

# YOUR VESTED INTEREST

North Dakota State Investment Board

March 2016

## FROM THE DIRECTOR'S CHAIR

David Hunter  
Executive Director/CIO



## SIB and RIO Oversee Investment Management for 24 ND Agencies



During the last legislative session I received a number of questions relating to the services offered by the State Investment Board (SIB) and the Retirement and Investment Office (RIO). Nearly everyone I met with understood that RIO provided excellent retirement benefit services to ND public school teachers and administrators through the ND Teachers' Fund for Retirement (TFFR). Most individuals also knew the SIB and RIO provided investment services to TFFR and the ND Public Employees

Retirement System (PERS) pension plans, along with the Legacy Fund and Budget Stabilization Advisory Board. However, most individuals were not aware that the SIB also provided investment management services to twenty other North Dakota agencies. As such, I thought it might be helpful to list the agencies receiving investment management services and to share some highlights about the SIB and RIO.

### State Investment Board (SIB)

Lt. Governor Drew Wrigley, *Chair*  
Mike Sandal, *PERS Trustee, Vice Chair*  
Lance Gaebe, *Land Commissioner*  
Mike Gessner, *TFFR Trustee*  
Adam Hamm, *State Insurance Commissioner*  
Rob Lech, *TFFR Trustee*  
Mel Olson, *TFFR Trustee*  
Kelly Schmidt, *State Treasurer*  
Yvonne Smith, *PERS Trustee*  
Cindy Ternes, CPA, *Designee WSI*  
Tom Trenbeath, *PERS Trustee*

### RIO Administrative Office

David Hunter, Executive Director/CIO  
Fay Kopp, Deputy Executive Director/  
Chief Retirement Officer  
Darren Schulz, Deputy CIO  
Shelly Schumacher, Editor

### ND Retirement and Investment Office

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Bismarck, ND 58507-7100  
701-328-9885, Toll free: 1-800-952-2970  
[www.nd.gov/rio](http://www.nd.gov/rio)

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### Pension Trust (\$4.7 billion)

*Teachers' Fund for Retirement (TFFR)*  
*Public Employees Retirement System (PERS)*  
*City of Bismarck Employee Pension Plan*  
*City of Grand Forks Employee Pension Plan*  
*City of Bismarck Police Pension Plan*  
*Park District City of Grand Forks Pension Plan*  
*Job Service of North Dakota*

### Separate Funds (\$3.6 billion)

*Legacy Fund*  
*PERS Retiree Health Insurance Fund*  
*ND Tobacco Prevention & Control Trust Fund*

### Insurance Trust (\$2.5 billion)

*Workforce Safety and Insurance (WSI)*  
*Budget Stabilization Fund (BSF)*  
*City of Fargo FargoDome Permanent Trust*  
*PERS Group Insurance Account*  
*State Fire and Tornado Fund*  
*Petroleum Tank Release Compensation Fund*  
*State Risk Management Fund*  
*State Risk Management Workers Comp. Fund*  
*North Dakota Association of Counties Fund*  
*State Bonding Fund*  
*North Dakota Board of Medical Examiners*  
*Insurance Regulatory Trust Fund*  
*Bismarck Deferred Sick Leave Account*  
*Cultural Endowment Fund*

As of December 31, 2015, the SIB and RIO administered the external investment management of approximately \$10.8 billion in assets for 24 governmental agencies including TFFR and PERS within the \$4.7 billion Pension Trust, WSI and BSF within the \$2.5 billion Insurance Trust, and the \$3.5 billion Legacy Fund. I firmly believe the SIB and RIO have provided prudent investment management over the years noting that the SIB has

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been successful in using active management to enhance our client's returns by over \$200 million in the last 5 years (after deducting management fees). This additional income is on top of returns generated if we were only investing in passive benchmarks or index investments.

### RIO Investment Mission Statement

RIO exists in order that:

- 1) SIB clients receive investment returns, consistent with their written investment policies and market variables, in a cost effective investment manner and under the Prudent Investor Rule.
- 2) Potential clients have access to information regarding the investment services offered by the SIB.
- 3) SIB clients and TFFR benefit recipients receive satisfactory services from the boards and RIO.

### RIO Investment Performance Review

In order to determine if SIB clients are receiving investment returns consistent with their written investment policies and market variables, RIO reviews each client's actual and expected investment performance with the SIB each quarter. An outside investment consultant also conducts a quarterly investment performance review to provide further assurance that reported investment results are being achieved, while adhering to approved risk levels and that actual asset allocation levels are consistent with stated targets. After conducting the above review procedures, I am pleased to report that every Pension Trust client generated actual investment results which exceeded their respective performance benchmarks for the 1, 3, and 5 year periods ended December 31, 2015. I am also pleased to report that these above benchmark returns were achieved while adhering to approved risk

levels. As a result, the SIB has been successful in using active management to enhance returns of our Pension Trust clients by over \$90 million in the last 5 years.

### Investment Management Fee Savings Initiatives

The SIB and RIO have been successful in reducing investment management fees in recent years. During the last two fiscal years, investment fees have declined from 0.65% to 0.47%. Based on \$10 billion of assets, this translates into \$17 million of annual fee savings.

### SIB Client Satisfaction Survey

Client satisfaction surveys conducted by our audit services team confirm that the SIB is meeting the expectations of our clients. The overall client satisfaction survey rating was a 3.7 based on a 4.0 scale (4.0 = Excellent and 3.0 = Above Average). This is the second consecutive year the SIB received a client survey rating well above average.

### RIO Website Transparency Enhancements

RIO recently completed a transparency enhancement initiative in order to make it easier for interested parties to gain access to information on our website (including quarterly investment performance reviews). The following documents can be accessed at the RIO website under "SIB Board" and "SIB Audit."

- The SIB Governance Manual [www.nd.gov/rio/SIB/Board/GovernanceManual/default.htm](http://www.nd.gov/rio/SIB/Board/GovernanceManual/default.htm)
- SIB meeting materials [www.nd.gov/rio/SIB/Board/SIB%20Meeting%20Materials/default.htm](http://www.nd.gov/rio/SIB/Board/SIB%20Meeting%20Materials/default.htm)
- SIB's Audit Charter and SIB Audit Committee meeting materials [www.nd.gov/rio/SIB%20Audit/Board/default.htm](http://www.nd.gov/rio/SIB%20Audit/Board/default.htm)

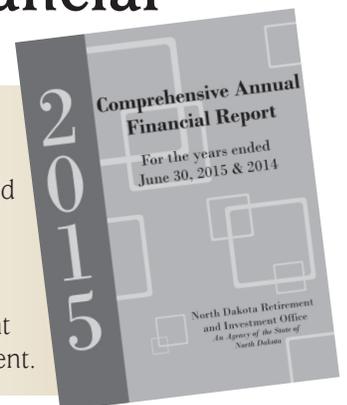
RIO staff can be reached at 701-328-9885, 800-952-2970, or via email at [djhunter@nd.gov](mailto:djhunter@nd.gov).

## Annual Audit Completed

The 2015 financial statements of the North Dakota Retirement and Investment Office received an unqualified audit opinion from the independent audit firm of CliftonLarsonAllen, LLP. There were no exceptions, recommendations, or findings in the report. The final audit report can be viewed from our website, [www.nd.gov/rio](http://www.nd.gov/rio).

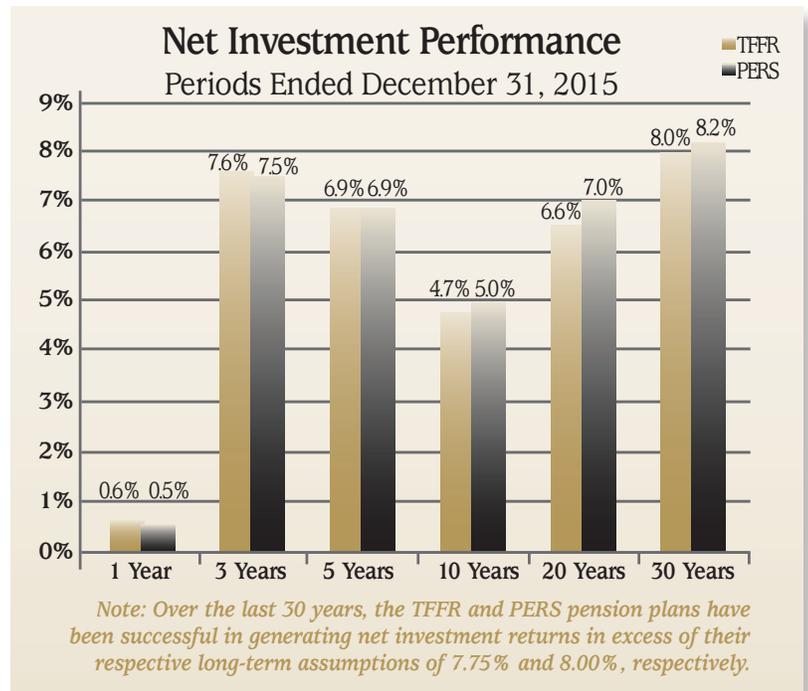
## 2015 Annual Financial Report Available

The North Dakota Retirement and Investment Office Comprehensive Annual Financial Report (CAFR) has been published and may be viewed from our website, [www.nd.gov/rio](http://www.nd.gov/rio). This report is a complete review of the financial, investment, and actuarial conditions of the State Investment Board and the Teachers' Fund for Retirement.



# PERS and TFFR Investment Performance

PERS and TFFR generated net investment returns just over 0.5% in CY2015 due to weak conditions in the global equity and debt markets which declined by 1% to 3%. U.S. equity and debt benchmarks performed slightly better and ranged from 1.4% for the S&P 500 to 0.5% for the Barclays Aggregate index (which is a widely used market benchmark for fixed income returns). Slowing global growth rates and escalating economic uncertainty were two of the major themes impacting investment results. As example, U.S. Gross Domestic Product (GDP) growth rates have declined from over 3% in prior years (from 1947 until 2015) to less than 2% during the last half of 2015. Global commodity prices fell sharply as a result of growing supply and demand imbalances, particularly in the energy sector, which has contributed to declining investor optimism and increased market volatility. Despite generally improving U.S. labor market conditions and an incredibly accommodating monetary policy,



global GDP growth rates remain below expectations. On a positive note, real estate was the best performing sector posting a 14% return in CY2015.

## Asset Allocation Primary Driver of Returns

Successful active management results when the SIB selects a team of investment managers which outperform an underlying benchmark index. For the one-year period ended December 31, 2015, active management improved TFFR and PERS net investment returns by 0.47%. Based on \$4.4 billion of combined investments for TFFR and PERS, this translates into over \$20 million of incremental income for the two retirement plans in the last calendar year.

### TFFR and PERS Asset Allocation Targets

	TFFR	PERS
<b>Global Equity</b>	<b>58%</b>	<b>57%</b>
Public	52%	52%
Private	6%	5%
<b>Global Fixed Income</b>	<b>23%</b>	<b>22%</b>
Investment Grade	19%	17%
Private	4%	5%
<b>Global Real Assets</b>	<b>18%</b>	<b>20%</b>
Real Estate	10%	10%
Infrastructure / Timber	8%	10%
<b>Cash Equivalents</b>	<b>1%</b>	<b>1%</b>
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>

TFFR and PERS review their investment policy statements on a regular basis. TFFR recently completed this review process and the TFFR board and SIB recently approved the following investment policy statement modifications:

- TFFR's investment return assumption was reduced from 8.0% to 7.75% effective July 1, 2015, based on TFFR's 2015 Actuarial Experience Study completed by Segal Consultants.
- Based on the results of an Asset Allocation Study completed by Callan Associates, TFFR's asset allocation was revised to reflect a 1% increase to global equity, a 1% increase to global fixed income, and a 2% decrease to global real assets.

RIO intends to implement TFFR's revised asset allocation policy during the second quarter of CY2016. PERS intends to conduct its investment policy statement review during this same time frame.



**NORTH DAKOTA  
RETIREMENT AND  
INVESTMENT OFFICE**  
*Teachers' Fund for Retirement  
State Investment Board*

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BISMARCK, ND  
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## TFFR and PERS Peer Performance

*TFFR and PERS net investment returns have outperformed most other U.S. public pension plans over the last 5-years.*

TFFR and PERS net returns have generally outperformed other U.S. public pension plans for the 1, 3, and 5 year periods ended December 31, 2015. This peer group comparison is based on Callan's U.S. Public Pension Database for plans which report net investment returns. The bar chart highlights net investment returns of over 100 peers noting that TFFR (A) was ranked in the 34th percentile, while PERS (B) was ranked in the 33rd percentile, for the "Last 5 Years." As a result, TFFR and PERS net investment return outperformed 66% and 67% of the other public pension plans during this period. The SIB and RIO have historically placed greater emphasis on 5 year performance metrics as shorter time periods may be overly impacted by one or two quarters of abnormal returns which are not reflective of longer-term strategic return expectations. Please note

that the "Member Count" of only 10 for the "Last 30 Years" makes it less meaningful than the other reporting periods in which the "Member Count" is 70 or more. The chart is based on unaudited valuations which are deemed to be materially accurate. RIO's financial results are audited annually with a June 30 fiscal year end.

