30,840
Saving Percentage 031 7.0% 5.0%

Priority:

L = Low priority agency activity or program
M = Medium priority agency activity or program
H = High priority agency activity or program

Impact:

1 = Allows continuation of the program/activity at a reduced level
2 = Eliminates the ability to perform program objectives
3 = Eliminates agency function
4 = Long term implications (moves the problem to next biennium)
5 = Short term (reduction to one time increase)