STATE OF WISCONSIN
Department of Employee Trust Funds
David A. Stella
SECRETARY

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Madison WI 53707-7931

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CORRESPONDENCE MEMORANDUM

DATE: February 23, 2010

TO: Employee Trust Funds Board

FROM: Matt Stohr, Director, Office of Legislative Affairs, Communications, and Quality Assurance

SUBJECT: Member Correspondence

This memo is for informational purposes only. No Board action is required.

I typically enclose a sampling of member correspondence (letters and e-mails) that the Department receives from Wisconsin Retirement System (WRS) members since the previous Board meeting. As of this writing, I have not received many letters or e-mails to share with the Board. The limited number of letters and e-mails we have received, however, center on the State of Wisconsin Investment Board (SWIB). Specifically, members have contacted the Department about the Investment Board's consideration of and action on leveraging fixed income to diversify risk away from stocks. Members have also contacted us about SWIB's incentive compensation program. We sent those letters to SWIB for response. I attached a few samples for your information.

Many WRS members also contact their state representative or senator, the Governor, and/or their congressional representative or senator about WRS issues. To date, the Department has received 20 member-contacts through the Governor's office and legislators since the December Board meeting. These contacts touched on a variety of issues, including: WRS contribution rates, WRS benefits, and health and disability insurance benefits. We have responded to all of these contacts.

I will be available at the March meeting to answer any questions you may have.

Attachments

Reviewed and approved by Rhonda Dunn, Executive Assistant.

Signature ____________________ Date __________

Board	Mtg Date	Item #
ETF	3.18.10	7B

[redacted]

TO: SWLB

2/2/10

Wisconsin Department of Trust Funds
Board of Directors,

Recently (I believe it was last fall) I read an article in the newspaper about large bonuses to be given to at least some of the employees working at the Trust offices and or the investment section. As a contributor financially to the retirement program I feel the policy of large bonuses or maybe any bonuses is incorrect. When large sums of money are involved some feel they are entitled to some of the money. Lawmakers can create and pass laws but it is very difficult to effectively control greed.

I am sure the employees receive a very good salary. So far I have not heard of one contributor to the fund ever receiving any type of annual bonuses. I always thought the "Board of Directors" were the "watchdogs" of our retirement program. This mentality of giving out bonuses seems to follow the big business world of executives deserving extra compensation for whatever reason.

I received a pay cut in my monthly retirement check this year and understand another pay cut is coming in May, 2010. How can we ever pay performance bonuses when losses effect us all. Pay an attractive salary. If that pay is not enough there are always others very capable.

Enclosed is a copy of the article from the paper. I would very much appreciate a reply.

Thanks for your time,

e-mail

nothing attached 2/4/10 SL

RECEIVED
...OYEE TRUST F...
2010 FEB -4 AM 10:44

[redacted]

RECEIVED
EMPLOYEE TRUST FUNDS

2/1/10

2010 FEB -4 A 10:06

Department of Employee Trust Funds
Madison Wisconsin 53707-7931

Gentlemen:

I have received the latest Trust Fund News containing the expected Annuity returns for 2009 investments and the projected adjustment rates in my annuity. I recognize this is only an estimate. On page 6 I see where the ETF has been recognized for Pension Plan Administration from the Public Pension Coordinating Council. Somewhere in the publication I had hoped you would have included "the rest of the story". I had gone to the etf web site in early January to see if tentative returns had been arrived at. At that time the message stated it would take a little longer than normal and would be available sometime later in January. Fine. There was also an article which could be downloaded which state the fund managers would be awarded a total of 1.7 million dollars as a bonus they would get for the 2008 fund management in 2008 when they only lost (?) billion dollars in the fund which was better than most. As I recall they would not receive this bonus until 2011. Regardless I am not sure if this would be simply be in the 2010 expenses. (?) I'm not sure if this is the 4 billion I remember or if it was some other figure. I tried to look up the article again when I got the Fund news but could no longer find it. How were these bonuses arrived at and by whom? I would like to see an explanation is the next news. In my circle of teaching friends, no one was aware that these awards have been made. I have not found anyone is happy with it. We will be having our monthly retirement luncheon on Friday this week and I am sure the point will come up.

~~Sincerely,~~

2/2/10

I tried e-mailing this to you but was unsuccessful

2010 FEB -4 A 10:06

EMPLOYEE TRUST FUNDS
RECEIVED

Walk, Sharon

From:
Sent: Friday, February 05, 2010 8:52 AM
To:
Subject: FW: Concerns

Barry Hinton
Wisconsin Department of Employee Trust Funds

From:
Sent: Friday, February 05, 2010 8:51 AM
Subject: RE: Concerns

Thank you for contacting the Wisconsin Department of Employee Trust Funds. I will forward your message to the Secretary's office.
If you have further questions, please feel free to contact this Department toll free at 877-533-5020, or in Madison at 608-266-3285. You may also visit us on the web at *etf.wi.gov*.

Barry Hinton
Wisconsin Department of Employee Trust Funds

From:
Sent: Tuesday, February 02, 2010 7:48 AM
To: *ETF ETFWEB
Subject: Concerns

See article below.

Is this as bad as it sounds?
Is our retirement fund at risk with the new methodology?
Borrowing?
When is the borrowing paid back?

Stohr, Matthew

From: Vicki.Hearing [vicki.hearing@swib.state.wi.us]
Sent: Tuesday, February 23, 2010 5:31 PM
To:
Cc: Stohr, Matthew
Subject: RE: Other

Attachments: FAQ_2010_Asset_Allocation.pdf

FAQ_2010_
_Allocation.|

By sending the attached commentary, I assume that you are seeking more information about the State of Wisconsin's decision to consider leverage as part of its strategy. The proposed strategy is intended to reduce risk, not increase returns as was inferred in the article. In fact, returns may be slightly lower in good markets but better in poor markets. Removing some of the volatility should help keep contribution rates and dividends paid to retirees more stable.

Leverage is achieved in many ways. It is generally done by investing in the use of various financial instruments, such as options, futures and margin, not borrowing money. Used appropriately, leverage is an important tool for many investors. This use happens more quietly and without a lot of attention from the media.

Leverage is most commonly used in real estate transactions through the use of mortgages to purchase a home. A classic example of leverage is the standard financial arrangement of buying a house. For a home purchase with a 20% down payment, the amount borrowed, or leveraged, is 80%. The value to equity, or leverage multiple is 100% to 20%, or 5 to 1. If SWIB's proposal is fully implemented by 2012, the amount leveraged is 20%, so the leverage multiple would be 1.2 to 1. The leverage multiple of SWIB's 2010 proposal is 1.04 to 1.

None of these strategies approved by the trustees have been implemented to date and changes will be made slowly over the next 10 months but only if market conditions warrant it. If we proceed, we will use caution and move forward in small increments. The Board will review each recommendation before it is implemented.

It is important to know the WRS is 88% funded as of 2009. A report issued by PEW recently indicates that the Wisconsin pension system is one of the leaders in the nation. There is a link to the information on our website at http://www.swib.state.wi.us/

Even with the severe market downturn in 2008 that resulted in a drop in the trust funds, the WRS remains sound.

SWIB's decision to stay invested in the stock market, even when markets are down, is based on a strategy that has served the WRS well. A focus on immediate returns will be driven by a strategy very different from one that is looking ahead to provide retirement funds for thousands of public employees in the future. Evidence indicates that the investors who miss the market's best performing individual days can miss a significant portion of stock market gains over the long term.

Market downturns are an expected part of investing in stocks. Given the large size of the WRS trust funds, it is not possible to effectively "time the markets." The evidence is strong for staying the course through up and down cycles. This is the best strategy for long-term investors like SWIB because it allows them to fully participate in the market's upward trend over time. Investors who are out of the stock market for its few best performing individual days may miss a substantial portion of market gains for longer periods. 2009 was a good example of this because the upswing came very quickly.

I have enclosed a series of questions and answers about the decision to use leverage that may be helpful. If you have further questions, please contact me.

Vicki Hearing - Public Information Officer - State of Wisconsin Investment Board -
vicki.hearing@swib.state.wi.us

-----Original Message-----
From: Stohr, Matthew [mailto:Matthew.Stohr@etf.state.wi.us]
Sent: Fridav, February 12, 2010 10:51 AM
[illegible]
Cc: Vicki.Hearing
Subject: FW: Other

Dear

Thank you for e-mailing the Department of Employee Trust Funds, the state agency that administers the Wisconsin Retirement System (WRS). I am forwarding the article you e-mailed us to the State of Wisconsin Investment Board, the state agency that invests WRS assets.

Sincerely,

Matt Stohr, Director
Legislation, Communications & Quality Assurance Wisconsin Department of Employee Trust Funds
P.O. Box 7931 Madison, WI 53707-7931
608.266.3641 (phone)
etf.wi.gov

>Learn more about our benefit programs by viewing an educational video today! Go to http://etf.wi.gov/webcasts.htm to check out the latest presentations in our video library.
>

-----Original Message-----
From: postmaster@ETF-12474 [mailto:postmaster@ETF-12474] On Behalf Of *ETF ETFWEB
Sent: Wednesday, February 03, 2010 10:57 AM
To: E-Mail (Call Center)
Subject: Other

The following feedback was submitted to ETF on 02/03/2010 at 10:57:01 AM CST

Subject Line Other

SSN Last 4
Member ID
Month/Year of Birth
First Name
Last Name
Street Address 1
Street Address 2
City, State, Postal Code , ,
Country
Day Time Phone
E-mail Address
Employer

Message: What's the Matter with Wisconsin? 1 comment
by: Roger Nusbaum February 02, 2010 | about: SPY / DIA / QQQQ
Roger Nusbaum picture Roger Nusbaum
6956

It has been very popular in the last few days to pick on the State of Wisconsin Investment Board, or SWIB, for its decision to lever up the fund on advice from from a cadre of consultants and managers to try and make up for a shortfall no doubt attributable to the decade just ended when US markets were down 24%.

Indeed, pension funds of all sorts need to figure out something as poor returns and models that rely on unrealistic expectation create a big threat to anyone who collects a pension check. You can read more about this from the WSJ, Mish, David Merkel (a more general post) and Larry Weinman.

Aside from the burden of unrealistic expectations, pools of capital like this have a very difficult time reducing or increasing exposure to a particular asset class. I write a lot about reducing equity exposure when the S&P 500 goes below its 200 DMA as a way of potentially avoiding down a lot. While I am not sure about the SWIB specifically, the typical pension cannot do this.

The change in SWIB's investment policy to allow leverage has gone through an approval process that involved some sort of study and decision making at a speed that is slower than markets move. Basically, SWIB is going to lever up some small, for now, amount to buy fixed income. Embarking on this sort of a thing after a decade of lousy equity performance and three decades of great bond performance seems ludicrous as every article about this I've read says and yet they appear to be moving full steam ahead with the expectation of a free lunch and probably the belief that they will be able to de-lever at just the right time.

It looks like they will be starting with 4% leverage and if I read correctly they could increase it to as much as 20% down the road. Small numbers like 4%, 5% or 6% will not, contrary to what some people think, bring about the demise of the SWIB. The Harvard Management Company has operated with 5% leverage for years without crashing down to zero. However the 5% leverage at HMC combined with its huge exposure to illiquid assets meaningfully impaired the Harvard Endowment and SWIB does face this potential as it will have the following allocations to potentially illiquid assets: 6% private equity, 6% real estate and 6% multiasset (whatever that means) in addition to 28% domestic equities, 25% international equities, 26% fixed income and 7% TIPS . It is also possible that their investments in private equity, real estate and multiasset (whatever that means) could be levered up making the overall leverage greater than 4%. Should the SWIB ever take the leverage up to 20%, as apparently they could, that could bankrupt it.

I do not know how long the people running the SWIB today have been there but the process that allowed them be overexposed to equities at the wrong time, and that is allowing them to lever up on an asset class that is now at very high prices, has been in place for a long time. Part of successful asset allocation and navigation of market cycles is learning from past mistakes. That appears to be absent here.

Mish recommends that the SWIB put 60% in cash in order to wait for a better opportunity. While strategically this could be correct it is not practical for a state retirement system. I did not find in any of the articles linked above how much of a gap the SWIB is trying to make up, but if they have that much in cash they would have no shot of making it up. With that much cash they could be wrong about when to sell or buy back in but, of course, they would not lose money if the stock market were to go down anywhere near as much as Mish thinks it will.

Mish is critical of the all in all the time nature of these funds, which I obviously agree with in theory, but I am not sure in practice how they could pull off taking defensive action without completely rewriting their policies and procedures.

I have no realistic solution other than abandoning the idea of leverage altogether (I am astounded that they or any state retirement system would do this). How they do not see that levering up because they have to has big problem written all over it is mind boggling. The behavior of believing we can handle it only to eventually get badly hurt is something that repeats over and over.
The only conclusion can be for us and it's an example of what not to do. We should not lever up in our portfolios. If we do not get the longer term result we think we need then something else will have to give and we should keep our portfolios simple relative to the time we can spend on our portfolios.

10-003

Cooperative Educational Service Agency 8

223 W. Park St., P.O. Box 320, Gillett, WI 54124-0320 920.855.2114 FAX 920.855.2090

RECEIVED

JAN 29 2010

EMPLOYEE TRUST FUNDS
OFFICE OF THE SECRETARY

1/28/10

Eric O. Stanchfield
Secretary of Employee Trust Fund
801 W. Badger Road
Madison, WI 53713-2526

Dear Mr. Stanchfield:

I am writing to express concern over what I read in a recent edition of the Wall Street Journal titled "Public Pensions Look at Leverage Strategy" published on January 27th. In this missive, the writer indicates that the Wisconsin Retirement System has borrowed money to invest. The purpose of this investment is to recover from losses due to the collapse of the markets. The following is a quote from that article:

> *"The State of Wisconsin Investment Board, which manages $78 billion, became among the first to adopt the strategy when it approved the plan Tuesday. The fund will borrow an amount equivalent to 4% of assets this year, and as much as 20% of its assets over the next three years.*
>
> *Fund officials say that use of leverage could eventually go higher—in theory, at least, up to 100% of assets, according to the staff analysis. But Chief Investment Officer David Villa says that level wouldn't be palatable for the Wisconsin fund. He said the pension fund was advised by four money managers, including Connecticut hedge-fund firms AQR Capital and Bridgewater Associates."*

Though I am not a financial professional or the "smartest guy in the room" - this is a cause for concern on many levels including for my staff hoping to be served under the state retirement system. We are where we are because lots of those smart guys invented new products to invest client money for outsized returns. I guess we are hoping to prevent the need to raise contributions down the road, but this seems to smack of that same chase for returns that resulted in the loss of equity for so many folks.

I look forward to information on this process and a guarantee of a positive result.

Sincerely

CC: Employee Trust Funds Board
c/o Cindy Gilles, Board Liaison
Department of Employee Trust Funds
PO Box 7931
Madison, WI 53707-7931