



Fiscal Policy

NEWS RELEASE

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Press coverage of IFPI's
"Does Equity Investing Pose an Unacceptable Risk for Indiana Pension Funds?"
as published in INDIANA LEGISLATIVE INSIGHT, July 1, 1996

Equities in favor of equities

Institute report suggest such investments not risky business

A new report to be published early this month by the Indiana Fiscal Policy Institute examines the risk of investing in equities for the State's pension funds. The bottom line: any risks incurred in such investments are likely to be far outweighed by the payback, your favorite newsletter has learned.

The report, *Does Equity Investing Pose an Unacceptable Risk for Indiana Pension Funds?*, authored by Institute President Bill Sheldrake, looks at the issues surrounding the 1996 ballot question that would amend the Indiana Constitution to allow State retirement funds to invest in stocks and other equities. The report reviews the history behind the current prohibition (shared by only two other states), reviews the State investment decision structure and oversight, analyzes the composition of investments, assesses risks, and offers projections (historically and prospectively) for the impact of equity investments.

A review of the financial risks of equity investments concludes that "well-managed pension funds should earn at least the market averages for the investment instruments in which they are allowed to invest," and dispels notions of an "Orange County"-like financial debacle hitting Hoosiers. Indiana's record with bond investments, the report suggests, indicates that the State should fare equally well with respect to tracking market averages if portfolios were expanded to include equity investment. The report does warn, however, of the need to avoid a targeted investment policy, or "social investing." This can be taken resolved, the Institute says, by strict adherence to the State's new "prudent investor" standard, and through additional statutory constraints.

So what's at stake? The Institute reports that if the Public Employees' Retirement Fund had been able to invest in equities at the median level of other state pension funds during the past 15 years, such an average commitment would have raised an additional \$933.2 million for PERF. PERF average earnings per year would have been an additional 2.39% (or 239 basis points) on top of the 10.11% per year that PERF has earned over the past 10 years (the most often-used market measure was a 10.07% return for the bond market over the same period). If the more financially troubled Teachers' Retirement Fund had been so enabled during the same period, it would have generated an additional \$584.8 million in fund assets.

If you're into big numbers, the 30-year future value of equity earning power for all of the State pension funds—the real fiscal impact of allowing the pension funds to invest in equities—would be more than \$43.15 billion.

Writes Sheldrake, "The next generation of State taxpayers, workers, and voters will pay an unnecessary \$43.2 billion for the same amount of public services simply by voting 'no' on [the amendment]. In effect, the presence of [the amendment] on the ballot means that Indiana taxpayers can vote themselves a tax cut by exercising their constitutional right."

The Institute's confident conclusion: "the benefits are great and the risks are low for the State to begin investing its pension funds in equities. The current generation of voters and taxpayers can bequeath a tax cut to themselves and to the succeeding generation ... Equity investing for State pension funds does not pose an unacceptable risk but holds out a great opportunity. It is an opportunity that will pay large dividends for the next generation of taxpayers, and it should not be foregone."