

**STATE OF WISCONSIN
DEPARTMENT OF EMPLOYEE TRUST FUNDS
801 West Badger Road
Madison, WI 53702**

CORRESPONDENCE MEMORANDUM

DATE: April 30, 2003

TO: Deferred Compensation Board

FROM: Pam Henning, Director
Office of Strategic Services

SUBJECT: Report on Other Investment Options

Background

At the November 2002 Deferred Compensation Board meeting, staff identified additional asset classes of investment options that could be considered for the Wisconsin Deferred Compensation (WDC) program. Staff indicated the current core spectrum offers a broad range of choices for the participants, but the Board may wish to consider other investment options that may provide additional diversification opportunities. The two areas identified were global asset allocation funds and Real Estate Investment Trusts (REIT).

The Board directed staff and the Investment Committee to review the global asset allocation funds and REITs as well as other investment choices and provide a report to the Board on its findings and recommendations.

Nationwide Retirement Solutions (NRS) completed a review of the current core investment options and presented a report to the Investment Committee at its meeting on April 22, 2003. The report identified five asset class categories that are not currently represented in the core investment options. The asset class categories identified are as follows:

- Small Cap Growth
- Small Cap Value
- Mid Cap Value
- Large Cap Value
- High Yield Bond

NRS' analysis indicated that global asset allocation funds do not provide significant risk/reward advantages in comparison to domestic hybrid (balanced) funds. The analysis also revealed that most large state Section 457 programs do not offer global asset allocation funds.

Information provided by NRS stated that even though REIT's risk/reward profile is attractive and offers diversification to the WDC program's current core spectrum, adding this option would require a change to the WDC program's current investment policy, which does not presently permit sector funds. In addition, NRS stated that adding funds from the other standard asset class categories listed above is recommended prior to adding these more nontraditional, specialty categories.

Recommendations

Staff and Investment Committee members offer the following recommendations:

1. The WDC program should proceed slowly in adding new specialty funds such as global asset allocation funds and REIT funds to the core spectrum.
2. The WDC program should monitor the performance of global asset allocation funds for the next year, and at that time the Board may ask the Investment Committee to review these fund categories again.
3. No action by the WDC Board is necessary regarding REIT funds. WDC investment policy currently prohibits addition of a sector fund such as the REIT. The Committee also noted that exposure to these funds may already exist in mutual funds under our management and that both global asset allocation funds and REITs can be selected through the self-directed brokerage option offered by the WDC program.
4. NRS should complete a review and analysis of two other fund categories, the International Bond Fund and the Small Cap Index Fund, prior to the next Investment Committee meeting this summer. The Investment Committee will review the results of NRS' analysis of these additional fund categories this summer and report back to the Board at the November 11, 2003 meeting with any recommendations.