



Virginia
Retirement
System

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September 12, 2013

The Honorable Robert F. McDonnell
Governor of Virginia
P.O. Box 1475
Richmond, VA 23218

The Honorable Lacey E. Putney
Chairman, House Appropriations Committee
House of Delegates
P.O. Box 127
Bedford, VA 24523

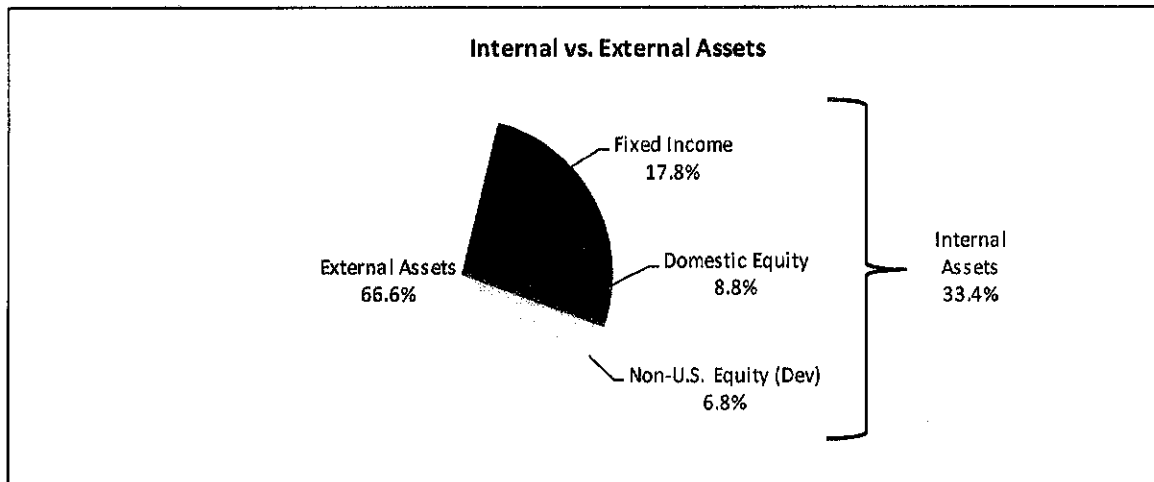
The Honorable Walter A. Stosch
Chairman, Senate Finance Committee
Senate of Virginia
4551 Cox Road, Suite 110
Glen Allen, VA 23060-6740

Re: Report on Virginia Retirement System Internal Asset Management

Dear Governor McDonnell, Chairman Putney and Chairman Stosch:

Pursuant to Item 483 of Chapter 806, 2013 Acts of Assembly (The Appropriations Act), I am pleased to provide a report on the fiscal 2013 results obtained by the internal investment management program at the Virginia Retirement System ("VRS").

The VRS internal investment management program continues to make an important contribution to the total fund. As of June 30, 2013, the internal investment management team managed a total of \$19.5 billion in assets (excludes the Currency Hedge Account), representing approximately 33.4% of the fund. This amount consisted of \$9.1 billion managed in equity related strategies, and \$10.4 billion managed in fixed income strategies. The following pie chart provides the breakdown between internally and externally managed assets as of June 30, 2013. In addition, I am attaching, as a supplementary exhibit, a schedule that shows the various investment mandates being managed internally by VRS staff at fiscal yearend.



The VRS Board of Trustees has established certain external benchmarks for evaluating portfolio managers and believes that intermediate time frames of 3 to 5 years are most useful for evaluating performance. I am pleased to report that the internally managed funds continued to demonstrate outstanding performance across both the 3- and 5-year periods ending on June 30, 2013, as demonstrated in the following table. We estimate that the value added to the total fund from these excess returns over the last 5 years is approximately \$511.5 million.

IAM Track Record as of June 30, 2013			
		3 Years	5 Years
Equity Mandates	Portfolio	18.0 %	7.3 %
	Benchmark	15.5 %	5.9 %
	Excess	2.5 %	1.4 %
Fixed Income Mandates	Portfolio	3.8 %	6.5 %
	Benchmark	3.5 %	6.0 %
	Excess	0.3 %	0.5 %

In addition to outstanding performance, the internal asset management team continues to operate at a low level of cost when compared to fees that would be charged by outside managers who offer similar strategies. We estimate that by managing these strategies internally the VRS is saving approximately \$11.4 million annually.

The Board of Trustees is proud of the efforts and results of the internal asset management team at VRS, and we are confident that the fund will continue to benefit from their work in the years ahead.

Sincerely,

Diana F. Cantor
Chairman, VRS Board of Trustees

EXHIBIT A

VRS Internal Mandates as of June 30, 2013			
Asset Class	Objective	Assets (MM)	
Equity	Passive U.S. Large	\$181.8	
	Passive Non-U.S. Large	\$716.3	
	Active U.S. Large	\$2,499.4	
	Active Non-U.S. Large	\$1,632.2	
	Active U.S. Small	\$286.2	
	Active U.S. Small Synthetic	\$127.1	
	Active U.S. REIT	\$76.4	
	Active U.S. Large Low Volatility	\$1,673.8	
	Active Non-U.S. Large Low Volatility	\$1,270.2	
	Rebalancing Account	\$636.1	
	Currency Hedge (Overlay)	\$2,733.7	
		Subtotal	\$11,833.2
	Fixed Income	Collateralized	\$3,008.9
Credit		\$3,721.3	
Government Related		\$3,669.2	
Rate Overlay		\$20.9	
		Subtotal	\$10,420.3
	Total	\$22,253.5	