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September 24, 2015

The Honorable Terence R. McAuliffe  
Governor of Virginia  
1111 East Broad Street  
Richmond, Virginia 23219

The Honorable Charles J. Colgan  
Co-Chairman, Senate Finance Committee  
Senate of Virginia  
10660 Aviation Lane  
Manassas, Virginia 20110

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

The Honorable S. Chris Jones  
Chairman, House Appropriations Committee  
House of Delegates  
P.O. Box 5059  
Suffolk, Virginia 23435

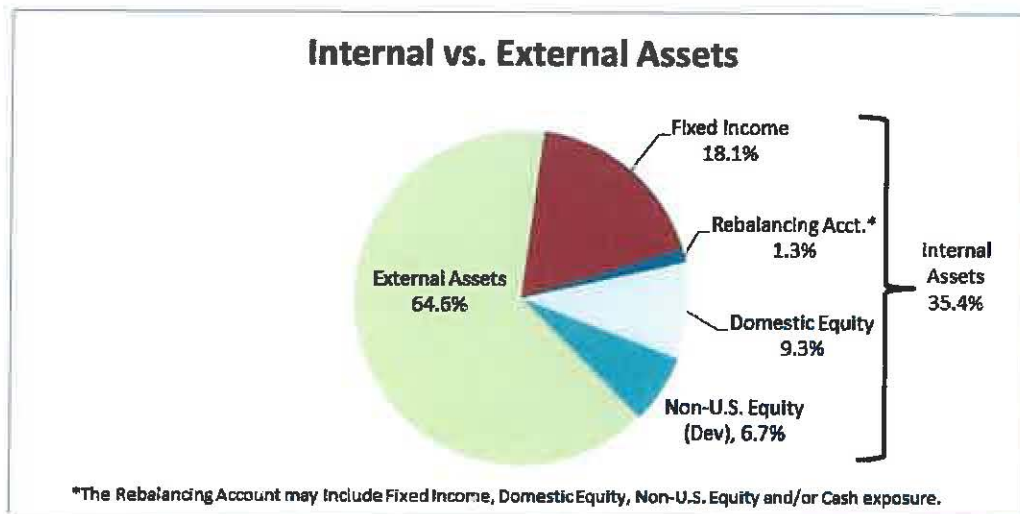
Re: Report on Virginia Retirement System Internal Asset Management

Dear Governor McAuliffe, Co-Chairman Colgan, Co-Chairman Stosch and Chairman Jones:

Pursuant to Item 483 of Chapter 2, 2014 Special Session I Acts of Assembly (The "Appropriations Act"), I am pleased to provide a report on the fiscal 2015 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, 2015, the internal investment management team managed a total of \$24.1 billion in assets (excludes the Currency Hedge Account), representing approximately 35.4% of the fund. This amount consisted of \$11.8 billion managed in equity related strategies, and \$12.3 billion managed in fixed income strategies. The following pie chart provides the breakdown

between internally and externally managed assets as of June 30, 2015. 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 year end.



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 strong performance relative to policy benchmarks across both the 3 and 5 year periods ending on June 30, 2015, as demonstrated in the following table. We estimate that the value added to the total fund from these excess returns over the last 10 years is approximately \$926 million.

IAM Track Record as of June 30, 2015			
		3 Years	5 Years
Equity Mandates	Portfolio	16.0%	16.7%
	Benchmark	14.8%	14.4%
	Excess	1.2%	2.3%
Fixed Income Mandates	Portfolio	2.3%	3.6%
	Benchmark	1.8%	3.3%
	Excess	0.5%	0.3%

The Honorable Terence R. McAuliffe, The Honorable Charles J. Colgan, The Honorable Walter A. Stosch  
and The Honorable S. Chris Jones

Page 3

September 24, 2015

In addition to strong performance relative to policy benchmarks, 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 \$23 million annually based on an outside consultant's data.

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,

A handwritten signature in black ink, appearing to read "Robert L. Greene", with a long horizontal flourish extending to the right.

Robert L. Greene  
Chairman, VRS Board of Trustees

Attachment

**EXHIBIT A**

<b>VRS Internal Mandates as of June 30, 2015</b>		
<b>Asset Class</b>	<b>Objective</b>	<b>Assets (MM)</b>
<b>Equity</b>	Passive, U.S. Large Cap	\$405.1
	Passive, Non-U.S. Large Cap	\$261.2
	Low Tracking Error, U.S. Large	\$4,301.6
	Low Tracking Error, Non-U.S. Large	\$2,325.1
	Low Tracking Error, U.S. Small	\$367.4
	Low Tracking Error, U.S. REIT	\$331.0
	Low Volatility, U.S. Large Cap	\$907.6
	Low Volatility, Non-U.S. Large	\$1,983.5
	Rebalancing Account	\$896.2
	Currency Hedge (Overlay)	\$3,892.5
	<b>Subtotal</b>	<b>\$15,671.2</b>
<b>Fixed Income</b>	Securitized	\$3,920.8
	Credit	\$4,089.0
	Government Related	\$4,286.9
	Rate Overlay	\$12.4
	<b>Subtotal</b>	<b>\$12,309.1</b>
	<b>Total</b>	<b>\$27,980.3</b>