

Retirement Fund Annual Summary

Published by the Arlington County Employee Retirement System Investment Office

2100 Clarendon Boulevard, Suite 504, Arlington, VA 22201

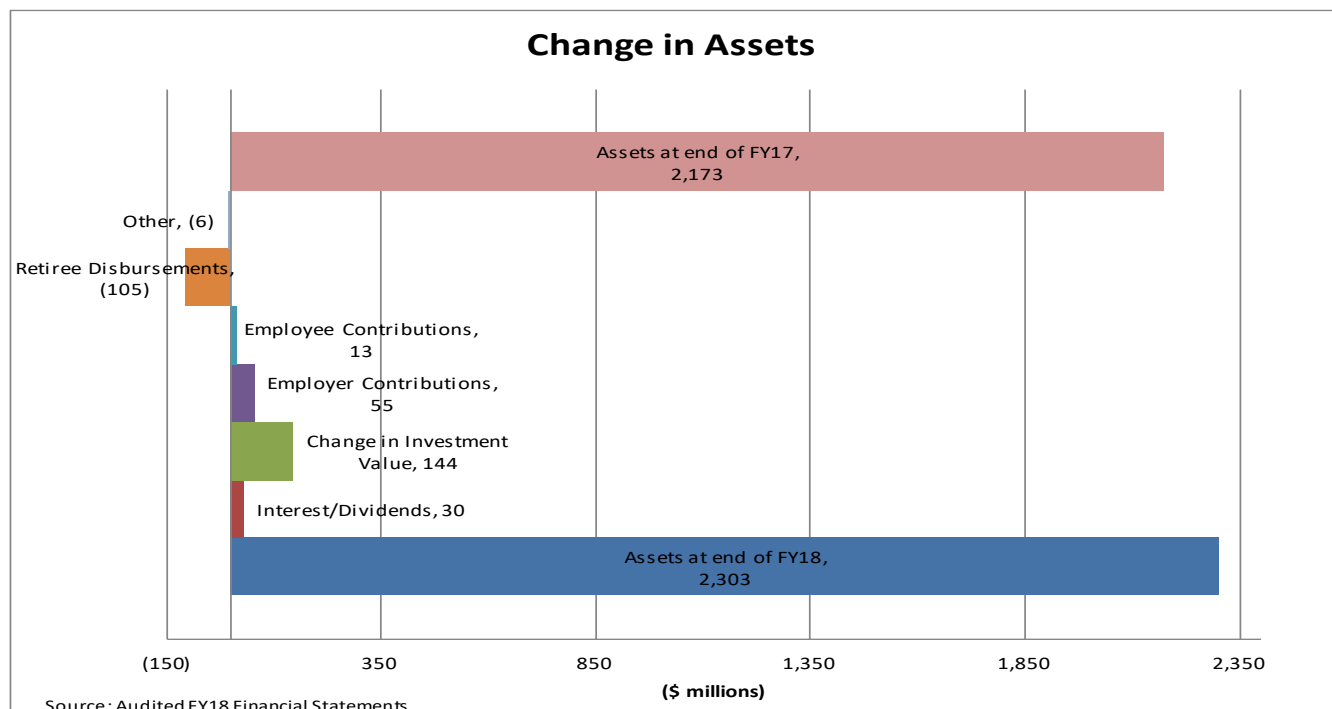
Telephone: (703) 228-3321 Fax: (703) 228-0646

Arlington's Retirement System remains financially and actuarially sound. The System's position results from regular contributions from members and Arlington County combined with better than average investment returns over the long term. With \$2,303 million in net assets at June 30, 2018 and a funded status of 104.4%, the System remains well positioned to meet its obligations.

Financial Highlights

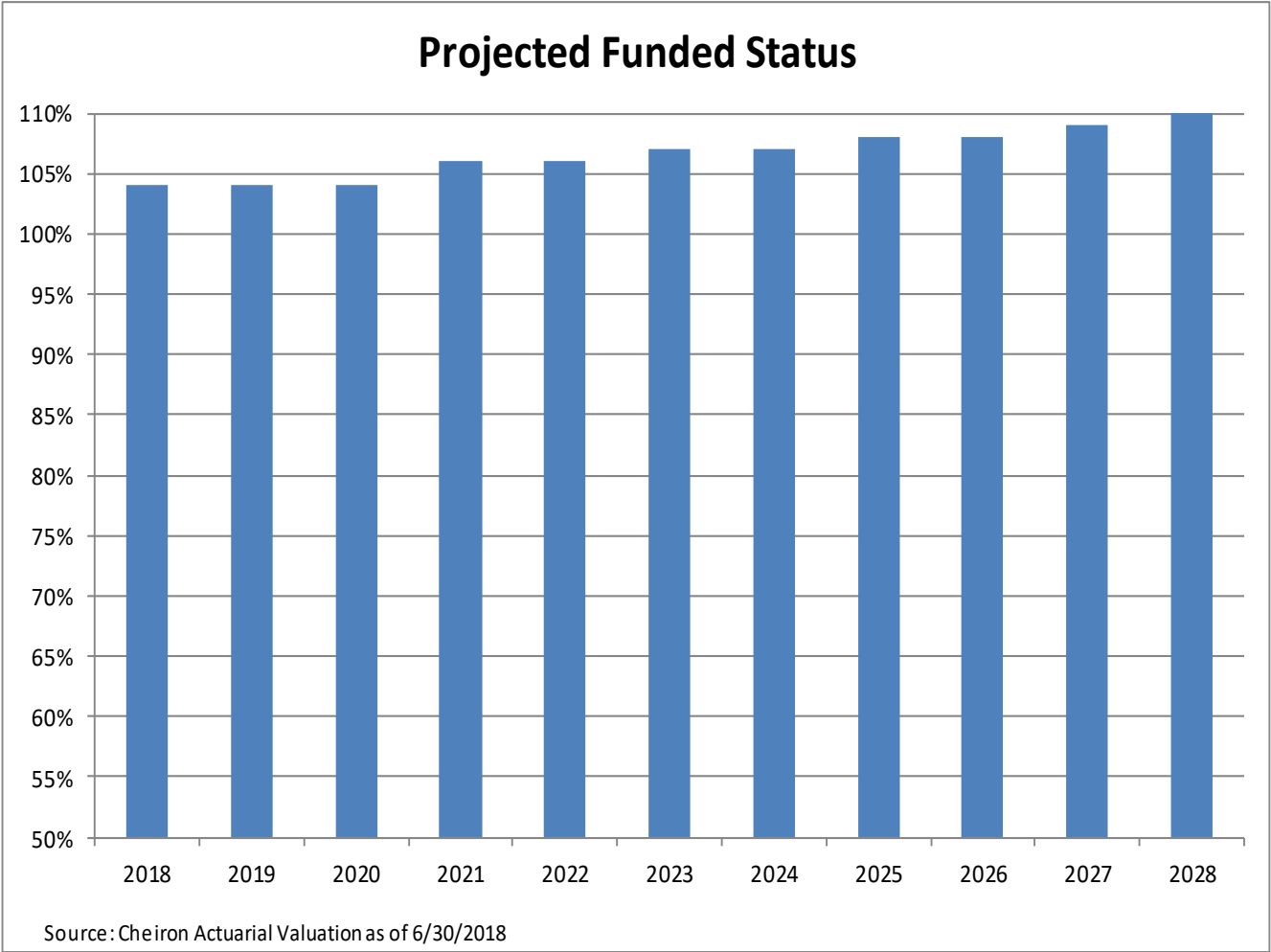
For the year ended June 30, 2018:

- Net assets increased by \$129 million to \$2,303 million, primarily due to an increase in the value of investments.
- The System's 0.9% investment outperformance relative to the overall policy benchmark was primarily attributable to strong returns from growth-oriented global equity managers and an underweight allocation to fixed income. The fiscal year return of 8.0% was below the 8.6% median return of the TUCS Public Plan Universe, placing the System in the 70th percentile (3rd Quartile) of public plans for the year. On a 3, 5 and 10-year basis, the System's performance ranked in the 61st, 60th and 43rd percentiles, respectively.
- Employer contributions totaled \$54.9 million and employee contributions totaled \$12.7 million. Dividend and interest income totaled \$29.8 million.
- Retirement benefit payments, including refunds paid to former members, totaled \$105.0 million.



Funded Status

Each year, the Retirement Board conducts an actuarial valuation to determine funding requirements. A retirement system is considered fully funded from an actuarial perspective when there is enough money in reserve to meet all accrued obligations to participants. The funded ratio varies each year driven primarily by investment returns. Fiscal year 2018’s funded ratio of 104.4%, which compares favorably to other public plans, was calculated using June 30, 2018 data. The 8.0% investment return for the year exceeded the 6.75% actuarial rate of return assumption. Assuming all actuarial assumptions are met in the future, the funded ratio is projected to remain at 104% in 2019 and to increase gradually to 110% in ten years.



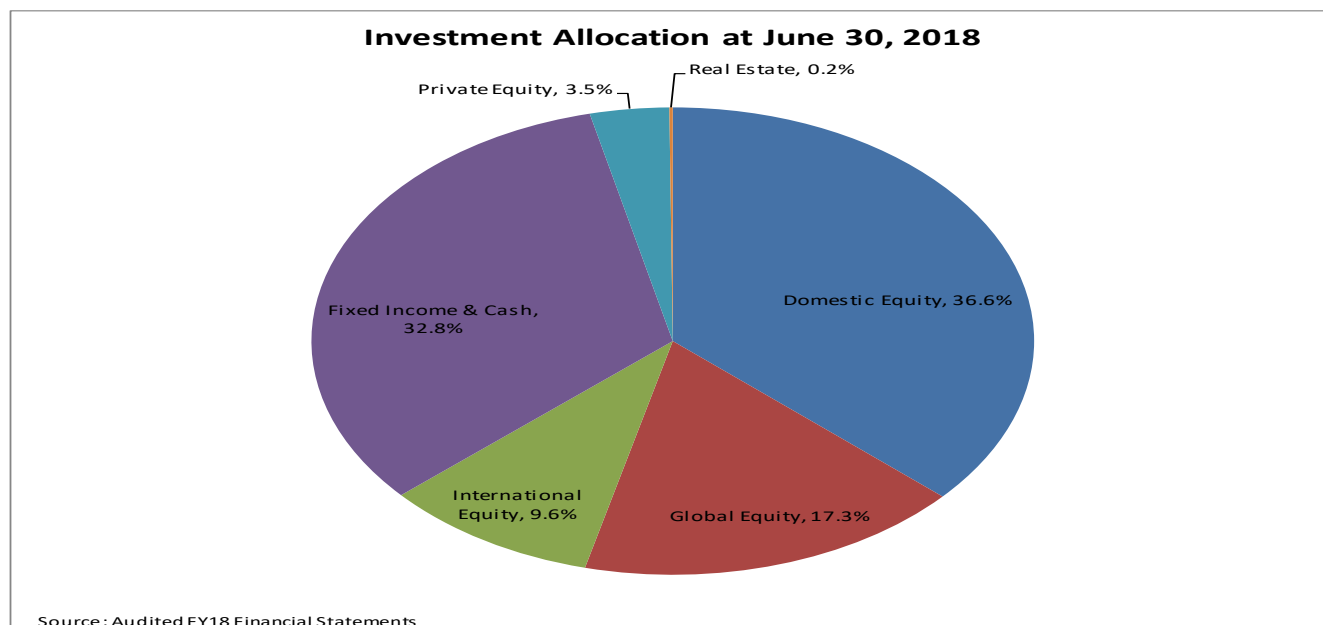
Investments

The Retirement Board has adopted a written investment policy under the authority provided by the Arlington County Code. The Board operates with the standard of care required in making investments as stated in the Code of Virginia §51.1-803 which states that “funds... shall be invested with the care, skill, prudence and diligence ... that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with the same aims.” Arlington County Code allows for the engagement of professional investment managers.

The financial markets performed above expectations during fiscal year 2018, setting the stage for the System to outperform its primary investment objective for the year, while longer term results exceed or equal the Fund’s objectives. Fiscal year 2018 started benefitting from the steady flow of positive economic data and corporate earnings reports. The move higher in domestic equities was also supported by details of the newly passed US tax plan. In fixed income, geopolitical tensions and low inflation served to minimize the rise in yields caused by strong economic conditions and expectations of tighter monetary policy. Global equity markets capped off a strong 2017 supported by signs of strengthening economic growth and robust corporate earnings. Fixed income performance was mostly positive, with longer term high quality bonds providing the highest returns. The Federal Reserve proceeded to raise short term policy rates. Markets greeted 2018 with higher volatility caused by fears that rising inflation may lead to a more aggressive pace of interest rate increases and concerns over the possibility of a global trade war unsettled markets. Fixed income markets also declined due to rising inflation expectations and the prospect of tighter monetary policy. Volatility remained in the second quarter. Returns for international investments were particularly impacted by a strong US dollar. Fixed income markets offered subdued returns and interest rates and credit spreads ticked modestly higher. The Federal Reserve raised interest rates in June.

From an investment perspective, the Board acted at several points during the year to manage the portfolio’s risk/return profile considering developments in the capital markets. The System’s investment portfolio remains well diversified and strives to balance capital preservation in down markets with generating a 6.75% return over the long term.

As of June 30, 2018, the System followed its investment policy guidelines and fixed income investments and cash equivalents totaled 32.8% of assets.



Other Post Employment Benefits

In February 2009, the Retirement Board voted to act as Trustee with investment oversight for two trusts, one for County funds and one for School funds, invested to prefund Other Post-Employment Benefits (OPEB) such as health care. Authority for a local retirement board to act as Trustee for OPEB assets is provided for in Virginia Code §15.2-1547. Additional funding of \$7.2 million for the County trust and \$2.6 million for the School trust were made during fiscal year 2018. As of June 30, 2018, the County and School trusts had assets of \$130 million and \$54 million, respectively. These trusts are completely separate and independently managed from Retirement System assets. The OPEB trusts are managed in accordance with an Investment Policy Statement tailored to their needs. Detailed financial reporting for the OPEB trusts is included in the County and School annual financial reports.

Website Updates

The Retirement Office posts fund updates quarterly providing information on investment balances, performance and asset allocation. In addition, the website contains information such as Retirement Board meeting agendas, meeting minutes, System history and contact information. A detailed description of the two offices responsible for the System — Investment and Benefits — is also included. To reach the site directly, please visit www.careers.arlingtonva.us/retirement-investment-office

Detailed Information

The tables that follow provide additional detailed information. Specifically:

- Table 1 – Investment Performance
- Table 2 – Plan Net Assets
- Table 3 – Asset Allocation
- Table 4 – Contribution Analysis
- Table 5 – Participant Data

Table 1
Arlington County Employees' Retirement System
Investment Performance Summary
(Returns for periods greater than one year are annualized)

				Fiscal Year Ended June 30				
	10 Years	5 Years	3 Years	2014	2015	2016	2017	2018
Investment Performance (gross of fees)								
Total Fund ⁽¹⁾ (Benchmark)	7.1%	8.2%	7.0%	18.4%	2.2%	0.3%	12.9%	8.0%
Domestic Equities (Russell 3000)	7.9%	9.9%	8.6%	22.2%	2.5%	0.7%	15.5%	10.2%
Global Equities (MSCI AC World)	9.3%	15.6%	13.8%	31.8%	6.1%	-2.8%	27.8%	18.5%
International Equities (MSCI AC World ex-US)	5.1%	6.9%	6.3%	18.7%	-2.3%	-8.6%	23.6%	6.2%
Fixed Income (Fixed Income)	4.7%	3.0%	2.4%	7.3%	0.5%	4.1%	2.6%	0.6%
Benchmark Performance								
Total Fund ⁽²⁾	6.5%	7.5%	6.5%	15.8%	2.6%	1.5%	11.1%	7.1%
Russell 3000	10.2%	13.3%	11.6%	25.2%	7.3%	2.1%	18.5%	14.8%
MSCI AC World	5.8%	9.4%	8.2%	23.0%	0.7%	-3.7%	18.8%	10.7%
MSCI AC World ex-US	2.5%	6.0%	5.1%	21.8%	-5.3%	-10.2%	20.5%	7.3%
Fixed Income ⁽³⁾	4.1%	2.6%	2.1%	5.2%	1.5%	5.8%	0.9%	-0.3%
CPI + 3.75% Annualized ⁽⁴⁾	5.0%	5.2%	5.5%	5.6%	3.6%	4.5%	5.4%	6.6%
Actuarial Assumed Rate of Return				7.25%	7.25%	7.25%	6.75%	6.75%

⁽¹⁾ Includes cash and alternative investment performance though returns for these asset classes are not listed separately

⁽²⁾ 40% RU 3000, 17.5% MSCI AC World ex-US, 39% BC Universal, 1.5% BC TIPS & 2% 90 Day T-Bill

Prior to 10/1/07, 43% RU 3000, 14% EAFE, 38% BC Aggregate & 5% 90 Day T-Bill

⁽³⁾ Weights fixed income benchmark components to 100%

⁽⁴⁾ 3.75% as of 7/1/16, 3.5% prior

Table 2
Plan Net Assets for Year Ended June 30

	2014	2015	2016	2017	2018
Beginning	\$1,696.8	\$1,979.6	\$1,995.1	\$1,963.5	\$2,173.9
Additions	370.5	107.7	65.4	311.8	236.1
Deductions	87.7	92.2	97.0	101.4	106.9
Net Change	282.8	15.5	(31.6)	210.4	129.2
Year End	\$1,979.6	\$1,995.1	\$1,963.5	\$2,173.9	\$2,303.1

Table 3
Asset Allocation at June 30, 2018

<u>Asset Class</u>	<u>Millions</u>	<u>% of fund</u>
Domestic Equity	\$841.8	36.6%
Global Equity	\$398.6	17.3%
International Equity	\$221.7	9.6%
Fixed Income & Cash	\$753.9	32.8%
Private Equity	\$81.5	3.5%
Real Estate	\$3.5	0.2%
Total Assets	\$2,301.0	100.0%

Note: Residual cash held by investment managers is included in the total for each asset class. This allocation data does not include operating accruals reflected in Tables 2 and 5.

Table 4
Contribution Analysis for Year Ended June 30
(\$ amounts in millions)

<i>(Dollars in millions)</i>	2013	2014	2015	2016	2017	2018
Estimated Covered Payroll	\$222.6 ⁽¹⁾	\$231.2 ⁽¹⁾	\$231.2 ⁽¹⁾	245.94 ⁽¹⁾	252.6 ⁽¹⁾	263.7 ⁽¹⁾
Total Employer Contribution	\$48.0	\$53.7	\$58.2	\$54.5	\$51.8	\$54.9
Total Employee Contribution	\$11.4	\$11.9	\$12.2	\$12.3	\$12.7	\$12.9
Employer/Employee Contribution	4.2	4.5	4.8	4.4	4.1	4.2
Unfunded Actuarial Liability	\$151.2	\$106.1	\$20.2	\$9.1	(\$58.0)	(\$96.4)

⁽¹⁾ Under new payroll definition which excludes overtime

Table 5
Participant Data and Ratios for Year Ended June 30

	2013	2014	2015	2016	2017	2018
Participant Data						
Active Employees	3,550	3,554	3,533	3,566	3,576	3,531
Deferred Vested Members	358	500	548	559	584	631
Retirees	3,833	3,882	3,945	3,909	4,004	4,085
Retirees as a % of Active Employees	108.0%	109.2%	111.7%	109.6%	112.0%	115.7%
Retirement Benefits Paid (millions)	\$81.4	\$85.3	\$88.9	\$94.0	\$98.7	\$104.2
Average Benefit Payment (\$/month)						
Chapter 21	\$2,671	\$2,756	\$2,831	\$2,898	\$2,967	\$3,049
Chapter 35 (Supplement)	\$793	\$813	\$832	\$846	\$854	\$869
Chapter 46 ⁽¹⁾	\$1,659	\$1,741	\$1,842	\$1,952	\$2,033	\$2,132
Investment Data						
Net Assets, Market Value (millions)	\$1,696.8	\$1,979.6	\$1,995.0	\$1,963.5	\$2,173.8	\$2,303.1
Ratio: Net Assets/ Benefits Paid	20.8	23.2	22.4	20.9	22.0	22.1

(1)The averages for Chapter 46 retirees is impacted by several factors: This Chapter is relatively new; disability retirees significantly affect the average and there is blending of VRS and non-VRS members' benefits.

About the Arlington County Retirement System

Benefit Provisions

The System provides normal and early service retirement benefits for members who attain age and service requirements as specified in the County Code. Coverage for service-connected disability benefits is immediate upon membership in the System. Ordinary, non-service related disability benefits are provided after the attainment of two years of service. Members are vested in the System after five years of service and are then eligible for benefits at their normal retirement date.

Arlington's Human Resources department provides an annual benefit statement to each member. Throughout the year, they provide counseling to all benefit applicants and to others requesting counseling and makes presentations at new employee orientations and at various employee group meetings and training sessions. All retirement handbooks and forms are available in the Human Resources office and on the web site at www.careers.arlingtonva.us/retirement-investment-office.

History

The System was established as a defined benefit plan under authority of an act of the General Assembly of Virginia in Chapter 21 of the Code of the County (for Uniform and General Employees) as of December 21, 1953 and in Chapter 35 (for School Board Employees) as of January 1, 1969. System provisions were modified and all County employees hired on or after February 8, 1981 are covered by the provisions of Chapter 46 of the Code of the County. While different County employees have different benefits depending on their date of hire or type of employment, the System utilizes a single Fund for all participants and there is no segregation of assets for individual classes of employees. A formal Trust was adopted for the System as of December, 2001 and all assets are now held under the Trust.

On November 16, 2004, amendments to Arlington County Code Chapters 21, 35, and 46 were made to transfer the administrative responsibilities of these Chapters to the County Manager with investment management responsibility remaining with the Retirement Board.

Arlington County Employees' Retirement System Board of Trustees

(as of December 2018)

	<u>Trustees</u>	<u>Term Expires</u>
Jonathan Kinney, President	Appointed by the County Board	1/31/2021
Richard Alt, Vice President	Elected by Retired Employees	1/31/2019
Michelle Cowan, Treasurer	Appointed by the County Manager	1/31/2019
Jimmie Barrett, Secretary	Elected by Uniformed Employees	1/31/2019
Michael-dharma Irwin	Elected by General Employees	1/31/2021
William Ross, Assistant Treasurer	Appointed by the County Board	1/31/2021
Barbara Donnellan	Appointed by the County Board	1/31/2021

Substitute Trustees

Brian Lynch	Elected by Uniformed Employees	1/31/2019
Wayne Rhodes	Elected by Retired Employees	1/31/2019

Investment Staff

Daniel Zito, Executive Director/Chief Investment Officer
Randee Stenroos, Assistant Director/Pension Investment Officer
Katrina Milne, Investment Analyst
Stephen Euell, Accountant and Office Manager

2018 Retirement Board Meetings

Retirement Board meetings, except for the portions held in executive session, are open to the public. Meetings are scheduled for 8:00 a.m. in One Courthouse Plaza on the following dates:

January 5 ⁽¹⁾	April 4	July 11	October 4
February 7	May 2	August 1 (tentative)	November 7
March 7	June 6	September 5	December 5

⁽¹⁾ Trustee Training

NOTICE: The Code of the County requires that a summary of the Annual Report of Arlington County Employees' Retirement System (System) be provided to members of the System each year. In accordance with the Code, this issue of the Newsletter becomes the summary for fiscal year ended June 30, 2018. Complete copies of the audited Comprehensive Annual Financial Report, which was issued in December, can be found on the retirement web site at www.careers.arlingtonva.us/retirement-investment-office and copies are available for inspection in the Retirement Office, at the Central Public Library and at the Government Reference Library.