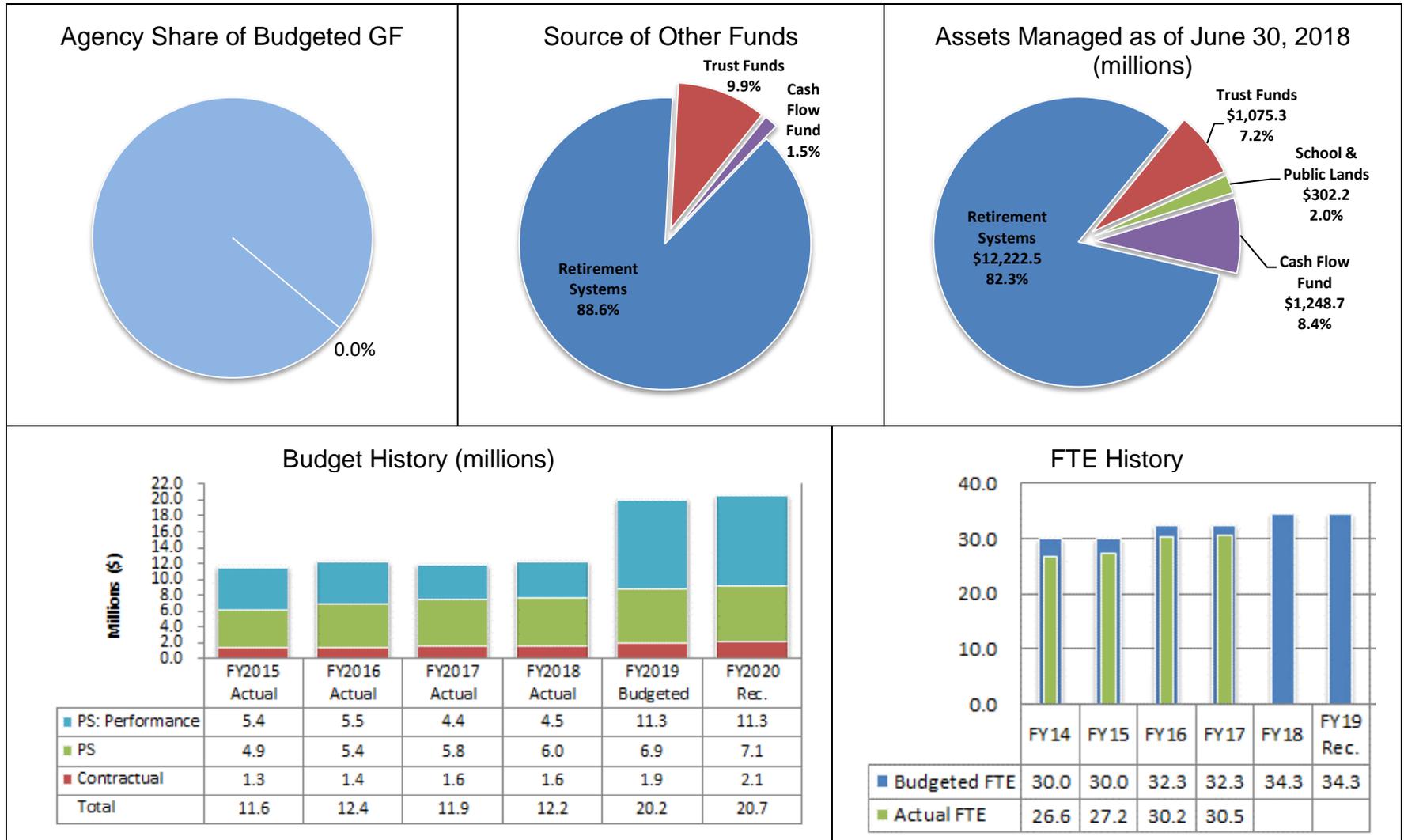


# FY20 Budget Briefing

## State Investment Council

Information contained in this document is based on the Governor's original FY20 recommended budget.  
This document may not correspond with the final FY20 budget adopted by the Legislature.



## 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 2017 Actual	FY 2018 Actual	FY 2019 Budget	FY 2020 Agency Request	FY 2020 Governors Recommended	Change From FY 2019
<b>BY PROGRAM</b>						
Investment of State Funds	7,468,101	7,727,966	8,880,967	9,344,060	9,344,060	463,093
Performance Based Compensation	4,397,259	4,498,960	11,302,056	11,328,728	11,328,728	26,672
<b>Total</b>	<b>11,865,360</b>	<b>12,226,926</b>	<b>20,183,023</b>	<b>20,672,788</b>	<b>20,672,788</b>	<b>489,765</b>
<b>BY FUND CATEGORY</b>						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	11,865,360	12,226,926	20,183,023	20,672,788	20,672,788	489,765
<b>Total</b>	<b>11,865,360</b>	<b>12,226,926</b>	<b>20,183,023</b>	<b>20,672,788</b>	<b>20,672,788</b>	<b>489,765</b>
<b>BY OBJECT EXPENDITURE</b>						
<b>Personnel Costs</b>	<b>10,194,121</b>	<b>10,534,143</b>	<b>18,183,543</b>	<b>18,423,009</b>	<b>18,423,009</b>	<b>239,466</b>
Salaries	8,798,392	9,088,795	15,737,284	15,940,379	15,940,379	203,095
Benefits	1,395,729	1,445,349	2,446,259	2,482,630	2,482,630	36,371
<b>Operating Expenditures</b>	<b>1,671,240</b>	<b>1,692,782</b>	<b>1,999,480</b>	<b>2,249,779</b>	<b>2,249,779</b>	<b>250,299</b>
Travel	66,817	56,549	85,000	85,000	85,000	0
Contractual Services	1,560,584	1,572,594	1,864,960	2,117,259	2,117,259	252,299
Supplies and Materials	5,953	3,948	9,000	7,000	7,000	(2,000)
Grants and Subsidies	0	0	0	0	0	0
Capital Outlay	37,885	59,691	40,520	40,520	40,520	0
Other	0	0	0	0	0	0
<b>Total</b>	<b>11,865,360</b>	<b>12,226,926</b>	<b>20,183,023</b>	<b>20,672,788</b>	<b>20,672,788</b>	<b>489,765</b>
<b>Full-Time Equivalent (FTE)</b>	<b>30.5</b>	<b>31.0</b>	<b>34.3</b>	<b>35.3</b>	<b>35.3</b>	<b>1.0</b>

### Major Items Summary - State Investment Council

	Agency Request					Governor's Recommendation				
	General	Federal	Other	Total	FTE	General	Federal	Other	Total	FTE
<b>FY 2020 Base Budget</b>	0	0	20,183,023	20,183,023	34.3	0	0	20,183,023	20,183,023	34.3
<b>Maintenance of Current Operations</b>										
A. Operating Expense Inflation	0	0	14,486	14,486	0.0	0	0	14,486	14,486	0.0
B. Performance Based Employee Compensation	0	0	72,842	72,842	0.0	0	0	72,842	72,842	0.0
C. Align Budget with Actual Expenditures	0	0	(2,559)	(2,559)	0.0	0	0	(2,559)	(2,559)	0.0
<b>Total Maintenance Adjustments</b>	0	0	84,769	84,769	0.0	0	0	84,769	84,769	0.0
<b>FY 2020 Program Maintenance Budget</b>	0	0	20,267,792	20,267,792	34.3	0	0	20,267,792	20,267,792	34.3
<b>Program Line Items</b>										
1. Legal Services for Distressed Debt	0	0	50,000	50,000	0.0	0	0	50,000	50,000	0.0
2. New Contracted Trade Order System	0	0	175,000	175,000	0.0	0	0	175,000	175,000	0.0
3. Full-Time Staff Attorney FTE	0	0	166,819	166,819	1.0	0	0	166,819	166,819	1.0
4. Investment Research Services	0	0	13,177	13,177	0.0	0	0	13,177	13,177	0.0
<b>Total Program Line Items</b>	0	0	404,996	404,996	1.0	0	0	404,996	404,996	1.0
<b>FY 2020 Total Budget</b>	0	0	20,672,788	20,672,788	35.3	0	0	20,672,788	20,672,788	35.3
Change from Base Budget	0	0	489,765	489,765	1.0	0	0	489,765	489,765	1.0
% Change from Base Budget	0.0%	0.0%	2.4%	2.4%	2.9%	0.0%	0.0%	2.4%	2.4%	2.9%

### Prior and Current Year Budget Recap - State Investment Council

Prior Year Recap	FTE	General	Federal	Other	Total
<b>FY 2018 Original Budget</b>	34.3	0	0	19,299,621	19,299,621
<b>Legislative Adjustments</b>					
Supplemental Bill - Health Insurance			0	26,769	26,769
Supplemental Bill			0	2,333	2,333
Supplemental Bill - Health Insurance			0	741	741
<b>Total Legislative Adjustments</b>	0.0	0	0	29,843	29,843
<b>Agency Adjustments</b>					
<b>Total Agency Adjustments</b>	0.0	0	0	0	0
<b>FY 2018 Adjusted Budget</b>	34.3	0	0	19,329,464	19,329,464
<b>Reversions</b>					
<b>Total Reversions</b>	0.0	0	0	0	0
<b>Unutilized FTE</b>	(3.3)				
FY 2018 Percent Reverted or Transferred	9.6%	0	0	0.0%	0.0%

Current Year Recap		FTE	General	Federal	Other	Total
<b>FY 2019 Original Budget</b>		<b>34.3</b>	<b>0</b>	<b>0</b>	<b>20,100,124</b>	<b>20,100,124</b>
<b>Legislative Adjustments</b>						
Market Adjustment	PS		0	0	78,307	78,307
Market Adjustment	OE		0	0	928	928
Bureau Billings	OE		0	0	3,664	3,664
<b>Total Legislative Adjustments</b>		<b>0.0</b>	<b>0</b>	<b>0</b>	<b>82,899</b>	<b>82,899</b>
<b>Agency Adjustments</b>						
<b>Total Agency Adjustments</b>		<b>0.0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>FY 2019 Adjusted Budget</b>		<b>34.3</b>	<b>0</b>	<b>0</b>	<b>20,183,023</b>	<b>20,183,023</b>

### 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 2017 Actual	FY 2018 Actual	FY 2019 Budget	FY 2020 Agency Request	FY 2020 Governors Recommended	Change From FY 2019
<b>BY PROGRAM</b>						
Investment of State Funds	7,468,101	7,727,966	8,880,967	9,344,060	9,344,060	463,093
<b>Total</b>	<b>7,468,101</b>	<b>7,727,966</b>	<b>8,880,967</b>	<b>9,344,060</b>	<b>9,344,060</b>	<b>463,093</b>
<b>BY FUND CATEGORY</b>						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	7,468,101	7,727,966	8,880,967	9,344,060	9,344,060	463,093
<b>Total</b>	<b>7,468,101</b>	<b>7,727,966</b>	<b>8,880,967</b>	<b>9,344,060</b>	<b>9,344,060</b>	<b>463,093</b>
<b>BY OBJECT EXPENDITURE</b>						
<b>Personnel Costs</b>	<b>5,796,862</b>	<b>6,035,183</b>	<b>6,881,487</b>	<b>7,094,281</b>	<b>7,094,281</b>	<b>212,794</b>
Salaries	4,881,330	5,016,583	5,805,776	5,985,433	5,985,433	179,657
Benefits	915,531	1,018,601	1,075,711	1,108,848	1,108,848	33,137
<b>Operating Expenditures</b>	<b>1,671,240</b>	<b>1,692,782</b>	<b>1,999,480</b>	<b>2,249,779</b>	<b>2,249,779</b>	<b>250,299</b>
Travel	66,817	56,549	85,000	85,000	85,000	0
Contractual Services	1,560,584	1,572,594	1,864,960	2,117,259	2,117,259	252,299
Supplies and Materials	5,953	3,948	9,000	7,000	7,000	(2,000)

	FY 2017 Actual	FY 2018 Actual	FY 2019 Budget	FY 2020 Agency Request	FY 2020 Governors Recommended	Change From FY 2019
Grants and Subsidies	0	0	0	0	0	0
Capital Outlay	37,885	59,691	40,520	40,520	40,520	0
Other	0	0	0	0	0	0
<b>Total</b>	<b>7,468,100</b>	<b>7,727,966</b>	<b>8,880,967</b>	<b>9,344,060</b>	<b>9,344,060</b>	<b>463,093</b>
<b>Full-Time Equivalent (FTE)</b>	<b>30.5</b>	<b>31.0</b>	<b>34.3</b>	<b>35.3</b>	<b>35.3</b>	<b>1.0</b>
<b>FUNDING SOURCES (Governor's Recommended)</b>	<b>General</b>	<b>Federal</b>	<b>Other</b>	<b>%General</b>	<b>%Federal</b>	<b>%Other</b>
INVESTMENT COUNCIL OPERATING	0	0	9,344,060	0.0%	0.0%	100.0%

**MAJOR ITEMS SUMMARY: INVESTMENT OF STATE FUNDS (3210)**

	Agency Request					Governor's Recommendation				
	General	Federal	Other	Total	FTE	General	Federal	Other	Total	FTE
<b>FY 2020 Base Budget</b>	<b>0</b>	<b>0</b>	<b>8,880,967</b>	<b>8,880,967</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,880,967</b>	<b>8,880,967</b>	<b>34.3</b>
<b>Maintenance of Current Operations</b>										
A. Operating Expense Inflation	0	0	14,486	14,486	0.0	0	0	14,486	14,486	0.0
B. Performance Based Employee Compensation	0	0	46,170	46,170	0.0	0	0	46,170	46,170	0.0
C. Align Budget with Actual Expenditures	0	0	(2,559)	(2,559)	0.0	0	0	(2,559)	(2,559)	0.0
<b>Total Maintenance Adjustments</b>	<b>0</b>	<b>0</b>	<b>58,097</b>	<b>58,097</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>58,097</b>	<b>58,097</b>	<b>0.0</b>
<b>FY 2020 Program Maintenance Budget</b>	<b>0</b>	<b>0</b>	<b>8,939,064</b>	<b>8,939,064</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,939,064</b>	<b>8,939,064</b>	<b>34.3</b>
<b>Program Line Items</b>										
1. Legal Services for Distressed Debt	0	0	50,000	50,000	0.0	0	0	50,000	50,000	0.0
2. New Contracted Trade Order System	0	0	175,000	175,000	0.0	0	0	175,000	175,000	0.0
3. Full-Time Staff Attorney FTE	0	0	166,819	166,819	1.0	0	0	166,819	166,819	1.0
4. Investment Research Services	0	0	13,177	13,177	0.0	0	0	13,177	13,177	0.0
<b>Total Program Line Items</b>	<b>0</b>	<b>0</b>	<b>404,996</b>	<b>404,996</b>	<b>1.0</b>	<b>0</b>	<b>0</b>	<b>404,996</b>	<b>404,996</b>	<b>1.0</b>
<b>FY 2020 Total Budget</b>	<b>0</b>	<b>0</b>	<b>9,344,060</b>	<b>9,344,060</b>	<b>35.3</b>	<b>0</b>	<b>0</b>	<b>9,344,060</b>	<b>9,344,060</b>	<b>35.3</b>
Change from Base Budget	0	0	463,093	463,093	35.3	0	0	463,093	463,093	35.3
% Change from Base Budget	0.0%	0.0%	5.2%	5.2%	0.0%	0.0%	0.0%	5.2%	5.2%	0.0%

**BUDGET DETAIL: INVESTMENT OF STATE FUNDS (3210)**

Prior Year Recap	FTE	General	Federal	Other	Total
<b>FY 2018 Original Budget</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,532,631</b>	<b>8,532,631</b>
<b>Legislative Adjustments</b>					
Supplemental Bill - Health Insurance		PS	0	0	26,769
Supplemental Bill		OE	0	0	2,333
Supplemental Bill - Health Insurance		OE	0	0	741
<b>Total Legislative Adjustments</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>29,843</b>	<b>29,843</b>
<b>Agency Adjustments</b>					
<b>Total Agency Adjustments</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>FY 2018 Adjusted Budget</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,562,474</b>	<b>8,562,474</b>
<b>Reversions</b>					
<b>Total Reversions</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Unutilized FTE</b>	<b>(3.3)</b>				
FY 2018 Percent Reverted or Transferred	9.6%	0	0	0.0%	0.0%
<b>Current Year Recap</b>	<b>FTE</b>	<b>General</b>	<b>Federal</b>	<b>Other</b>	<b>Total</b>
<b>FY 2019 Original Budget</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,798,068</b>	<b>8,798,068</b>
<b>Legislative Adjustments</b>					
Market Adjustment		PS	0	0	78,307
Market Adjustment		OE	0	0	928
Bureau Billings		OE	0	0	3,664
<b>Total Legislative Adjustments</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>82,899</b>	<b>82,899</b>
<b>Agency Adjustments</b>					
<b>Total Agency Adjustments</b>	<b>0.0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>FY 2019 Adjusted Budget</b>	<b>34.3</b>	<b>0</b>	<b>0</b>	<b>8,880,967</b>	<b>8,880,967</b>
<b>FY 2020 Base</b>					
Agency Request	34.3	0	0	8,880,967	8,880,967
Governor's Recommendation	34.3	0	0	8,880,967	8,880,967

**A. Operating Expense Inflation**

The agency requested a total increase of **\$14,486** in other funds relating to \$4,410 increase in rent, \$5,520 increase in bank custodian charges, and \$4,556 increase in contract printer maintenance costs.

Agency Request	0.0	0	0	14,486	14,486
Governor's Recommendation	0.0	0	0	14,486	14,486

	FTE	General	Federal	Other	Total
<b>B. Performance Based Employee Compensation</b>					
The agency requested an increase of <b>\$46,170</b> in other funds for an increase in employee compensation. This includes a 1.75% increase for 28 investment positions, plus promotional increases of between 2% and 11% for never and intermediate level investment team members.					
Agency Request	0.0	0	0	46,170	46,170
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>46,170</i>	<i>46,170</i>
<b>C. Align Budget with Actual Expenditures</b>					
The agency requested a decrease of <b>(\$2,559)</b> in other funds relating to supplies, materials, and janitorial services.					
Agency Request	0.0	0	0	(2,559)	(2,559)
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>(2,559)</i>	<i>(2,559)</i>
<b>FY 2020 Maintenance of Current Operations</b>					
Agency Request	34.3	0	0	8,939,064	8,939,064
<i>Governor's Recommendation</i>	<i>34.3</i>	<i>0</i>	<i>0</i>	<i>8,939,064</i>	<i>8,939,064</i>

**1. Legal Services for Distressed Debt**

The agency requested an increase of **\$50,000** in other funds for legal services relating to investments dealing with distressed debt. The additional authority is needed because the investment council cannot count on being reimbursed by the company in future cases. The potential returns for the investment council outweigh the additional expenses related to distressed debt investments.

In FY2019, \$50,000 was appropriated for distressed debt legal services. The FY2020 request is for an additional \$50,000, which would allow for a total of \$100,000 in distressed debt legal services.

Agency Request	0.0	0	0	50,000	50,000
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>50,000</i>	<i>50,000</i>

**2. New Contracted Trade Order System**

The agency requested an increase of **\$175,000** in other funds for a new trade order system. The new trade order system will help assure compliance in trading and portfolio management risk controls, such as, limits on individual trades or size of investments. The system will reduce the risk of trading errors and reduce the time spent by staff on mainly reviewing aspects of the current trading system. The system will be a contracted service.

The investment council currently utilizes a free software trading system, but the software requires manually reviewing many aspects involved in investment trading.

Agency Request	0.0	0	0	175,000	175,000
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>175,000</i>	<i>175,000</i>

	FTE	General	Federal	Other	Total
<b>3. Full-Time Staff Attorney FTE</b>					
The agency requested an increase of <b>\$166,819</b> in other funds and 1 FTE for a new full-time staff attorney for the investment council. The full-time staff attorney would manage portions of the compliance processes and assist in the legal aspects of distressed debt investments.					
In FY16, the investment council was appropriated \$32,456 and 0.3 FTE for a part-time staff attorney. The part-time staff attorney will stay on during FY2020 to transition and help with training the new attorney. The extra spending authority and 0.3 FTE will be removed during the FY2021 budget.					
Agency Request	1.0	0	0	166,819	166,819
<i>Governor's Recommendation</i>	1.0	0	0	166,819	166,819
<b>4. Investment Research Services</b>					
The agency requested <b>\$13,177</b> in other funds relating to investment research services. The increase is a result of canceling a few services and making changes to other research services. The request in research services is a net increase of 1.14%. Research services are continually evaluated, and investment services may be replaced by another provider if a higher quality product is found.					
In FY2019, \$55,100 was appropriated for investment research services to allow for additional investment services to be added.					
Agency Request	0.0	0	0	13,177	13,177
<i>Governor's Recommendation</i>	0.0	0	0	13,177	13,177
<b>FY 2020 Total</b>					
Agency Request	35.3	0	0	9,344,060	9,344,060
<i>Governor's Recommendation</i>	35.3	0	0	9,344,060	9,344,060
Agency Request					
Change from Original Appropriation	1.0	0	0	463,093	463,093
% Change from Original Appropriation	2.9%	0.0%	0.0%	5.2%	5.2%
<i>Governor's Recommendation</i>					
<i>Change from Original Appropriation</i>	1.0	0	0	463,093	463,093
<i>% Change from Original Appropriation</i>	2.9%	0.0%	0.0%	5.2%	5.2%

<b>REVENUES AND STATISTICS: INVESTMENT OF STATE FUNDS (3210)</b>				
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<b>Investment of State Funds</b>	Actual FY 2017	Actual FY 2018	Estimated FY 2019	Estimated FY 2020
<b>REVENUES</b>				
Investment Management Fees:				
Retirement System (SDRS)	10,443,697	11,235,502	9,864,781	12,243,265
Cash Flow Fund (CFF)	267,055	259,845	268,437	270,000
School and Public Lands (S&PL)	261,720	277,404	245,974	304,656
Dakota Cement Trust (DCT)	302,082	313,465	270,683	336,052
Education Enhancement Trust (EET)	494,188	524,835	463,868	575,007
Health Care Trust (HCT)	131,874	136,966	117,933	146,572
Total	11,900,616	12,748,017	11,231,676	13,875,552

	Actual FY 2017	Actual FY 2018	Estimated FY 2019	Estimated FY 2020
<b>PERFORMANCE INDICATORS</b>				
SDRS Yr-End Assets/Inv Income (Millions)	\$11,632/\$1,465	\$12,222/\$957.1		
SDRS Total Fund Return/Capital Mkt Benchmark	13.81%/10.96%	7.94%/7.33%		
S&PL Yr-End Assets/Invest Income (Millions)	\$286.4/\$30.7	\$302.2/\$20.3		
S&PL Total Fund Return/Benchmark Return	11.68%/9.96%	6.80%/6.82%		
DCT Yr-End Assets/Invest Income (Millions)	\$316.5/\$34.6	\$325.5/\$22.5		
DCT Total Fund Return/Benchmark Return	11.55%/9.96%	6.78%/6.82%		
EET Yr-End Assets/Invest Income (Millions)	\$554.5/\$57.9	\$602.6/\$38.8		
EET Total Fund Return/Benchmark Return	11.52%/10.01%	6.82%/6.90%		
HCT Yr-End Assets/Invest Income (Millions)	\$143.0/\$15.1	\$147.1/\$9.8		
HCT Total Fund Return/Benchmark Return	11.58%/9.96%	6.76%/6.82%		
CFF Average Amount Invested (Millions)	\$1,299	\$1,345		
CFF Investment Income Received (Millions)	\$16.40	\$16.20		
CFF Average Yield/Benchmark Yield	1.3%/1.46%	1.26%/1.20%		

**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 2017 Actual	FY 2018 Actual	FY 2019 Budget	FY 2020 Agency Request	FY 2020 Governors Recommended	Change From FY 2019
<b>BY PROGRAM</b>						
Performance Based Compensation	4,397,259	4,498,960	11,302,056	11,328,728	11,328,728	26,672
<b>Total</b>	<b>4,397,259</b>	<b>4,498,960</b>	<b>11,302,056</b>	<b>11,328,728</b>	<b>11,328,728</b>	<b>26,672</b>
<b>BY FUND CATEGORY</b>						
General	0	0	0	0	0	0
Federal	0	0	0	0	0	0
Other	4,397,259	4,498,960	11,302,056	11,328,728	11,328,728	26,672
<b>Total</b>	<b>4,397,259</b>	<b>4,498,960</b>	<b>11,302,056</b>	<b>11,328,728</b>	<b>11,328,728</b>	<b>26,672</b>
<b>BY OBJECT EXPENDITURE</b>						
<b>Personnel Costs</b>	<b>4,397,259</b>	<b>4,498,960</b>	<b>11,302,056</b>	<b>11,328,728</b>	<b>11,328,728</b>	<b>26,672</b>
Salaries	3,917,062	4,072,212	9,931,508	9,954,946	9,954,946	23,438
Benefits	480,197	426,748	1,370,548	1,373,782	1,373,782	3,234
<b>Operating Expenditures</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
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
<b>Total</b>	<b>4,397,259</b>	<b>4,498,960</b>	<b>11,302,056</b>	<b>11,328,728</b>	<b>11,328,728</b>	<b>26,672</b>
<b>Full-Time Equivalent (FTE)</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
<b>FUNDING SOURCES (Governor's Recommended)</b>	<b>General</b>	<b>Federal</b>	<b>Other</b>	<b>%General</b>	<b>%Federal</b>	<b>%Other</b>
INVESTMENT COUNCIL OPERATING	0	0	11,328,728	0.0%	0.0%	100.0%

**MAJOR ITEMS SUMMARY: PERFORMANCE BASED COMPENSATION (3211)**

	Agency Request					Governor's Recommendation				
	General	Federal	Other	Total	FTE	General	Federal	Other	Total	FTE
<b>FY 2020 Base Budget</b>	0	0	11,302,056	11,302,056	0.0	0	0	11,302,056	11,302,056	0.0
<b>Maintenance of Current Operations</b>										
A. Performance Based Employee Compensation	0	0	26,672	26,672	0.0	0	0	26,672	26,672	0.0
<b>Total Maintenance Adjustments</b>	0	0	26,672	26,672	0.0	0	0	26,672	26,672	0.0
<b>FY 2020 Program Maintenance Budget</b>	0	0	11,328,728	11,328,728	0.0	0	0	11,328,728	11,328,728	0.0
<b>Program Line Items</b>										
<b>Total Program Line Items</b>	0	0	0	0	0.0	0	0	0	0	0.0
<b>FY 2020 Total Budget</b>	0	0	11,328,728	11,328,728	0.0	0	0	11,328,728	11,328,728	0.0
Change from Base Budget	0	0	26,672	26,672	0.0	0	0	26,672	26,672	0.0
% Change from Base Budget	0.0%	0.0%	0.2%	0.2%	0.0%	0.0%	0.0%	0.2%	0.2%	0.0%

**BUDGET DETAIL: PERFORMANCE BASED COMPENSATION (3211)**

	FTE	General	Federal	Other	Total
<b>Prior Year Recap</b>					
<b>FY 2018 Original Budget</b>	0.0	0	0	10,766,990	10,766,990
<b>Legislative Adjustments</b>					
<b>Total Legislative Adjustments</b>	0.0	0	0	0	0
<b>Agency Adjustments</b>					
<b>Total Agency Adjustments</b>	0.0	0	0	0	0
<b>FY 2018 Adjusted Budget</b>	0.0	0	0	10,766,990	10,766,990
<b>Reversions</b>					
<b>Total Reversions</b>	0.0	0	0	0	0
<b>Unutilized FTE</b>	0.0				
FY 2018 Percent Reverted or Transferred	0	0	0	0.0%	0.0%
<b>Current Year Recap</b>					
<b>FY 2019 Original Budget</b>	0.0	0	0	11,302,056	11,302,056
<b>Legislative Adjustments</b>					
<b>Total Legislative Adjustments</b>	0.0	0	0	0	0
<b>Agency Adjustments</b>					
<b>Total Agency Adjustments</b>	0.0	0	0	0	0
<b>FY 2019 Adjusted Budget</b>	0.0	0	0	11,302,056	11,302,056

<b>FY 2020 Base</b>						
Agency Request	0.0	0	0	11,302,056	11,302,056	
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>11,302,056</i>	<i>11,302,056</i>	

**A. Performance Based Employee Compensation**

The agency requested an increase of **\$26,672** 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. The incentive plan includes funding for potential maximum incentives up to 200% of the base salaries. Incentives are rewarded for out performance and range from 0% to 200%.

Agency Request	0.0	0	0	26,672	26,672	
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>26,672</i>	<i>26,672</i>	

**FY 2020 Maintenance of Current Operations**

Agency Request	0.0	0	0	11,328,728	11,328,728	
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>11,328,728</i>	<i>11,328,728</i>	

**FY 2020 Total**

Agency Request	0.0	0	0	11,328,728	11,328,728	
<i>Governor's Recommendation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>11,328,728</i>	<i>11,328,728</i>	

Agency Request						
Change from Original Appropriation	0.0	0	0	26,672	26,672	
% Change from Original Appropriation	0.0%	0.0%	0.0%	0.2%	0.2%	
<i>Governor's Recommendation</i>						
<i>Change from Original Appropriation</i>	<i>0.0</i>	<i>0</i>	<i>0</i>	<i>26,672</i>	<i>26,672</i>	
<i>% Change from Original Appropriation</i>	<i>0.0%</i>	<i>0.0%</i>	<i>0.0%</i>	<i>0.2%</i>	<i>0.2%</i>	

**REVENUES AND STATISTICS: PERFORMANCE BASED COMPENSATION (3211)**

<b>Performance Based Compensation</b>	Actual FY 2017	Actual FY 2018	Estimated FY 2019	Estimated FY 2020
<b>PERFORMANCE INDICATORS</b>				
SDRS 1yr / 4yr / 10yr annualized returns	13.8%/9.1%/6.1%	7.94%/6.44/8.26		
Since inception 43 yrs FY 16 / 44 yrs FY 17	10.40%	10.36%		
SDRS vs Capital Market Benchmark				
Added Value 1yr / 4yr / 10yr annualized	2.9%/ .9%/1.2%	.61%/ .68%/1.75%		
Added Value Since Inception 43 yrs / 44yrs	1.00%	0.98%		
SDRS vs State Fund Universe (prelim)				
Added Value 1yr / 4yr / 10yr annualized	1.5%/ .8%/1.3%	.61%/ .07%/1.35%		
Added Value Since Inception 43 yrs / 44 yrs	1.30%	0.82%		
SDRS Investment Income (millions)				
1 year /4 years /10 years	\$1465/3706/5886	\$957/2,935/7,535		
SDRS Add'l Income vs Capital Mkts Bench (millions)				
1 year /4 years /10 years	\$299/370/1033	\$71/313/1,466		

**Trust Funds**

**Health Care Trust (established April 2001)**

Principal as of 12/31/18	\$85,631,024	Asset Allocation	Current	FY 19 Benchmark
Principal as of 12/31/18 adjusted for inflation	\$119,542,681	Global & Private Equity	42%	51%
Fair Value (FV) as of 12/31/18	\$139,382,000	Real Estate	7%	10%
Difference - FV less principal	\$53,750,976	Fixed Income-IG	21%	30%
Difference - FV less infl. adj. prin.	\$19,839,319	Fixed Income-HY	4%	7%
Fiscal year to date return	-1.65%	HY RE Debt	7%	0%
Longterm expected mean return	5.96%	Money Market	19%	2%
Payout of 4% plus expected inflation of 3%	7.00%	Total	100%	100%
Expected return cushion/shortfall	-1.04%			
Distribution for FY 20 (July 1, 2019) ESTIMATE	5,520,000	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.		
Distribution for FY 19 (July 2, 2018)	5,414,857			

**Education Enhancement Trust (established April 2001)**

Principal as of 12/31/18	\$397,235,184
Principal as of 12/31/18 adjusted for inflation	\$531,005,833
Fair Value (FV) as of 12/31/18	\$570,560,000
Difference - FV less principal	\$173,324,816
Difference - FV less infl. adj. prin.	\$39,554,167
Fiscal year to date return	-2.00%
Longterm expected return (lower due to tax-exempts)	5.92%
Payout of 4% plus expected inflation of 3%	7.00%
Expected return cushion/shortfall	-1.08%
Distribution for FY 20 (July 1, 2019) ESTIMATE	21,335,000
Distribution for FY 19 (July 2, 2018)	20,430,222

Asset Allocation	Current	FY 19 Benchmark
Global & Private Equity	44%	51%
Real Estate	6%	10%
Fixed Income-IG	9%	20%
Fixed Income-tax ex	8%	10%
Fixed Income-HY	4%	7%
HY RE Debt	6%	0%
Money Market	23%	2%
Total	100%	100%

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)**

Principal as of 12/31/18	\$238,000,000
Principal as of 12/31/18 adjusted for inflation	\$340,410,000
Fair Value (FV) as of 12/31/18	\$319,869,000
Difference - FV less principal	\$81,869,000
Difference - FV less infl. adj. principal	(\$20,541,000)
Fiscal year to date return	-1.70%
Longterm expected mean return	5.96%
Payout of 4% plus expected inflation of 3%	7.00%
Expected return cushion/shortfall	-1.04%
Distribution for FY 19 (June 2019 to GF)ESTIMATE	12,682,000
Distribution for FY 18 (June 2018 to GF)	12,442,947

Asset Allocation	Current	FY 19 Benchmark
Global & Private Equity	43%	51%
Real Estate	7%	10%
Fixed Income-IG	20%	30%
Fixed Income-HY	4%	7%
HY RE Debt	7%	0%
Money Market	20%	2%
Total	100%	100%

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.

**School & Public Lands**

Inflation protection mandated by Constitutional Amendment - (payout is reduced by inflation to extent inflation not offset by realized net gains)

Fair Value as of 12/31/18	\$298,936,000
Fiscal year to date return	-1.80%
Longterm expected mean return	5.96%
Distribution for FY 19 K-12 (2/7/19)	12,112,218
Distribution for FY 18 Board of Regents (6/6/18)	2,641,703
TOTAL	14,753,921

Asset Allocation	Current	FY 19 Benchmark
Global & Private Equity	43%	51%
Real Estate	7%	10%
Fixed Income-IG	18%	30%
Fixed Income-HY	4%	7%
HY RE Debt	6%	0%
Money Market	23%	2%
Total	100%	100%

## 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

<b>Investment Council Provided FY2020 Budget Request Summary</b>
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	Actual FY 2018	Budgeted FY 2019	Request FY 2020	% change
<b>PERSONAL SERVICES</b>				
<b>TOTAL FTEs</b>	34.25	34.25	35.25	
<b>BASE COMPENSATION</b>				
Base Compensation - Investment Staff	4,528,558	4,977,473	5,161,675	3.70%
Base Comp - Accountants, Atty, Admin, Longevity	427,722	601,764	597,219	-0.76%
<b>TOTAL STAFF - FULL TIME</b>	4,956,280	5,579,237	5,758,894	3.22%
P/T Staff Attorney & Interns	57,453	63,277	63,277	0.00%
Investment Council	2,850	6,301	6,301	0.00%
Retirement & resignation flexibility funds	0	156,961	156,961	0.00%
Benefits	1,018,601	1,075,711	1,108,847	3.08%
<b>Total Base Compensation</b>	6,035,183	6,881,487	7,094,281	3.09%
<b>Investment Performance Incentives</b>				
Maximum Potential Investment Perf Incentive	4,072,212	9,931,508	9,954,945	0.24%
Benefits	426,748	1,370,548	1,373,782	0.24%
<b>Total Investment Performance Incentives</b>	4,498,960	11,302,056	11,328,728	0.24%
<b>Total Personal Services</b>	10,534,143	18,183,543	18,423,009	1.32%
<b>OPERATING EXPENSES</b>				
Contractual Total	1,572,594	1,864,960	2,117,259	13.53%
Travel	56,549	85,000	85,000	0.00%
Office Supplies & Postage	3,948	9,000	7,000	-22.22%
Capital Assets	59,194	40,520	40,520	0.00%
<b>Total Operating Expenses</b>	1,692,285	1,999,480	2,249,779	12.52%
<b>TOTAL BUDGET</b>	12,226,429	20,183,023	20,672,788	2.43%
<b>UNIT COST SUMMARY *</b>				
Internal Expenses as % of Total Adjusted Assets	0.084%	0.094%	0.094% **	
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

\*\* Unit cost includes an assumed 2.25% salary policy

## Other Fund Balance History

Company	60 Month Average	Minimum Balance	Most Recent Occurrence of Minimum	Balance on June 30				
				2014	2015	2016	2017	2018
3017 - INVESTMENT OF STATE FUNDS	3,425,939	(115,382)	August 2013	1,247,180	3,865,242	1,894,306	1,929,561	2,451,347
8000 - INVESTMENT OF STATE FUNDS	8,589,508	708,303	July 2013	8,621,677	16,448,082	17,793,314	15,854,764	15,637,582

## Historical Budget Changes

<u>Investment Council</u>	General Funds	Federal Funds	Other Funds	Total Funds	FTEs
<b>FY14 Budget Increases</b>					
<ul style="list-style-type: none"> <li>Personal Services- Base Salary Increase According to Long Term Plan &amp; 2 New FTEs</li> <li>Performance Based Compensation</li> </ul>			519,707	519,707	2.0
			803,485	803,485	
<b>FY15 Budget Increases</b>					
<ul style="list-style-type: none"> <li>Personal Services - Base Salaries and Benefits</li> <li>Miscellaneous Operating Expenses</li> <li>Performance Based Compensation</li> </ul>			289,920	289,920	
			115,560	115,560	
			4,624,945	4,624,945	
<b>FY16 Budget Increases</b>					
<ul style="list-style-type: none"> <li>Two New Research Analysts</li> <li>Part Time Staff Attorney</li> <li>Base Salary and Promotional Increases</li> <li>Miscellaneous Contractual Services</li> <li>Capital Outlay</li> <li>Performance Based Compensation</li> </ul>			147,454	147,454	2.0
			32,456	32,456	0.3
			291,943	291,943	
			41,855	41,855	
			4,192	4,192	
			796,804	796,804	
<b>FY17 Budget Increases</b>					
<b>FY2017 Line Items</b>					
<ul style="list-style-type: none"> <li>Base Salary, Promotional Increases</li> <li>Contractual Services</li> <li>Capital Outlay</li> <li>Performance Based Compensation</li> </ul>			187,818	187,818	
			50,904	50,904	
			(2,792)	(2,792)	
			1,000,708	1,000,708	
<b>FY18 Budget Increases</b>					
<b>Maintenance of Current Operation Items</b>					
<ul style="list-style-type: none"> <li>Change in Employee Compensation</li> </ul>			765,956	765,956	
<b>FY2018 Line Items</b>					
<ul style="list-style-type: none"> <li>Additional Investment FTEs</li> <li>Investment Research Services</li> </ul>			151,817	151,817	2.0
			55,100	55,100	

**Investment Council**

	<b>General Funds</b>	<b>Federal Funds</b>	<b>Other Funds</b>	<b>Total Funds</b>	<b>FTEs</b>
<b>FY19 Budget Increases</b>					
<b>Maintenance of Current Operation Items</b>					
Contract Inflation	0	0	7,975	7,975	0.0
Capital Outlay One-Time Expense	0	0	1,100	3,200	0.0
Bureau Billing Increase	0	0	4,090	4,090	0.0
Base Salaries Increases	0	0	669,991	669,991	0.0
Capital Outlay One-Time Adjustment	0	0	(4,833)	(4,833)	0.0
<b>FY2019 Line Items</b>					
Legal Services for Distressed Debt Investments	0	0	50,000	50,000	0.0
Investment Research Services	0	0	62,640	62,640	0.0
Add Office Space	0	0	9,540	9,540	0.0