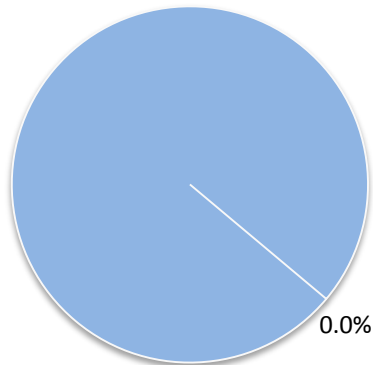


FY19 Budget Briefing

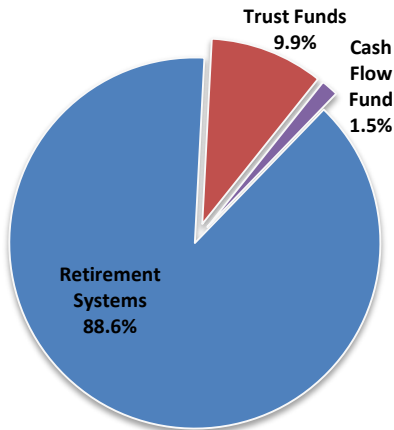
State Investment Council

Information contained in this document is based on the Governor's original FY19 recommended budget.
This document may not correspond with the final FY19 budget adopted by the Legislature.

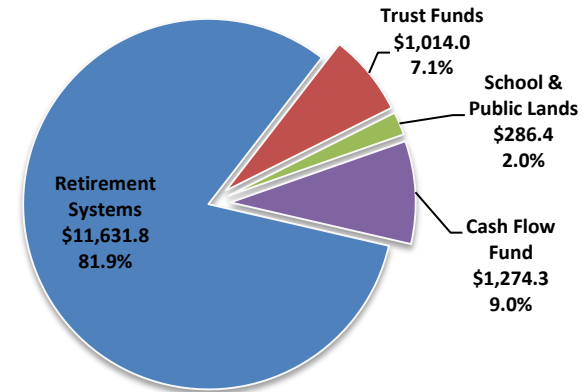
Agency Share of Budgeted GF



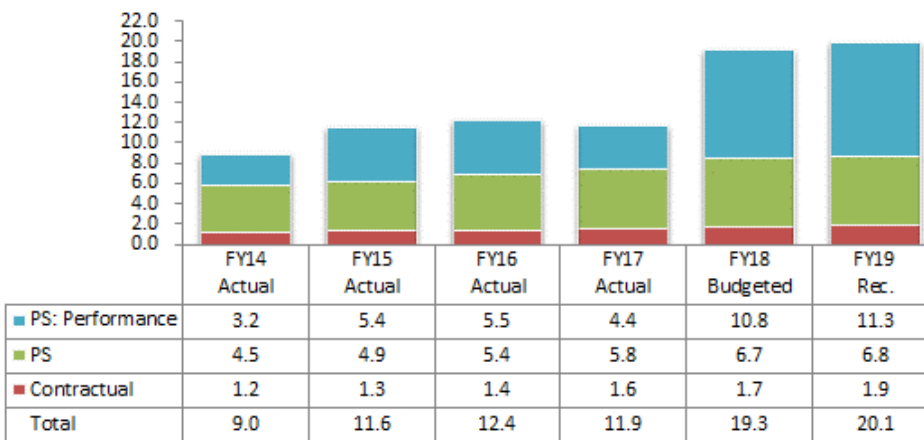
Source of Other Funds



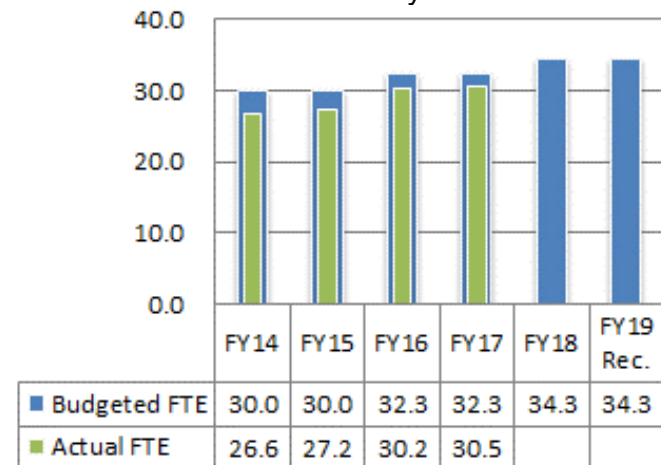
Assets Managed as of June 30, 2017 (millions)



Budget History (millions)



FTE History



KEY PERSONNEL

- Matthew L. Clark, State Investment Officer
- Christopher L. Nelson, Assistant Investment Officer
- Laurie A. Riss, Business Manager
- Brett D. Fligge, Assistant Investment Officer
- Tammy V. Otten, Assistant Investment Officer

MISSION OF THE STATE INVESTMENT COUNCIL

To manage the South Dakota Retirement System assets in order to obtain maximum long-term total returns consistent with prudent risk; to manage the state's cash flow fund in order to obtain maximum long-term total returns consistent with the liquidity needs of the fund, the legal list and prudent risk; to manage the investment portfolios of the School and Public Lands Fund, the Dakota Cement Trust, the Health Care Trust and the Education Enhancement Trust to obtain the highest risk adjusted return over the long term and to provide income payouts; to determine investment options for the 457 deferred compensation savings plan; and to establish and oversee the Higher Education Savings Plan.

STATE INVESTMENT COUNCIL BUDGET REQUEST

	FY 2016 Actual	FY 2017 Actual	FY 2018 Budget	FY 2019 Agency Request	FY 2019 Governors Recommended	Change From FY 2018
BY PROGRAM						
Investment of State Funds	6,907,849	7,468,101	8,532,631	8,889,009	8,798,068	265,437
Performance Based Compensation	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
Total	12,379,483	11,865,360	19,299,621	20,191,065	20,100,124	800,503
BY FUND CATEGORY						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	12,379,483	11,865,360	19,299,621	20,191,065	20,100,124	800,503
Total	12,379,483	11,865,360	19,299,621	20,191,065	20,100,124	800,503
BY OBJECT EXPENDITURE						
Personnel Costs	10,873,430	10,194,121	17,435,245	18,196,177	18,105,236	669,991
Salaries	9,455,081	8,798,392	15,079,917	15,748,356	15,668,443	588,526
Benefits	1,418,350	1,395,729	2,355,328	2,447,821	2,436,793	81,465
Operating Expenditures	1,506,053	1,671,240	1,864,376	1,994,888	1,994,888	130,512
Travel	68,001	66,817	85,000	85,000	85,000	0
Contractual Services	1,386,011	1,560,584	1,726,123	1,860,368	1,860,368	134,245
Supplies and Materials	7,662	5,953	12,733	9,000	9,000	(3,733)
Grants and Subsidies	0	0	0	0	0	0
Capital Outlay	44,380	37,885	40,520	40,520	40,520	0
Other	0	0	0	0	0	0
Total	12,379,485	11,865,360	19,299,621	20,191,065	20,100,124	800,503
Full-Time Equivalent (FTE)	30.3	30.5	34.3	34.3	34.3	0.0

MAJOR ITEMS SUMMARY: STATE INVESTMENT COUNCIL

	Agency Request			Governor's Recommendation		
	General	Total	FTE	General	Total	FTE
FY 2019 Base Budget	0	19,299,621	34.3	0	19,299,621	34.3
Maintenance of Current Operations Adjustments						
A. Contract Inflation	0	7,975	0.0	0	7,975	0.0
B. Capital Outlay One-time Expense	0	1,100	0.0	0	1,100	0.0
C. Bureau Billing Increase	0	4,090	0.0	0	4,090	0.0
D. Increase for Performance Based Employee Compensation	0	760,932	0.0	0	669,991	0.0
E. Capital Outlay Adjustment and Align Budget	0	(4,833)	0.0	0	(4,833)	0.0
FY 2019 Program Maintenance Budget	0	20,068,885	34.3	0	19,977,944	34.3
Program Expansion Line Items						
1. Legal Services for Distressed Debt Investments	0	50,000	0.0	0	50,000	0.0
2. Investment Research Services	0	62,640	0.0	0	62,640	0.0
3. Add Office Space	0	9,540	0.0	0	9,540	0.0
FY 2019 Total Budget	0	20,191,065	34.3	0	20,100,124	34.3
Change from Original Appropriation	0	891,444	0.0	0	800,503	0.0
% Change from Original Appropriation	0.0%	4.6%	0.0%	0.0%	4.1%	0.0%

PREVIOUS AND CURRENT YEAR BUDGET RECAP - STATE INVESTMENT COUNCIL

		FTE	General	Federal	Other	Total
Prior Year Recap						
FY 2017 Budget		0.0	0	0	18,328,312	18,328,312
Prior Year Reversions	PS		0	0	(6,329,926)	(6,329,926)
Prior Year Reversions	OE		0	0	(133,025)	(133,025)
Unutilized FTE		(1.8)				
FY 2017 Percent Reverted or Transferred		5.5%	0	0	(35.3%)	(35.3%)
Current Year Recap						
FY 2018 Budget		34.3	0	0	19,297,249	19,297,249
Health Insurance	PS		0	0	2,573	2,573
Bureau Billings	OE		0	0	(201)	(201)
FY 2018 Estimated Expenditures		34.3	0	0	19,299,621	19,299,621

Investment of State Funds (3210)

To manage the South Dakota Retirement System assets in order to obtain maximum long-term total returns consistent with prudent risk; to manage the state's cash flow fund in order to obtain maximum long-term total returns consistent with the liquidity needs of the fund, the legal list and prudent risk; to manage the investment portfolios of the School and Public Lands Fund, the Dakota Cement Trust, the Health Care Trust and the Education Enhancement Trust to obtain the highest risk adjusted return over the long term and to provide income payouts; to determine investment options for the 457 deferred compensation savings plan; and to establish and oversee the Higher Education Savings Plan.

Budget Request: Investment of State Funds (3210)

	FY 2016 Actual	FY 2017 Actual	FY 2018 Budget	FY 2019 Agency Request	FY 2019 Governors Recommended	Change From FY 2018
BY PROGRAM						
Investment of State Funds	6,907,849	7,468,101	8,532,631	8,889,009	8,798,068	265,437
Total	6,907,849	7,468,101	8,532,631	8,889,009	8,798,068	265,437
BY FUND CATEGORY						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	6,907,849	7,468,101	8,532,631	8,889,009	8,798,068	265,437
Total	6,907,849	7,468,101	8,532,631	8,889,009	8,798,068	265,437
BY OBJECT EXPENDITURE						
Personnel Costs	5,401,796	5,796,862	6,668,255	6,894,121	6,803,180	134,925
Salaries	4,553,427	4,881,330	5,618,590	5,816,848	5,736,935	118,345
Benefits	848,370	915,531	1,049,665	1,077,273	1,066,245	16,580
Operating Expenditures	1,506,053	1,671,240	1,864,376	1,994,888	1,994,888	130,512
Travel	68,001	66,817	85,000	85,000	85,000	0
Contractual Services	1,386,011	1,560,584	1,726,123	1,860,368	1,860,368	134,245
Supplies and Materials	7,662	5,953	12,733	9,000	9,000	(3,733)
Grants and Subsidies	0	0	0	0	0	0
Capital Outlay	44,380	37,885	40,520	40,520	40,520	0
Other	0	0	0	0	0	0
Total	6,907,851	7,468,100	8,532,631	8,889,009	8,798,068	265,437
Full-Time Equivalent (FTE)	30.3	30.5	34.3	34.3	34.3	0.0

Major Items Summary: Investment of State Funds (3210)

	Agency Request			Governor's Recommendation		
	General	Total	FTE	General	Total	FTE
FY 2019 Base Budget	0	8,532,631	34.3	0	8,532,631	34.3
Maintenance of Current Operations Adjustments						
A. Contract Inflation	0	7,975	0.0	0	7,975	0.0
B. Capital Outlay One-time Expense	0	1,100	0.0	0	1,100	0.0
C. Bureau Billing Increase	0	4,090	0.0	0	4,090	0.0
D. Increase for Performance Based Employee Compensation	0	225,866	0.0	0	134,925	0.0
E. Capital Outlay Adjustment and Align Budget	0	(4,833)	0.0	0	(4,833)	0.0
FY 2019 Program Maintenance Budget	0	8,766,829	34.3	0	8,675,888	34.3
Program Expansion Line Items						
1. Legal Services for Distressed Debt Investments	0	50,000	0.0	0	50,000	0.0
2. Investment Research Services	0	62,640	0.0	0	62,640	0.0
3. Add Office Space	0	9,540	0.0	0	9,540	0.0
FY 2019 Total Budget	0	8,889,009	34.3	0	8,798,068	34.3
Change from Original Appropriation	0	356,378	0.0	0	265,437	0.0
% Change from Original Appropriation	0.0%	4.2%	0.0%	0.0%	3.1%	0.0%

Budget Detail: Investment of State Funds (3210)

		FTE	General	Federal	Other	Total
Prior Year Recap						
FY 2017 Budget		32.3	0	0	8,175,588	8,175,588
Prior Year Reversions	PS		0	0	(574,461)	(574,461)
Prior Year Reversions	OE		0	0	(133,025)	(133,025)
Unutilized FTE		(1.8)				
FY 2017 Percent Reverted or Transferred		5.5%	0	0	(8.7%)	(8.7%)
Current Year Recap						
FY 2018 Budget		34.3	0	0	8,530,259	8,530,259
Health Insurance	PS		0	0	2,573	2,573
Bureau Billings	OE		0	0	(201)	(201)
FY 2018 Estimated Expenditures		34.3	0	0	8,532,631	8,532,631
FY 2019 Base						
Agency Request		34.3	0	0	8,532,631	8,532,631
Governor's Recommendation		34.3	0	0	8,532,631	8,532,631

	FTE	General	Federal	Other	Total
Current Year Recap					
A. Contract Inflation					
The agency requested an increase of \$7,975 in other funds because of a 2% increase from the bank custodian for the custody of assets. <i>The Governor recommends this request.</i>					
Agency Request	0.0	0	0	7,975	7,975
Governor's Recommendation	0.0	0	0	7,975	7,975
B. Capital Outlay One-time Expense					
The agency requested \$1,100 in other funds to upgrade a printer. This request nets to \$0 because of a reduction of \$1,100 in capital outlay. <i>The Governor recommends this request.</i>					
Agency Request	0.0	0	0	1,100	1,100
Governor's Recommendation	0.0	0	0	1,100	1,100
C. Bureau Billing Increase					
The agency requested an increase of \$4,090 in other funds with \$3,700 for printer maintenance contracts through BIT and \$390 for increases to liability insurance. <i>The Governor recommends this request.</i>					
Agency Request	0.0	0	0	4,090	4,090
Governor's Recommendation	0.0	0	0	4,090	4,090
D. Increase for Performance Based Employee Compensation					
The agency requested an increase of \$225,866 in other funds for base salary and promotional increases. The base salaries budget for full-time staff (not including state salary policy) increases by 3.39%. An increase of 1.75% for 28 investment positions and promotional increases of 1% to 15.2% for newer and intermediate investment team members, accountant positions, and new assistant business manager. The investment council staff does receive state salary policy, which would be in additional to the budget request. <i>The Governor recommends an increase of \$134,925 for this request.</i>					
Under the Governor's recommendation, investment positions will not receive the 1.75%. Senior investment positions would only receive the state salary policy if any.					
Agency Request	0.0	0	0	225,866	225,866
Governor's Recommendation	0.0	0	0	134,925	134,925
E. Capital Outlay Adjustment and Align Budget					
The agency requested a decrease of (\$4,833) in other funds with \$3,733 from office supplies and postage and \$1,100 related to a capital outlay adjustment. <i>The Governor recommends this request.</i>					
Agency Request	0.0	0	0	(4,833)	(4,833)
Governor's Recommendation	0.0	0	0	(4,833)	(4,833)
FY 2019 Maintenance of Current Operations					
Agency Request	34.3	0	0	8,766,829	8,766,829
Governor's Recommendation	34.3	0	0	8,675,888	8,675,888

Current Year Recap **FTE** **General** **Federal** **Other** **Total**

1. Legal Services for Distressed Debt Investments

The agency requested an increase of \$50,000 in other funds for legal services for distressed debt investments. The additional funding may be necessary for distressed debt investments if those investments were to go into bankruptcy. The legal services would help to ensure the best outcome from a potential bankruptcy. *The Governor recommends this request.*

Agency Request	0.0	0	0	50,000	50,000
Governor's Recommendation	0.0	0	0	50,000	50,000

2. Investment Research Services

The agency requested an increase of \$62,640 in other funds for investment research services. The additional funding is needed for the additional staff members added. A new investment service was added, while two others were canceled. Changes are made in investment research services according to the needs and circumstances at the time. *The Governor recommends this request.*

	Actual FY 2017	Received FY 2017	Unexpended	Received FY 2018	Request FY2019
CONTRACTUAL SERVICES					
Investment Services					
Consulting Services	0	30,000	30,000	30,000	80,000
Investment Accounting, Performance Benchmarking	98,275	106,000	7,725	106,000	113,100
Investment Databases, Newsfeeds & Quote Fees	510,313	517,336	7,023	547,436	553,636
Investment Research Services	279,124	293,185	14,061	338,185	387,525
Flexibility - From Brokerage to Independent Research	115,000	120,000	5,000	100,000	100,000
Total Investment Services	1,002,713	1,066,521	63,808	1,121,621	1,234,261
Administrative Expenses					
Office Rent	125,069	125,069	(0)	125,069	134,609
Bond/Liability Insurance	2,700	7,800	5,100	7,800	8,190
Telephone	15,769	14,000	(1,769)	18,000	18,000
Office Equip Rental/Maintenance	4,847	6,056	1,209	6,000	6,000
Bureau of Info & Telecommunications (BIT)	57,916	61,454	3,538	65,300	69,000
State Central Services	11,579	11,698	119	12,799	12,799
Legislative Audit	45,490	51,500	6,010	51,500	51,500
Attorney General's Office - Legal Services	0	18,509	18,509	18,509	18,509
Custodial Fees - Global	260,381	263,025	2,644	263,025	271,000
Seminars/Educational Programs	32,954	33,500	546	33,500	33,500
Business Publications	1,167	3,000	1,833	3,000	3,000
Total Administrative Expenses	557,872	595,611	37,739	604,502	626,107
TOTAL CONTRACTUAL SERVICES	1,560,584	1,662,132	101,548	1,726,123	1,860,368

Agency Request	0.0	0	0	62,640	62,640
Governor's Recommendation	0.0	0	0	62,640	62,640

	FTE	General	Federal	Other	Total
Current Year Recap					
3. Add Office Space					
The agency requested an increase of \$9,540 in other funds to add office space at their current location. The additional 600 sq. ft. of office space will be used to accommodate staff members. The agency has filled the two new FTE positions, as well as a vacant position, and they will begin full-time in May of 2018. The space will also allow for interns in the future, which otherwise there would not be room for. <i>The Governor recommends this request.</i>					
Agency Request	0.0	0	0	9,540	9,540
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>9,540</i>	<i>9,540</i>
FY 2019 Total					
Agency Request	34.3	0	0	8,889,009	8,889,009
<i>Governor's Recommendation</i>	<i>34.3</i>	<i>0</i>	<i>0</i>	<i>8,798,068</i>	<i>8,798,068</i>
Agency Request					
Change from Original Appropriation	0.0	0	0	356,378	356,378
% Change from Original Appropriation	0.0%	0.0%	0.0%	4.2%	4.2%
<i>Governor's Recommendation</i>					
<i>Change from Original Appropriation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>265,437</i>	<i>265,437</i>
<i>% Change from Original Appropriation</i>	<i>0.0%</i>	<i>0.0%</i>	<i>0.0%</i>	<i>3.1%</i>	<i>3.1%</i>

Performance Based Compensation (3211)

To focus on adding value over the long term in all financial market conditions and to motivate and retain successful investment team members by linking a portion of total compensation to investment return performance relative to benchmarks.

Budget Request: Performance Based Compensation (3211)

	FY 2016 Actual	FY 2017 Actual	FY 2018 Budget	FY 2019 Agency Request	FY 2019 Governors Recommended	Change From FY 2018
BY PROGRAM						
Performance Based Compensation	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
Total	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
BY FUND CATEGORY						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
Total	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
BY OBJECT EXPENDITURE						
Personnel Costs	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
Salaries	4,901,654	3,917,062	9,461,327	9,931,508	9,931,508	470,181
Benefits	569,980	480,197	1,305,663	1,370,548	1,370,548	64,885
Operating Expenditures	0	0	0	0	0	0
Travel	0	0	0	0	0	0
Contractual Services	0	0	0	0	0	0
Supplies and Materials	0	0	0	0	0	0
Grants and Subsidies	0	0	0	0	0	0
Capital Outlay	0	0	0	0	0	0
Other	0	0	0	0	0	0
Total	5,471,634	4,397,259	10,766,990	11,302,056	11,302,056	535,066
Full-Time Equivalent (FTE)	0.0	0.0	0.0	0.0	0.0	0.0

Major Items Summary: Performance Based Compensation (3211)

	Agency Request			Governor's Recommendation		
	General	Total	FTE	General	Total	FTE
FY 2019 Base Budget	0	10,766,990	0.0	0	10,766,990	0.0
Maintenance of Current Operations Adjustments						
A. Increase for Performance Based Employee Compensation	0	535,066	0.0	0	535,066	0.0
FY 2019 Program Maintenance Budget	0	11,302,056	0.0	0	11,302,056	0.0
Program Expansion Line Items						
FY 2019 Total Budget	0	11,302,056	0.0	0	11,302,056	0.0
Change from Original Appropriation	0	535,066	0.0	0	535,066	0.0
% Change from Original Appropriation	0.0%	5.0%	0.0%	0.0%	5.0%	0.0%

Budget Detail: Performance Based Compensation (3211)

Prior Year Recap		FTE	General	Federal	Other	Total
FY 2017 Budget		0.0	0	0	10,152,724	10,152,724
Prior Year Reversions	PS		0	0	(5,755,465)	(5,755,465)
Unutilized FTE		0.0				
FY 2017 Percent Reverted or Transferred		0	0	0	(56.7%)	(56.7%)

Current Year Recap		FTE	General	Federal	Other	Total
FY 2018 Budget		0.0	0	0	10,766,990	10,766,990
FY 2018 Estimated Expenditures		0.0	0	0	10,766,990	10,766,990

FY 2019 Base		FTE	General	Federal	Other	Total
Agency Request		0.0	0	0	10,766,990	10,766,990
Governor's Recommendation		0.0	0	0	10,766,990	10,766,990

A. Increase for Performance Based Employee Compensation

The agency requested an increase of \$535,066 in other funds for performance based employee compensation. The Investment Council targets 70% of the cost-of-living adjusted private sector median for investment positions' total compensation, including average expected incentives. The incentive plan includes funding for potential maximum incentives up to 200% of FY2018 base salaries of investment positions. Incentives are rewarded for outperformance and range from 0% to 200%. *The Governor recommends this request.*

Agency Request		0.0	0	0	535,066	535,066
Governor's Recommendation		0.0	0	0	535,066	535,066

FY 2019 Maintenance of Current Operations

Agency Request		0.0	0	0	11,302,056	11,302,056
Governor's Recommendation		0.0	0	0	11,302,056	11,302,056

FY 2019 Total

Agency Request		0.0	0	0	11,302,056	11,302,056
Governor's Recommendation		0.0	0	0	11,302,056	11,302,056

Agency Request						
Change from Original Appropriation		0.0	0	0	535,066	535,066
% Change from Original Appropriation		0.0%	0.0%	0.0%	5.0%	5.0%

Governor's Recommendation						
Change from Original Appropriation		0.0	0	0	535,066	535,066
% Change from Original Appropriation		0.0%	0.0%	0.0%	5.0%	5.0%

TRUST FUNDS

Health Care Trust (established April 2001)

		<u>Asset Allocation</u>	<u>Current</u>	<u>FY 17 Benchmark</u>
Principal as of 6/30/17	\$ 85,631,024	Global Equity	32%	51%
Principal as of 6/30/17 adjusted for inflation	\$ 115,247,435	Private Equity	4%	0%
Fair Value (FV) as of 6/30/17	\$ 143,034,115	Real Estate	7%	10%
Difference - FV less principal	\$ 57,403,091	Fixed Income-IG	20%	30%
Difference - FV less infl. adj. prin.	\$ 27,786,680	Fixed Income-HY	5%	7%
		HY RE Debt	6%	0%
Fiscal year to date return	11.58%	Money Market	26%	2%
Longterm expected mean return	5.86%	Total	100%	100%
Payout of 4% plus expected inflation of 3%	7.00%			
Expected return cushion/shortfall	-1.14%			

Distribution for FY 18 (July 1, 2017)	5,214,739
Distribution for FY 17 (July 1, 2016)	4,970,123

Law allows up to 4% of the 16 quarter average to be distributed as long as principal is not violated as of December 31 each year.

Education Enhancement Trust (established April 2001)

		<u>Asset Allocation</u>	<u>Current</u>	<u>FY 17 Benchmark</u>
Principal as of 6/30/17	\$ 366,546,780	Global Equity	34%	51%
Principal as of 6/30/17 adjusted for inflation	\$ 482,001,898	Private Equity	3%	0%
Fair Value (FV) as of 6/30/17	\$ 554,492,395	Real Estate	7%	10%
Difference - FV less principal	\$ 187,945,615	Fixed Income-IG	9%	20%
Difference - FV less infl. adj. prin.	\$ 72,490,497	Fixed Income-tax e:	8%	10%
		Fixed Income-HY	4%	7%
Fiscal year to date return	11.52%	HY RE Debt	6%	0%
Longterm expected return (lower due to tax-exempts)	5.81%	Money Market	28%	2%
Payout of 4% plus expected inflation of 3%	7.00%	Total	100%	100%
Expected return cushion/shortfall	-1.19%			

Distribution for FY 18 (July 1, 2017)	19,377,842
Distribution for FY 17 (July 1, 2016)	18,242,854

Law allows up to 4% of the 16 quarter average to be distributed as long as principal is not violated as of December 31 each year.

Dakota Cement Trust (established April 2001)

		<u>Asset Allocation</u>	<u>FY 17</u>	
			<u>Current</u>	<u>Benchmark</u>
Principal as of 6/30/17	\$ 238,000,000	Global Equity	34%	51%
Principal as of 6/30/17 adjusted for inflation	\$ 328,178,846	Private Equity	4%	0%
Fair Value (FV) as of 6/30/17	\$ 316,483,727	Real Estate	7%	10%
Difference - FV less principal	\$ 78,483,727	Fixed Income-IG	20%	30%
Difference - FV less infl. adj. principal	\$ (11,695,119)	Fixed Income-HY	5%	7%
		HY RE Debt	7%	0%
Fiscal year to date return	11.55%	Money Market	24%	2%
Longterm expected mean return	5.86%	Total	100%	100%
Payout of 4% plus expected inflation of 3%	7.00%			
Expected return cushion/shortfall	-1.14%			

Constitution allows 4% of the lesser of 1) the 16 quarter average balance or 2) the current December 31 fair value, be distributed by June of the following year.

Distribution for FY 17 (May 2017 to GF)	11,981,721
Distribution for FY 16 (May 2016 to GF)	11,436,003

School & Public Lands

Inflation protection mandated by Constitutional Amendment - (payout is reduced by inflation to extent inflation not offset by realized net gains)		<u>Asset Allocation</u>	<u>FY 17</u>	
			<u>Current</u>	<u>Benchmark</u>
Fair Value as of 6/30/17	\$ 286,383,911	Global Equity	35%	51%
Fiscal year to date return	11.68%	Private Equity	3%	0%
Longterm expected mean return	5.86%	Real Estate	7%	10%
Distribution for FY 17 K-12 (2/7/17)	10,196,471	Fixed Income-IG	18%	30%
Distribution for FY 17 Board of Regents (6/8/17)	<u>2,409,329</u>	Fixed Income-HY	5%	7%
		HY RE Debt	6%	0%
		Money Market	26%	2%
TOTAL	12,605,800	Total	100%	100%

HISTORICAL UNIT COST

	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017</u>
UNIT COST - NORMALIZED (using expected incentives & adjusted assets)				
Internal Expenses as % of Total Assets (target .10%)	0.072%	0.091%	0.088%	0.093%
Total Expenses as % of Total Assets	0.382%	0.387%	0.352%	0.341%
UNIT COST - ACTUAL (using actual expenses & assets)				
Internal Expenses as % of Total Assets	0.074%	0.088%	0.094%	0.087%
Total Expenses as % of Total Assets*	0.300%	0.165%	0.289%	0.269%

*Outside manager expenses vary based on the amount and stage of life cycle of investments in limited partnerships

INTERNAL MANAGEMENT

- Cost of managing assets internally is lower than external active managers
 - Savings come from compensation discount, lack of marketing cost, cheaper facilities and other frugalities, and no need to make a profit or pay corporate income taxes
 - Cost efficiency study indicates we are among the lowest cost funds for our size and type of assets
 - Index funds are also low in cost but preclude any opportunity to add value above indexes
- SDIC's long-term history suggests managing assets internally can increase returns
 - Key reason is greater influence over internal staff to focus on long-term value
 - Our experience suggests most investors lack patience. Most managers recognize they will not be allowed a long timeframe for investment decisions to prove out, thus chase short-term results
 - Increased conviction comes from doing your own work
- Difficulty is that internal management is a lot more work than hiring outside managers
 - Requires internal research capability – requires expensive higher skilled people
 - Must build and maintain support for investment process – difficult in tough markets
 - Staff compensation attracts criticism – must periodically explain outsourcing would cost far more
- Asset categories managed internally
 - Global Equity (domestic since 1974, international since 1992, merged in 2004)
 - Fixed Income (since 1973)
 - High Yield Debt (since 1977), Distressed Corporate Debt (since 2009)
 - Asset Allocation Shift (since 1986)
 - Merger Arbitrage (since 1990) & Convertible Arbitrage (since 1993)

USE OF EXTERNAL MANAGERS

- Investment categories the Investment Office does not manage internally
 - Real Estate – requires specialized real estate management expertise
 - Private Equity – requires hands-on business management expertise
 - Distressed residential mortgages – requires house and servicer level databases
- Educational relationships in areas with an internal capability
 - Global Equity – to interact with firms on our internal “smart investor” list
 - Distressed corporate debt – interaction while enhancing internal capabilities
 - Research and ideas from outside firms can supplement our own research efforts
 - Interaction with leading firms helps identify best practices to aid our process
- Select highly respected managers with successful long-term track records
 - Investment team-driven approach has avoided hiring scandals common elsewhere

INVESTMENT COUNCIL PROVIDED FY2019 BUDGET REQUEST SUMMARY

	Received FY 2018	FY 2019 Budget Request	% chng	FY 2019 Gov Recommend	% chng
PERSONAL SERVICES					
TOTAL FTEs	34.25	34.25		34.25	
BASE COMPENSATION					
Base Compensation - Investment Staff	4,965,754	5,154,064	3.79%	5,074,151	2.18%
Base Comp - Accounting, Admin & Longevity	428,982	438,930	2.32%	438,930	2.32%
TOTAL STAFF - FULL TIME	5,394,736	5,592,994	3.68%	5,513,081	2.19%
P/T Staff Attorney & Interns	62,527	62,526	0.00%	62,526	0.00%
Investment Council	6,227	6,227	0.00%	6,227	0.00%
Retirement & resignation flexibility funds	155,100	155,100	0.00%	155,100	0.00%
Benefits	1,049,665	1,077,274	2.63%	1,066,246	1.58%
Total Base Compensation	6,668,255	6,894,121	3.39%	6,803,180	2.02%
Investment Performance Incentives					
Maximum Potential Investment Perf Incentive	9,461,327	9,931,508	4.97%	9,931,508	4.97%
Benefits	1,305,663	1,370,548	4.97%	1,370,548	4.97%
Total Investment Performance Incentives	10,766,990	11,302,056	4.97%	11,302,056	4.97%
Total Personal Services	17,435,245	18,196,177	4.36%	18,105,235	3.84%
OPERATING EXPENSES					
Contractual Total (see next page for further details)	1,726,123	1,860,368	7.78%	1,860,368	7.78%
Travel	85,000	85,000	0.00%	85,000	0.00%
Office Supplies & Postage	12,733	9,000	-29.32%	9,000	-29.32%
Capital Assets	40,520	40,520	0.00%	40,520	0.00%
Total Operating Expenses	1,864,376	1,994,888	7.00%	1,994,888	7.00%
TOTAL BUDGET	19,299,621	20,191,065	4.62%	20,100,123	4.15%
UNIT COST SUMMARY *					
Internal Expenses as % of Total Adjusted Assets	0.094%	0.094%		0.093%	
Total Expenses as % of Total Adjusted Assets	0.341%	0.341%		0.341%	

* Based on total assets adjusted to long-term value and expenses using assumed average investment performance incentives

AGENCY FUNDING SOURCES

FY19 Funding Sources	TOTAL
3017 - INVESTMENT COUNCIL OPERATING	20,100,124
Grand Total	20,100,124

OTHER FUND BALANCE HISTORY

Company	60 Month Average	Minimum Balance	Most Recent Occurrence of Minimum	Balance on June 30				
				2017	2016	2015	2014	2013
3017 - INVESTMENT OF STATE FUNDS	3,441,025	(115,382)	August 2013	1,929,561	1,894,306	3,865,242	1,247,180	1,043,941
8000 - INVESTMENT OF STATE FUNDS	8,869,570	708,303	July 2013	15,854,764	17,793,314	16,448,082	8,621,677	11,736,137

HISTORICAL BUDGET CHANGES

<u>Investment Council</u>	General Funds	Federal Funds	Other Funds	Total Funds	FTEs
FY13 Budget Increases					
• Base Salaries and Performance Incentives			264,410	264,410	
• Employee Benefits			50,153	50,153	
• Other Operating Expenses			78,782	78,782	
• BIT Career Banding			935	935	
FY14 Budget Increases					
• Personal Services- Base Salary Increase According to Long Term Plan & 2 New FTEs			519,707	519,707	2.0
• Performance Based Compensation			803,485	803,485	
FY15 Budget Increases					
• Personal Services - Base Salaries and Benefits			289,920	289,920	
• Miscellaneous Operating Expenses			115,560	115,560	
• Performance Based Compensation			4,624,945	4,624,945	
FY16 Budget Increases					
• Two New Research Analysts			147,454	147,454	2.0
• Part Time Staff Attorney			32,456	32,456	0.3
• Base Salary and Promotional Increases			291,943	291,943	
• Miscellaneous Contractual Services			41,855	41,855	
• Capital Outlay			4,192	4,192	
• Performance Based Compensation			796,804	796,804	

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Investment Council

	General Funds	Federal Funds	Other Funds	Total Funds	FTEs
FY17 Budget					
FY2017 Line Items					
• Base Salary, Promotional Increases			187,818	187,818	
• Contractual Services			50,904	50,904	
• Capital Outlay			-2,792	-2,792	
• Performance Based Compensation			1,000,708	1,000,708	
FY18 Budget					
Maintenance of Current Operation Items					
• Change in Employee Compensation			765,956	765,956	
FY2018 Line Items					
• Additional Investment FTEs			151,817	151,817	2.0
• Investment Research Services			55,100	55,100	