Employees' Retirement System of the Government of the Virgin Islands

Presentation for September Legislative Meetings

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All May Seem Well and Good…
As Investment Performance Has Been Strong

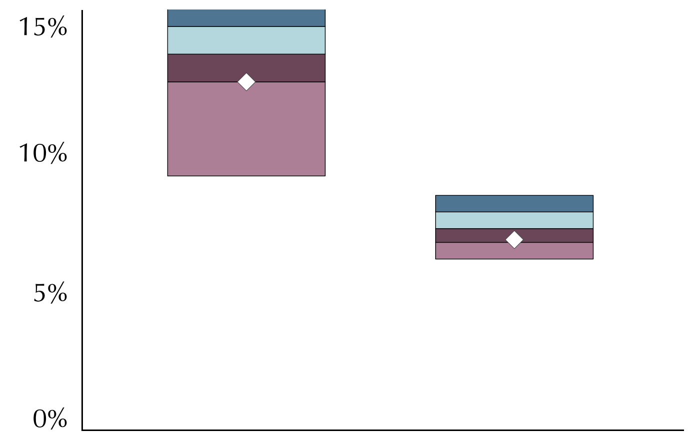
- The Employees' Retirement System of the Government of the Virgin Islands ("GERS" or "the Retirement System") has produced an annualized return of 9.3% going back to 1981.
- Even with the impact of the Global Financial Crisis of 2008, GERS still produced an annualized return higher than the actuarial assumed rate of 7.5%.

Trailing Performance as of Most Recent Fiscal Year End

	1 YR (%)	3 YR (%)	5 YR (%)	10 YR (%)	Inception Date	Since Inception (%)
GERS Aggregate Performance[1]	**8.5**	**12.4**	**9.0**	**6.7**	**7/1/81**	**9.3**
All Public Plans-Total Fund Median	10.2	13.4	10.2	7.1		NA

[1] Performance is gross of fees and listed as of most recent fiscal year end (9/30/2014) and only includes the performance of the assets held at GERS' custodian bank (State Street). It excludes member loans and local assets which have averaged over $200 million per year over the last ten years.

GERS Has Generally Performed In-Line with Peers



	3 YR (%)	10 YR (%)
GERS Aggregate Performance[1]	**12.4**	**6.7**
All Public Plans Total Fund Top 25th	14.4	7.7
All Public Plans Total Fund Median	13.4	7.1
All Public Plans Total Fund Bottom 75th	12.4	6.6

- Over the trailing ten year period the Retirement System trails slightly the median pension plan by 0.4%.

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GERS Has Taken Steps to Reduce Investment Costs

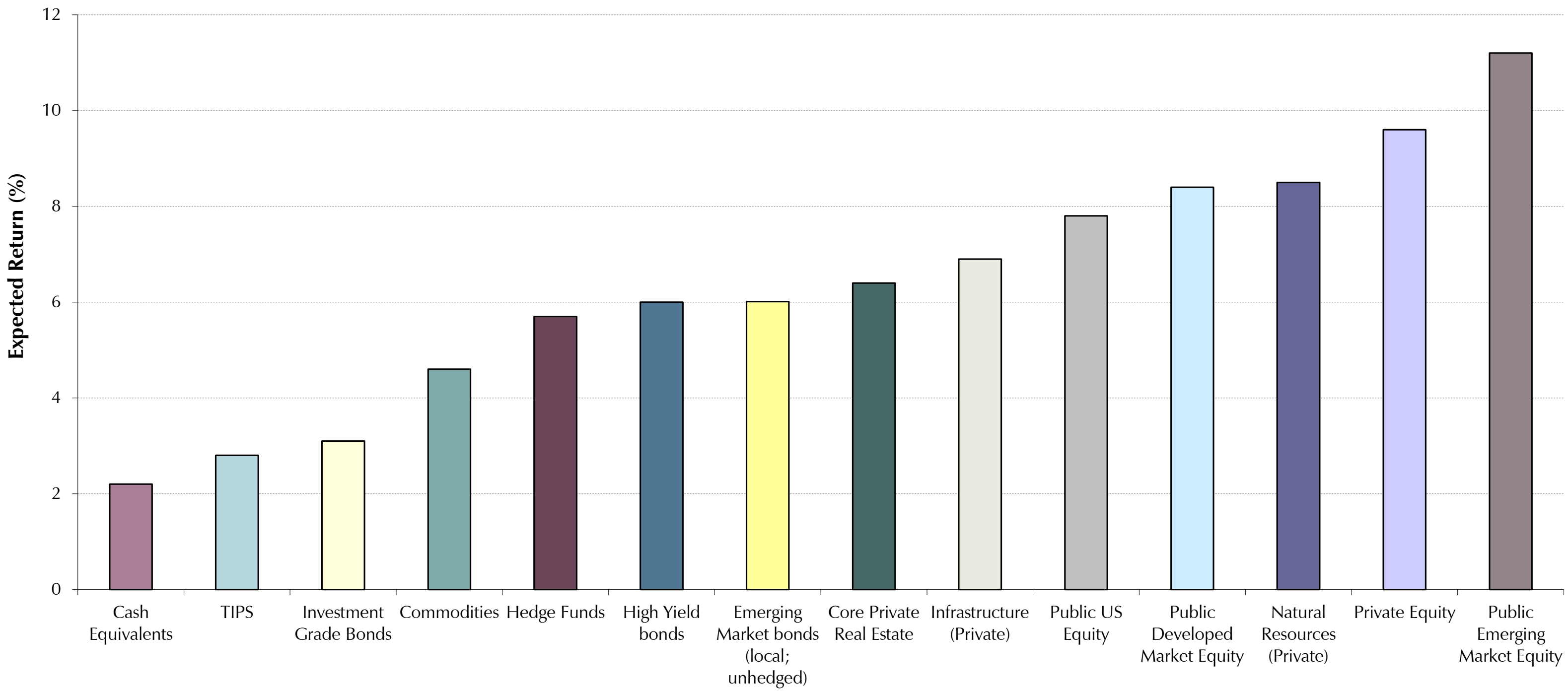
- In 2014 the Board of Trustees voted to consolidate overlapping managers and use index funds for efficient asset classes.
- Meketa Investment Group estimates the adjustments save the Retirement System approximately $1 million in fees, annually, compared to the prior structure.
- Relative to peer plans, the Retirement System pays less in investment management fees (0.36% annually[1] vs. industry average[2] of 0.44% annually)
- Using the peer plan fees as a comparison results in savings of approximately $650,000 per year (based on current asset levels).

[1] Calculation is the sum of the total estimated management fees paid each year of the assets listed divided by the total market value (of the assets listed) as of March 31, 2015.

[2] Based on article published in Pension and Investments of survey of plans with total assets of $220 billion in aggregate.

GERS Has Taken Steps to Maximize Potential Returns within the Current Limitations of the Code

- The Code places position restrictions on international equities and restricts non-investment grade bonds.
- According to Meketa Investment Group's annual Asset Study[1], we believe that only a few asset classes (in isolation) are expected to produce annualized returns in excess of 7.5%. GERS is currently restricted or prohibited from investing in many of these asset classes.



[1] Twenty-year expected returns based upon Meketa Investment Group's 2015 Annual Asset Study.

However, Investment Returns Alone Cannot Solve GERS' Funding and Liquidity Issues… Capital Infusion into the System and a Revision of the Code are Needed

- As the investment base shrinks (with cash outflows), the annual required investment return to meet those benefit payments becomes prohibitively large and unattainable.
- The longer the wait, the more challenging the situation becomes.
- With a cash infusion, the asset base of the Retirement System will increase. The investment return needed each year (percentage rate of return) on a larger base of assets is lower to pay the same (or similar) nominal required benefit payments.
- A $600 million cash infusion has been discussed in the past. If it were to materialize, Meketa Investment Group would recommend more flexibility in the Code to maximize the return potential of the capital at work. Specifically, we would suggest:
  - Increasing equity investments outside of the United States
  - Diversifying the public fixed income exposure in a greater array of bonds
  - Investing in additional private market fund investments that offer the potential for higher returns

Return/Risk Should Not Be Viewed In Isolation

- No one can predict asset class returns in any given year. The flexibility to pursue a variety of asset classes with different return/risk profiles will allow GERS to create a more efficient portfolio (i.e., better return to risk ratio).

2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Emerging Markets Debt 9.7%	Commodities 25.9%	Emerging Equity 55.8%	Emerging Equity 25.6%	Emerging Equity 34.0%	Emerging Equity 32.2%	Emerging Equity 39.4%	Bonds 5.2%	Emerging Equity 78.5%	Emerging Equity 18.9%	Real Estate 14.3%	Emerging Equity 18.2%	US Equity 32.4%	Private Equity 17.6%
Bonds 8.4%	TIPS 17.0%	EAFE Equity 39.1%	Emerging Markets Debt 23.0%	Private Equity 30.4%	EAFE Equity 26.3%	Private Equity 26.6%	Cash 1.7%	High Yield 58.2%	Commodities 16.7%	TIPS 14.1%	EAFE Equity 17.3%	EAFE Equity 22.8%	US Equity 13.7%
TIPS 8.0%	Emerging Markets Debt 13.7%	High Yield 29.0%	EAFE Equity 20.6%	Commodities 21.4%	Private Equity 18.6%	Emerging Markets Debt 18.1%	TIPS -1.1%	EAFE Equity 31.8%	Private Equity 15.7%	Private Equity 12.0%	Emerging Markets Debt 16.8%	Private Equity 18.1%	Real Estate 11.8%
Real Estate 7.2%	Bonds 10.2%	US Equity 28.7%	Private Equity 15.9%	Real Estate 20.1%	Real Estate 16.6%	Commodities 16.2%	Emerging Markets Debt -5.2%	US Equity 26.5%	Emerging Markets Debt 15.7%	Bonds 7.8%	US Equity 16.0%	Real Estate 11.0%	Bonds 6.0%
High Yield 5.3%	Real Estate 6.7%	Commodities 24.0%	Real Estate 14.5%	EAFE Equity 13.5%	US Equity 15.8%	Real Estate 15.8%	Real Estate -6.5%	Emerging Markets Debt 22.0%	High Yield 15.1%	High Yield 5.0%	High Yield 15.8%	Hedge Funds 8.7%	TIPS 4.5%
Hedge Funds 4.6%	Cash 1.6%	Hedge Funds 19.5%	High Yield 11.1%	Hedge Funds 9.3%	Emerging Markets Debt 15.2%	TIPS 11.6%	Private Equity -7.1%	Hedge Funds 20.0%	US Equity 15.1%	US Equity 2.1%	Private Equity 14.5%	High Yield 7.4%	Hedge Funds 3.3%
Cash 3.8%	High Yield -1.4%	Emerging Markets Debt 16.9%	US Equity 10.8%	Emerging Markets Debt 6.3%	Hedge Funds 12.9%	EAFE Equity 11.2%	Hedge Funds -19.0%	Commodities 18.9%	Real Estate 13.1%	Cash 0.1%	Real Estate 10.5%	Cash 0.0%	High Yield 2.5%
Emerging Equity -2.6%	Hedge Funds -1.4%	Real Estate 8.9%	Commodities 9.2%	US Equity 4.9%	High Yield 11.9%	Hedge Funds 10.0%	High Yield -26.2%	TIPS 10.0%	Hedge Funds 10.2%	Emerging Markets Debt -1.8%	TIPS 7.3%	Bonds -2.0%	Cash 0.0%
US Equity -11.8%	Emerging Equity -6.2%	TIPS 8.3%	Hedge Funds 9.0%	Cash 3.0%	Cash 4.6%	Bonds 7.0%	Commodities -35.6%	Bonds 5.9%	EAFE Equity 7.8%	Hedge Funds -5.2%	Hedge Funds 6.4%	Emerging Equity -2.6%	Emerging Equity -2.2%
Commodities - 19.5%	Private Equity -14.1%	Private Equity 7.3%	TIPS 8.5%	TIPS 2.8%	Bonds 4.3%	US Equity 5.5%	US Equity -37.0%	Cash 0.1%	Bonds 6.5%	EAFE Equity -12.1%	Bonds 4.2%	Emerging Markets Debt -9.0%	EAFE Equity -4.9%
EAFE Equity -21.2%	EAFE Equity -15.6%	Bonds 4.1%	Bonds 4.3%	High Yield 2.7%	Commodities 2.1%	Cash 4.7%	EAFE Equity -43.4%	Private Equity -6.6%	TIPS 6.3%	Commodities -13.4%	Cash 0.1%	TIPS -9.4%	Emerging Markets Debt -5.7%
Private Equity -25.6%	US Equity -22.1%	Cash 1.0%	Cash 1.2%	Bonds 2.4%	TIPS 0.5%	High Yield 1.9%	Emerging Equity -53.3%	Real Estate -16.9%	Cash 0.1%	Emerging Equity -18.4%	Commodities -1.1%	Commodities -9.5%	Commodities -17.0%

Suggested Road Map for a $600 million Cash Infusion – Revised Code

- Priority One – Increase international equity exposure
  - The Retirement System currently has $108.5 million invested in international equities (approximately 14%), as of June 30, 2015. While performance between U.S. equities and international equities will fluctuate in cycles over time, Meketa Investment Group believes international equities offer high, long-term return potential for investors as well as diversification benefits.
- Priority Two – Diversify Fixed Income exposure
  - Currently the System is only allowed to purchase investment grade bonds. As of June 30, 2015 the yield on the Barclays Aggregate (a proxy for the U.S. investment grade bond universe) was 2.4%. We believe that the flexibility to invest in non-investment grade bonds will offer higher return potential for the Retirement System as well as diversification benefits.
- Priority Three – Reduce Liquidity Concerns Efficiently
  - Getting an infusion of cash into the Retirement System buys GERS much needed time to begin considering and implementing an orderly liquidation plan for some of the local illiquid investments. We believe that if the Retirement System continues on a path to insolvency and does not get a meaningful cash infusion, there is a risk these assets will need to be sold in a short timeframe and GERS may be forced to accept weak offers.
- Priority Four – Continue to Monitor Investment Costs
  - Any dollar spent on investment management fees is a dollar out of the Retirement System. Staff and Meketa Investment Group will remain diligent and seek to continue to reduce investment costs for GERS' portfolio.

Suggested Road Map for a No-Cash-Infusion Scenario

- There will be no need/urgency in modifying the Code.
- As the pool of assets depletes from large benefit payments, the investment return will not matter.
- At some point, contributions paid into the Retirement System will be immediately paid out in benefit checks.
- If the Retirement System produces a 7.5% return every year (its stated goal) it still will not matter. The Retirement System should become insolvent in less than ten years.
- If a drastic market correction occurs (i.e., equity markets down 20% or more) the Retirement System could become insolvent within five years.
- GERS may consider a "soft landing" path to try to prevent a rapid decline in assets scenario. Such scenario would alter the asset allocation of the Retirement System, leading to a lower estimated rate of return, but with commensurate higher predictability of returns (e.g., lower volatility).

If the Cash Infusion and Code Amendment Are Not Approved…

- Local asset investments will need to be sold to meet cash needs.
  - Selling assets in distress will result in less than market value sale prices.
- The GERS loan program will need to be stopped.
- The Retirement System will reach insolvency.
- The domino effect will be significant.
  - Currently GERS pays approximately $250 million a year in benefit payments, but the economic impact is much greater. For each dollar spent in the Virgin Islands, there is a "multiplier effect."
  - NIRS (National Institute on Retirement Security) estimates that the multiplier effect[1] of pension benefits is 2.4x.
  - Thus the yearly impact of benefit payments is approximately $600 million into the Virgin Islands GDP.
  - Without the Retirement System, or a Retirement System that is only capable of paying out a fraction of earned benefit payments, the local economy of the Virgin Islands may take a significant negative hit.
  - As conditions worsen, hard working employees may leave the islands, the population may decrease, and local economy could spiral into a depression.

[1] http://www.nirsonline.org/storage/nirs/documents/Pensionomics%202009/nirs_2009_pensionomics_report_final.pdf

Summary and Recommendations

- The situation is dire, and action is needed now.
- The longer the wait, the worse the situation becomes.
- An increase of cash into GERS prolongs the life of the Retirement System.
- With additional assets and flexibility, Meketa Investment Group recommends revising the asset allocation.
  - Increase non-U.S. equity exposure.
  - Diversify fixed income.
  - Use private market funds strategically.