



The SWIB Report

Published by the State of Wisconsin Investment Board for WRS participants

May 2005

Performance Update

The stock market continued to experience volatility in the first quarter of 2005. Major indexes for the US markets declined somewhat amid investor concerns over rising energy costs. However, some market observers remained optimistic that the markets will produce positive returns for 2005.

Bonds yields are expected to rise. As a result, the expected return for bonds should be lowered. Major indexes for US and foreign bond markets were down for the first quarter.

Calendar year-to-date Preliminary Returns As of 3/31/05

Fixed Fund—— -0.8%
Variable Fund — -1.6%

About SWIB

The State of Wisconsin Investment Board (SWIB) is the state agency responsible for investing the Wisconsin Retirement System (WRS) assets.

2005 Board Meetings

Meetings are held at the SWIB office, 121 E. Wilson St., second floor. **Agendas are posted on the SWIB website.** Dates are:

May 11	Sept. 14
June 8	Oct. 12/13*
July (none)	Nov. 9
August 10	Dec. 14

* Off-site meeting

Study focuses on investment styles for future success

The pace of today's investment marketplace continues to accelerate. To be successful, SWIB must be more flexible than ever, able to adjust to opportunities and maximize its own strengths as well as the strengths of its outside managers. With this in mind, the Board asked staff to undertake a comprehensive review of our current mix of strategies, investment styles and performance.

The goal is to determine if there are better investment management strategies or changes in authority and resources needed to manage the assets of the pension fund.

As a part of this project, SWIB is comparing the following:

- SWIB's mix of investment management styles to other public pension funds.
- Investment results (after fees and consideration of risk) of portfolios managed by SWIB staff to those of outside managers SWIB has hired.
- SWIB's management flexibility to that of its peers.

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Questions? SWIB offers answers

Want to know more about SWIB and the investments of the retirement trust funds? There are two main resources available. The first is the SWIB website at www.swib.state.wi.us. The second is to contact SWIB directly by calling the beneficiary hotline, sending a letter or email.

The website is an excellent resource with a wide range of information from how the Investment Board operates to the types of investments made. It includes a monthly Board meeting schedule and current agenda, posted just prior to the meeting.

Year-to-date investment performance is posted monthly once the numbers are final, which can take up to four weeks. Participants can also register for occasional updates by email by contacting SWIB at info@swib.state.wi.us.



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Trust Funds Investment Strategy

Fixed Fund

The Fixed Fund is the largest of the two trust funds that make up the Wisconsin Retirement System (WRS). All participants have at least 50% of their initial deposits in the Fixed Fund.

Investment Goals: The basic objective is to earn an average 7.8% annual return over the long term, the assumption recommended by the WRS actuary and set by the ETF Board. The ten-year annualized return as of December 31, 2004, was 10.5%.

A second goal is to exceed the benchmark established by the Board of Trustees. The benchmark measures SWIB's performance against the markets. The Fixed Fund benchmark is mainly a composite of several industry indexes rolled up and weighted to reflect the Board's asset allocation.

Investment Strategy: In keeping with the extended time horizon of the Fund's obligations to provide pensions for all participants, this fully diversified, balanced fund seeks long-term growth.

Investment Guidelines: Guidelines are established for each asset class by the Trustees. State law permits investments in stock, bonds, loans, securities, real estate and other investments not specifically prohibited by law.

Variable Fund

About 8% of the WRS assets are managed in the Variable Fund. Participants who choose the Variable Fund can place half of future pension fund contributions in this Fund. Participants in the Variable Fund option also accept a greater degree of risk, in part because it is a stock fund, for the potential of greater long-term returns.

Investment Goal: The investment objective is to achieve returns that equal or exceed that of similar equity portfolios over a full market cycle. The Russell 3000 Index, a broad US equity index representing approximately 98% of the US market, is also used as a performance measure. However, the Variable Fund is diversified into international markets not represented in the Russell 3000.

Investment Strategy: Assets are generally invested in equities with 79% in domestic stocks, 20% in international stocks and 1% in cash. Investments are well diversified across large, mid-size and small capitalization companies in the US and by region internationally. The stocks are the same as in the Fixed Fund.

Investment Guidelines: Under Wisconsin Statutes, the assets of the Variable Fund are invested primarily in stocks or other recognized forms of equities. The fund may temporarily invest in other types of securities because of market conditions.

2005 Fixed Fund Asset Target Changes

Assets	2004 Target	2005 Target
US Stocks	39%	Remains at 39%
International Stocks	20%	Remains at 20%
Fixed Income	31%	Decreased to 29%
Real Estate	4%	Increased to 5%
Private Equit/Debt	6%	Decreased to 5%
Multi-Asset*	----	Established at 2%

* The multi-asset portfolio was added in 2003, but became a separate allocation in 2005.

Stocks (equities) primarily consist of stocks in US companies, diversified among small-, medium- and large-sized companies, and international stocks.

Fixed Income includes US government bonds and corporate bonds purchased in public markets and global bonds (US or foreign bonds meeting minimum credit quality requirements).

Real Estate includes commercial real estate with SWIB as a sole direct owner, or in joint ventures and partnerships and private commercial mortgages in partnership with Northwestern Mutual Life.

Private Equity/Debt primarily includes leveraged buyouts and venture capital, and, also, direct, long-term loans to Wisconsin companies. These investments carry greater risk, but offer the prospect of greater return.

Multi-Asset primarily includes equity and debt investments in developed and emerging markets, and also includes opportunistic investments in real estate, natural resources, private equity, and money market instruments.

2004 Investment Recap:

Annualized Performance Ending 12/31/04

	1-Year Return	5-Year Return	10-Year Return
Fixed Fund	12.8%	4.4%	10.5%
Benchmark	11.7	3.6	10.0
Variable Fund	12.7%	-0.1%	10.6%
Benchmark	13.4	-0.9	10.0

Strong returns from international stocks and private market investments combined with a fourth quarter surge in US stocks helped push the Fixed Retirement Fund to a 12.8% return on December 31, 2004. The Variable Fund returned 12.7% for the year.

Private Markets Group: Private equity/debt returned 21.7% compared to 9.8% for the benchmark. Real estate returned 21.4% versus 12.4% for its benchmark. Both portfolios benefited from the rise in the Euro, exposure to international investments and a market demand that created significant selling opportunities at attractive prices.

Public Fixed Income Group: Global bonds returned 10.8% against a benchmark of 10.3%. In a weak bond market, US investment

grade fixed income holdings saw a 4.4% total return versus a 4.2% benchmark. Emerging market debt returned 17.8% versus a benchmark of 11.6%.

Public Equities (Stocks) Group: Domestic stocks returned 10.7%, below a return of 11.9% for the Russell 3000, a broad market indicator for US stock returns. Investments in health care hurt the overall performance of domestic stocks, also hit hard by a 10% drop in large pharmaceuticals for the year. International stock investments in developed markets returned 21.7% and SWIB's internally managed portfolio returned 23.2% compared to the benchmark of 20.4%. Emerging market equities returned 28.2% against a benchmark of 26.0%.

The **multi-asset portfolio** returned 15.7% versus 13.2%.

SWIB names head of Fixed Income

J. Alain Hung has been named head of fixed income. His duties include overall investment responsibility for the \$17.8 billion public fixed income group. Alain joined SWIB in 1996 as the global fixed income portfolio manager and has more than 17



Alain Hung

years experience in finance and investing. He received a bachelor's degree in finance/accounting and a master's degree in applied economics from Acadia University in Nova Scotia. He earned the Chartered Financial Analyst designation in 2000.

Chirag Gandhi has been promoted to global fixed income portfolio manager and **Todd Ludgate** has been promoted to government credit portfolio manager.

Governor announces SWIB Board officers

The Governor has reappointed **James A. Senty**, chair of the Investment Board and **Thomas J. Boldt** as vice chair.

Senty is president of Midwest Gas Cos. in La Crosse and serves as chairman of the Board of Park Bank in Madison. Boldt is president of The Boldt Group, Inc. and chief executive officer of The Boldt Company in Appleton.

Eric O. Stanchfield, secretary of the Department of Employee Trust Funds, will continue to serve as the Board secretary. His position is appointed by the members of the Board.

Annual Investment Returns		
Year	Fixed Fund	Variable Fund
2004	12.8%	12.7%
2003	24.2%	32.7%
2002	-8.8%	-21.9%
2001	-2.3%	-8.3%
2000	-0.8%	-7.2%
1999	15.7%	27.8%
1998	14.6%	17.5%
1997	17.2%	21.6%
1996	14.4%	19.8%
1995	23.1%	25.6%
1994	-0.6%	0.8%
1993	15.0%	16.5%
1992	9.7%	10.7%
1991	20.4%	27.1%
1990	-1.5%	-11.3%
1989	19.2%	22.6%
1988	14.4%	21.7%
1987	2.2%	-1.1%
1986	14.5%	11.5%
1985	27.5%	32.7%
20-year Average Annual Return	11.1%	11.4%

Study continued from page 1

■ The role of active portfolio management versus passive investment using index funds, such as the S&P 500.

“This is a major strategic project requiring a very comprehensive study by the staff,” said David Mills, executive director. “The results and recommendations that come out of this project will provide us with an excellent foundation for building a program for the future.

“Once the fact-finding is completed, our next step is to discuss the results with the Board, state policymakers and fund participants over the next few months,” he added.



Q. How do SWIB's investment results affect me?

A. The impact of investment results on individual WRS accounts is determined by the Department of Employee Trust Funds and depends on several factors established by law. Favorable investment returns have increased the monthly benefit retirees received every year but 2003, when no increase was provided. For retirees participating in the Variable Fund, investment returns resulted in an increase seven out of the last 10 years. In addition, investment gains can reduce the amount of employee and employer pension contributions. Over 80% of the cost of benefits that today's retirees receive is also funded from investment earnings.

Q. What are the criteria for making investment decisions?

A. The law requires that all of our investment decisions be guided solely by what is in the best interest of the WRS. We strive to produce the long-term asset growth needed to meet the obligations to current and future retirees. We evaluate both rate of return and risk when considering a mix of assets.

Performance compared to peers

Public pension funds measure performance in different ways. One common way is to compare the rate of return against an investment standard, or benchmark. (See chart on the top of page 3.) The Legislative Audit Bureau (LAB) also compares SWIB's performance to

nine other public pension funds listed below. As of December 31, 2004, the Fixed Fund ranked fifth for one-year returns, first for five-year, for the second consecutive year, and ninth for ten-year returns compared to nine other large public pension funds surveyed by the LAB for performance

evaluation in the past. The Fixed Fund's five-year return ranked first on a risk adjusted basis.

While returns varied significantly for the one- and five-year periods, the ten-year variance was less than 0.7% with SWIB ranking the same as three other funds when rounded to one decimal point.

Another survey conducted by the Trust Universe Comparison Service (TUCS) ranks the Fixed Fund's one-year return in the top 25%, the five-year return in the top third and ten-year return above the median of about 50 other public pension funds with assets over \$1 billion.

TUCS returns are not reported on a risk-adjusted basis.

December 31, 2004 Gross Return Comparison

Fund	One-year	Rank	Five-year	Rank	Ten-year	Rank
SWIB (Fixed Trust Fund)	12.8%	5	4.4%	1	10.5%	9
New Jersey Division of Inv.	10.3	10	0.7	10	10.5	7
Virginia*	13.7	2	3.7	3	11.1	1
Florida Retirement System	12.3	8	2.5	8	10.9	2
New York State Teachers*	12.0	9	2.5	7	10.9	3
Minnesota Combined *	12.5	7	2.3	9	10.4	10
California Public Employees	13.5	3	3.3	5	10.5	6
Pennsylvania Public Schools	15.1	1	4.0	2	10.9	4
Texas Teachers	12.7	6	2.9	6	10.7	5
Washington State Inv Board*	13.2	4	3.6	4	10.5	7

*Returns for Minnesota, New York, Virginia, and Washington are net of fees.

The chart above shows SWIB's investment performance compared to nine other large pension funds surveyed by the Legislative Audit Bureau. These returns are not adjusted for risk. Liabilities and investment objectives vary from fund to fund and may contribute to differing performance results.