



JOINT LEGISLATIVE AUDIT
& REVIEW COMMISSION
OF THE VIRGINIA GENERAL ASSEMBLY

Semi-Annual VRS Investment Report July 2000

As of April 30, 2000, the market value of the VRS pension fund was \$39.7 billion, an increase of more than 13 percent since the last VRS investment report based on September 30, 1999 investment performance data. In addition, for the one-, three-, and five-year periods, the fund's investment performance exceeded established benchmarks. In addition, the VRS' investment returns for all time periods measured exceeded the actuarial assumed investment return of eight percent.

The environment in the domestic public equity markets continued to impact the fund's overall investment performance. Large-cap growth stocks continued to be the focus of investors, which impacted more diversified public equity portfolios like VRS'. For example, during the first quarter of calendar year 2000, the Russell Top 200 Growth Index returned 4.2 percent while the Russell Top 200 Value Index returned only 0.3 percent.

Other asset classes had a positive impact on the portfolio's overall performance (Table 1, page 2). VRS' non-U.S. equity program outperformed its benchmark for all periods reported. The fixed income program's performance was consistent with its benchmark. Finally, the private equity program, due primarily to the strength of the venture capital markets, substantially outperformed its benchmarks for all time periods reported.

Profile: Virginia Retirement System Investments

Market Value of Assets: \$39.7 billion

Number of External Managers:

Public Equity – 18 Fixed Income – 5

Number of External Investment Accounts:

Public Equity – 28 Fixed Income – 8

Estimated FY 2000 Investment Expenses:

\$106.2 million (26.8 basis points)

Estimated FY 2000 Investment Department Operating Expenses:

\$5.2 million (1.3 basis points)

Number of VRS Investment Department Staff: 31 positions (one vacancy)

Total Return on Investments

<i>10 years</i>	<i>5 years</i>	<i>3 years</i>	<i>1 year</i>
13.6%	17.7%	17.3%	14.7%

Performance/Intermediate Benchmarks

<small>(Time Periods Ending 4/30/00)</small>	17.1%	16.8%	10.7%
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Investment Policy Indicators (as of April 30, 2000)

Asset Class	Asset Allocation (% of Total Assets or \$ Amount)		Asset Allocation (% of Asset Class)		Type of Management (% of Asset Class)	
	Target	Actual	Domestic	International	External	VRS
Public Equity	62%	62.2%	77.8%	22.2%	84.1%	15.9%
Fixed Income	25%	24.2%	97.5%	2.5%	64%	36%
Private Equity	\$3.2 billion	\$3.2 billion	88.7%	11.3%	100%	0%
Real Estate	\$1.4 billion	\$1.4 billion	95.5%	4.5%	100%	0%

Table 1			
VRS Investment Performance for Periods Ending April 30, 2000			
Program/ <i>Performance Objective</i>	Prior 1 Year	Prior 3 Years	Prior 5 Years
Total Fund	14.7%	17.3%	17.7%
<i>VRS Performance Benchmark</i>	<i>10.7%</i>	<i>16.8%</i>	<i>17.1%</i>
<i>Actuarial Assumed Investment Return</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>
Domestic Equity	10.0%	21.4%	23.0%
<i>Russell 3000</i>	<i>12.9%</i>	<i>23.5%</i>	<i>24.3%</i>
International Equity	22.4%	10.6%	9.6%
<i>Custom MSCI ACW ex U.S.</i>	<i>16.4%</i>	<i>9.2%</i>	<i>7.3%</i>
Fixed Income	1.2%	6.2%	6.9%
<i>Lehman VRS Custom</i>	<i>1.3%</i>	<i>6.1%</i>	<i>6.5%</i>
Private Equity	111.4%	48.8%	43.6%
<i>Russell 3000 plus 250 Basis Points</i>	<i>15.4%</i>	<i>26.0%</i>	<i>26.8%</i>
Real Estate	8.9%	9.7%	9.3%
<i>Blend of NCREIF and NAREIT Indexes</i>	<i>10.2%</i>	<i>12.3%</i>	<i>11.5%</i>
Source: JLARC staff analysis of VRS data.			

The VRS investment department has been involved in a number of initiatives intended to benefit VRS' investment program. Examples of completed or ongoing initiatives for selected fund asset classes are provided below.


- ▶ ***Domestic Equity Program:*** Completed refinements to the program that resulted in the implementation of a performance-based fee structure for most external active managers.
- ▶ ***Fixed Income Program:*** Continued to increase VRS management of the passively managed portion of the fixed income portfolio. Since December 1998, the percentage of fixed income assets managed by VRS staff has increased from about 16 percent to 36 percent (\$3.5 billion) by April 2000.
- ▶ ***Private Equity Program:*** Continued to monitor exposure to the domestic venture capital area. Staff are preparing to assume manage-

ment of all private equity accounts currently administered by an external investment firm resulting in an estimated \$2 million in annual management fee cost savings.

OVERSIGHT VRS Report

VRS Oversight Report is published periodically by the Joint Legislative Audit and Review Commission (JLARC) in fulfillment of Section 30-78 et seq. of the Code of Virginia. This statute requires JLARC to provide the General Assembly with oversight capability concerning the Virginia Retirement System (VRS), and to regularly update the Legislature on oversight findings.

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► *Other Alternative Investments:* The Board of Trustees approved an initial investment of approximately \$500 million from the passive U.S. equity program in Treasury Inflation Protection Securities (TIPS) which are issued by the U.S. Treasury. TIPS are intended to provide the VRS fund with protection against the effects of inflation as well as additional diversification.

Finally, later this year the VRS investment department, the Investment Advisory Committee, and the Board of Trustees will begin the process

of formally reviewing and updating the fund's asset allocation policy. This will occur through a process known as an asset/liability study. This process will systematically consider factors affecting the fund's future benefit liabilities in order to address the risks faced by the pension fund. The recent Board of Trustees annual retreat focused almost exclusively on issues related to the upcoming asset/liability study. The results of the asset/liability study and a recommended asset allocation policy based on the results of this analysis will likely be presented for the Board's consideration in early to mid-2001.

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