2014

WASHINGTON STATE INVESTMENT BOARD

THIRTY-THIRD ANNUAL REPORT OVERVIEW

HIGHLIGHTS FROM THE EXECUTIVE DIRECTOR

The Washington State Investment Board (WSIB) may be one of the best kept secrets in Washington state. It is a relatively small state agency – 84 employees – quietly and efficiently managing billions of dollars to ensure a safe and secure retirement future for almost half-a-million public employees. The WSIB's long-term, diversified investment strategy has made Washington's public pension fund one of the best performing in the nation. Outside our state's borders, and even our country's borders, the WSIB enjoys a reputation as an innovative, forward-thinking, reasoned and respected institutional investor.

This winter the WSIB was the only U.S. institutional investor invited to attend the World Economic Forum in Davos, Switzerland. The forum gave me the opportunity to listen to and exchange ideas with the most well respected financial and political leaders in the world. One of those discussions resulted in launching a joint initiative to address the challenge of recruiting and retaining women in private equity. Although still in the early stage, the effort has already attracted global participation from leading private equity firms and other influential limited partners. This initiative goes hand-in-hand with the WSIB's involvement with the Thirty Percent Coalition, a group of more than 70 members committed to the goal of women holding 30 percent of corporate board seats by the end of 2015. The coalition includes senior business executives, national women's organizations, institutional investors, corporate governance experts and board members working together to drive the pace of change.

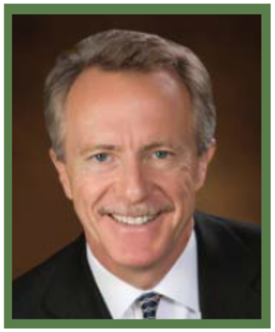
The WSIB also is the only U.S. pension fund serving with financial, corporate and academic leaders from around the world on a project called Focusing Capital on the Long Term. This is a joint initiative by the Canada Pension Plan Investment Board and McKinsey & Company, a management consulting firm, with the goal of coming up with practical recommendations for tackling short-termism in the markets. The WSIB's mission is to maximize investment returns at a prudent level of risk. It is our success in achieving that goal that has resulted in the WSIB increasingly being sought out as a thought leader in international circles. While our investment strategy and performance are among the best in the country, we are not immune to external, social and economic pressures. There is considerable interest among our Board members and beneficiaries in engaging more with companies and our investment partners about the potential financial risks posed by climate change. We need to be responsive to these concerns while remaining focused on our primary responsibility – ensuring the retirement future of the beneficiaries who depend on us.

The money we earn for the retirement funds makes up the lion's share of our assets under management and attracts the most attention, but the WSIB has other equally important investment responsibilities. We also manage Labor and Industries' Funds ($14.5 billion) to help the state meet its financial obligations to injured workers and their employers, the Guaranteed Education Trust (GET) Fund ($2.7 billion) that was created to invest money received from the sale of pre-paid college tuition credits to offset the future cost of a college education and the Developmental Disabilities Endowment Fund ($45.7 million) which was created as a means to support families as they plan for the long-term care needs of individuals with disabilities. Finally, we manage what are called the Permanent Funds ($979 million), the majority of which was established through land grants from the federal government to benefit Washington schools, colleges and universities.

I am extremely proud of the WSIB and its many accomplishments. But in the end, it is the strong and capable Board and the highly professional staff that have earned the WSIB the reputation and success it enjoys.

Sincerely,
Theresa Whitmarsh, Executive Director

LETTER FROM THE CHAIR



To our beneficiaries and participants,

I am pleased to introduce the Washington State Investment Board's (WSIB) fiscal year (FY) ending June 30, 2014 Annual Report. Throughout its 33-year history, the WSIB continues to deliver excellent investment performance and impeccable accountability. The citizens of Washington state should expect and deserve nothing less from an organization entrusted to manage billions of dollars of pension and other public fund assets that serve to benefit thousands of people statewide.

On behalf of all who work for the WSIB or serve on the 15-member, independent Board of Trustees, we fully recognize our fiduciary duty to prudently manage investments for the exclusive benefit of those who devote their lives to serving the public, educating our children, maintaining our schools, fighting fires, enforcing the law, caring for the disabled, protecting the environment, and supporting our colleges and universities. We are proud of their achievements and it's an honor to play a significant role in helping them to build a more financially secure future.

The WSIB ended FY 2014 with $104 billion in total assets under management, the majority of that being the $79.4 billion Commingled Trust Fund (CTF) portfolio for the state's defined benefit retirement systems. The fiscal year-end rate of return for the CTF was 17.06 percent. The three, five, and 10-year return rates for the CTF were 10.07 percent, 12.83 percent, and 8.35 percent respectively. This is one of the best performance records compared to any other public pension fund in the country.

Other notable accomplishments for 2014 include adopting a new investment belief and revision to the WSIB's proxy voting guidelines that call on companies, fund managers, and general partners to disclose anticipated risks related to climate change and what is being done to manage and mitigate those risks. As a long-term investor, the WSIB needs this information to prudently manage the risks, vulnerabilities, and opportunities associated with climate change across all fund portfolios.

Looking ahead to future initiatives, I can assure you that Board members and staff will continue to invest prudently, approach complex market and geo-political challenges with responsible, thoughtful solutions, and pursue new opportunities to bolster and protect all fund investments to the greatest extent possible.

In closing, I want to thank the entire Board and staff for their contributions throughout the year and our beneficiaries and participants for their continued support and trust.

Sincerely,

Treasurer James L. McIntire, Chair

BOARD MEMBERS

The WSIB is an independent Board of Trustees whose fiduciary responsibility is to manage retirement and public fund investments with the highest standard of professional conduct. The Board's primary investment objective is to maximize returns at a prudent level of risk for the exclusive benefit of fund participants and beneficiaries. Individual Board members are recommended by the Chair and appointed by the Board to serve on any of the Board's four different committees to more efficiently analyze investment and governance issues. Committee recommendations are brought to the Board for consideration and a vote.

Administrative Committee

The Administrative Committee has oversight of general policy and organizational issues: personnel, budget, legislative program; legal services; nomination of non-voting Board members, and other issues not included in other committee charters.

Audit Committee

The Audit Committee has oversight of audits of Board activities and operations: compliance, risk management, internal/external audits, financial reporting, and internal controls. It is also responsible for development of policies and procedures for corporate governance and oversight of the Conflict of Interest Policy.

Private Markets Committee

The Private Markets Committee develops strategy, provides oversight, and makes recommendations to the Board for investments in real estate, private equity, tangible assets, and other direct or private transactions.

Treasurer
James L. McIntire
Chair

Marcie Frost
Vice Chair

Joel Sacks

Kelly Fox

Judy Kuschel

George Masten

Stephen Miller

Arlista D. Holman

Representative
Timm Ormsby

Senator
Sharon Nelson

Robert S.
Nakahara, C.P.A.

Jeffrey T. Seely

David
Nierenberg

William A.
Longbrake

Richard
Muhlebach

Public Markets Committee

The Public Markets Committee develops strategy, provides oversight, and makes recommendations to the Board for public markets investments, including the Labor & Industries (L&I) portfolio, fixed income, and equity portfolios.

EXECUTIVE MANAGEMENT

Theresa J. Whitmarsh – Executive Director

Appointed in 2009

The WSIB's executive director is appointed by the Board to oversee the staff, develop and recommend agency and investment policies for Board adoption, and ensure adherence to state policies and laws.

Gary Bruebaker, CFA, CPA – Chief Investment Officer

Appointed in 2001

The Investment Division is comprised of investment professionals who manage investments in major asset classes including public equity, private equity, real estate, fixed income, and tangible assets. The division is also served by a senior investment officer who develops asset allocation and risk budgeting strategies. The division deploys both internal and external investment management strategies.

Victor Moore – Chief Operating Officer/Chief Financial Officer

Appointed in 2010

The Operations Division provides a number of services in support of the investment function, including investment accounting, trade settlement, cash management, private market funding, cash and stock distributions, foreign and domestic tax matters, and investment compliance monitoring. It provides agency-wide risk management, information systems management, human resources, and administrative services.

Liz Mendizabal – Institutional Relations Director

Appointed in 2003

Institutional Relations manages duties typically found in a public affairs and client services division of an investment management agency. These services include performance reporting, annual report preparation, corporate governance, legislative issues, media inquiries, constituent communications, and stakeholder relations.

CONSULTANTS

Investment Accounting Data System
Financial Control Systems

Master Custodian Bank
State Street Bank

Insurance Portfolio Consultant
Conning Asset Management

Private Equity, Real Estate, & Tangibles Consultant
Hamilton Lane Advisors, LLC, Courtland Partners, Ltd.

Consultants and Service Providers
Cerium Networkds Inc.
CliftonLarsonAllen LLP
Duff & Phelps, LLC
EFL Associates of Colorado, Inc.
Glass, Lewis & Co.
Kamakura Corp.
KPM & Associates
LP Capital Advisors
Macias Gini & O'Connell LLP
McLagan
Meketa Investment Group, Inc.
Mercer Investment Consulting, Inc.
MSCI Inc.
Peterson Sullivan LLP
Real Asset Portfolio Mgmt. LLC
Squar, Milner, Peterson, Miranda & Williamson, LLP
TorreyCove Capital Partners
Tunlaw Partners LLC

Real Estate Partners
Aevitas Property Partners
Alere Property Group
Calzada Capital Partners
Cherokee
Emerging Markets Fund of Funds
Evergreen Investment Advisors
Fillmore Capital Partners
Global Co-Investment
Hemisferio Sul
Hometown America
Hudson Advisors
Morgan Stanley
Pacific Realty
Principal Enterprise Capital
Proprium
Warburg Pincus
Washington Holdings

Tangibles Partners
Agriculture Capital Management
Alinda Capital Partners
Campbell Global
Fortress Investment Group
Global Infrastructure Partners
Highstar Capital
Lime Rock Resource
Orion Resource Partners
Sheridan Production Partners
Stonepeak Advisors
UBS AgriVest
Wood Creek Capital Mgmt.

Overlay Manager
State Street Global Advisors

Public Equity Fund Managers
Aberdeen Asset Mgmt. PLC
Arrowstreet Capital, L.P.
BlackRock Institutional Trust Co.
DE Shaw Investment Mgmt.
Grantham, Mayo, Van Otterloo & Co. LLC
JPMorgan Asset Mgmt., Inc.
Lazard Asset Mgmt. LLC
Longview
Magellan Asset Mgmt. Ltd.
Mondrian Investment Partners Ltd
State Street Global Advisors
Wentworth, Hauser & Violich
William Blair & Co.

COMMINGLED TRUST FUND (CTF) PARTNERS & FUND MANAGERS

Private Equity Partners

Accel Partners
Actis
Advent International
Affinity Equity Partners
Alta Communications
Ampersand Ventures
Apax Partners
Apex Investment Partners
Austin Ventures
Avenue Capital Group
Banc Funds
Battery Ventures
BC Partners
Blackstone Group
Boston Ventures
Bridgepoint Capital
Butler Capital Partners
Canaan Partners
Capital Resource Partners
CDH Investments
Charterhouse Capital Partners
Cinven Ltd.
Clayton Dubilier & Rice
Code, Hennessy & Simmons
Collison, Howe and Lennox
Cypress Group
Denham Capital
Doughty Hanson & Co.
Edgewater Funds
EIG Global Energy Partners
El Dorado Ventures
Elevation Partners
Endeavour Capital
Essex Woodlands
Evercore Capital Partners
First Reserve Corp.
Evergreen Pacific Partners
First Reserve Corp.
Fisher Lynch Capital
Flagship Ventures
Fortress Investment Group
FountainVest Partners
Francisco Partners
Frazier & Co.
Friedman Fleischer & Lowe
GGV Capital
GI Partners
Gilbert Global Equity Partners
Great Hill Partners
Green Mountain Partners
Gryphon Investors
GTCR
H.I.G. Ventures
HarbourVest Partners
Healthcare Ventures
Hellman & Friedman
Indigo Capital Partners
Insight Venture Partners
Intersouth Partners
JMI Equity
Kohlberg Kravis Roberts & Co.
KSL Capital Partners
Leonard Green & Partners
M/C Venture Partners
Madison Dearborn Partners
MatlinPatterson Global Advisors
Menlo Ventures
Mobius Venture Capital
Morgan Stanley Venture Partners
New Enterprise Associates
Nordic Capital
Oaktree Capital Mgmt.
Oak Investment Partners
Oaktree Capital Mgmt.
Olympus Partners
OVP Venture Partners
Palamon Capital Partners
Permira
Polaris Venture Partners
Providence Equity Partners
Roark Capital Group
Silver Lake Partners
Southern Cross Group
Spark Mgmt. Partners
Sprout Group
TA Associates
Tailwind Capital Partners
Technology Crossover Ventures
The Riverside Company
Three Arch Partners
TowerBrook Capital Partners
TPG Partners
Trident Capital Partners
Triton Partners
U.S. Venture Partners
Union Square Ventures
Unitas Capital
VantagePoint Venture Partners
Värde Partners
Vestar Capital Partners
Vision Capital
Vivo Ventures
Warburg Pincus
Welsh Carson Anderson & Stowe
Worldview Technology Partners

CORPORATE GOVERNANCE

The WSIB believes a strong, focused corporate governance program is an important part of managing and protecting pension fund assets. Through active support of corporate governance measures and prudent voting of company proxies, the WSIB works to enhance shareowner value and support our long-term investment objectives.

Good corporate governance is a system of checks and balances that fosters transparency, responsibility, accountability and market integrity. A growing body of research provides empirical support for good governance practices. A number of studies demonstrate that companies with strong corporate governance tend to have lower risk of fraud and higher returns.

For the most part, 2014 was a relatively calm year in the board room. The number of directors who failed to receive majority support continued to decline and shareholders once again overwhelmingly supported executive compensation programs at public companies. The high level of support for corporate pay plans is partially the result of a greater effort by corporate boards and management to engage with shareholders regarding compensation concerns. Companies that engaged successfully managed to greatly improve their voting outcomes compared with the previous year.

For companies that received 70 percent or less shareholder approval of their compensation plans, pay-for-performance and outsized pay to CEOs were the most common reasons for negative votes. Of the 2,211 say-on-pay proposals on the ballot during the first nine months of 2014, the WSIB said "no" to 328 plans.

For the first time, the 2014 proxy voting season saw environmental and social (E&S) policy proposals outpace the number of governance shareholder proposals, with E&S initiatives accounting for 53 percent of all ballot proposals. The top five E&S proposal topics this year were on corporate political activities, climate change, sustainability reporting, human rights issues and board diversity. The average level of support for E&S proposals was 22 percent, up slightly from 2013.

The WSIB believes that in order to maximize investment returns we must maintain vigilant oversight of the way companies in which we invest are managed. As a long-term investor, the WSIB doesn't have the option of selling its shares if it doesn't like the way a company is performing. Therefore, active participation is a necessity.

Between January 1, 2014, and September 30, 2014 the WSIB voted 3,239 proxy ballots. Proxy votes were cast on 29,867 individual proposals dealing primarily with election of directors, ratification of auditor, compensation plans, and shareowner proposals.

Of the total director votes during that time period, the WSIB withheld – or voted against – 2,055 incumbent directors, largely because of lack of board independence or unreasonably generous compensation practices. The WSIB's policy states that "Executive compensation should be linked directly with performance of the business the executive is charged with managing."

In line with that commitment, the WSIB:

- Voted against 26 percent of the compensation plans proposed.
- Voted against 236 compensation committee members for paying excessive compensation.

As one of the country's largest institutional investors, the WSIB believes the proxy voting ballot is one of the most effective ways to influence greater board accountability and transparency.

Framework

A cornerstone of a successful investment strategy is effective risk management. Enterprise Risk Management (ERM) is intended to cover risk management in the broadest possible terms, encompassing all forms of risk management activity across the entire agency. The WSIB's enterprise-wide approach to risk management includes involvement of the Board, executive management, audit, operational, legal, and investment staff. Risks are seen as opportunities for success as well as failure. The risks the WSIB face arise from both managing the assets and managing the organization. While the WSIB tries to anticipate every risk that it faces, unknown and unprecedented events will occur. The ERM program provides a framework to evaluate and manage uncertainty and rare events.

Managing the Assets

Risks arise from the deployment of the assets under management in a fiercely competitive environment. This investment needs to comply with the standards that a prudent investor would use to manage the assets of others, as well as with the laws of the state of Washington and Board investment policies. The WSIB has identified two primary risks for managing assets, fiduciary and investment risk.

- Fiduciary Risk – This is the risk of acting and making decisions for reasons other than the benefit of constituents. The WSIB is a fiduciary whose mission is to manage investments for retirement and public trust funds "with the highest standard of professional conduct for the exclusive benefit of fund beneficiaries." To manage this risk, the WSIB has an independent Board, retains the services of legal fiduciary counsel, and complies with state ethics laws. Our code of conduct and conflict of interest procedures, established for both the Board and staff, ensures that our values and expectations are understood and integrated throughout the Board and agency at all times. The Board has established investment policies and procedures designed exclusively to maximize return at a prudent level of risk.
- Investment Risk – Investment risks encompass all potential risks resulting from deployment of assets into various investment strategies. Investment risks include volatility risk, interest rate risk, security pricing risk, liquidity risk, and currency risk, and may stem from changes in political, economic, demographic, and technological factors. The WSIB seeks to manage the overall level of investment risk and uncertainty by broadly diversifying across asset classes, investment managers, sectors, strategies, and geographies. The WSIB seeks to evaluate these risks both in normal and worst case scenario environments. Investment risk can also result from not responding as markets change or failing to recognize the emergence of new markets. It can also result from deviating from long-term investment strategy during short term market downturns. By managing the agency's strategic and operational risks, and also by fostering a strong ERM program that enables proactive decision making, the WSIB aims to make informed choices about the investment risk it faces.

Managing the Organization

These risks stem from building and maintaining an organization that is best suited to managing this investment effort. Our organization must operate within a governmental framework while implementing investment management strategies that are more closely aligned with private investment entities. WSIB has identified three risks under this theme, strategic risk, governmental environment risk, and operational risk.

- Strategic Risk – This is the risk of not being prepared to make the decisions necessary for meeting the needs of constituents. To manage this risk, we strive to have effective Board governance, the appropriate organizational structure for our mission, capable leadership, and an established strategic planning process. Our organizational structure includes an internal audit department, an enterprise-wide risk management team, and a business coordination group.
- Governmental Environment Risk – This is the risk of not continuously understanding, anticipating, and responding to changes in our environment. The WSIB is a state agency operating under a government framework within a political environment that is not always aligned with the practices and priorities of investment entities. To help manage this, the executive director and our institutional relations director work to monitor actual or proposed legislative changes that may affect our ability to accomplish our mission.
- Operational Risk – Operational risk refers to losses that could arise from shortcomings or failures in internal processes, people, or systems, or from failures of external processes, people, or systems that the WSIB depends on. We manage this risk through continuous improvements of our control structure; training, supervision and development of our staff; and the commitment of executive management to mitigate key operational risks identified by the ERM team. To foster organizational growth and change, management has committed to creating an environment where staff continues to learn and to institute state of the art practices.

Safeguarding Our Reputation

- Reputation Risk – The WSIB must maintain its reputation in order to be a sought after partner in the market place, a trusted fiduciary by stakeholders and the legislature, and a valued resource for the citizens of the state of Washington. Failure in any of these prior five risk categories will damage the WSIB's reputation and its credibility, and make it difficult, if not impossible, to achieve the goals of its constituents. The agency has dedicated resources focused on coordinating and monitoring communication for the agency. The Board has also adopted rigorous codes of conduct and conflict of interest policies to ensure that its actions meet the most stringent standards and review. Ongoing education and information assist the Board members in making informed decisions. This enables the WSIB to promote and protect our reputation.

CTF INVESTMENT SUMMARY OF THE LAST YEAR

Strategic Asset Allocation

Strategic asset allocation is the process of selecting a mix of asset classes, such as stocks and bonds, and determining their proportions within an investment portfolio. Asset allocation decisions account for nearly 92 percent of the variation between returns on different portfolios and are often considered to be the most important driver of investment performance. Portfolio assets are diversified to help offset declines in any one class, smooth out marketplace ups and downs, and reduce overall investment risk.

The WSIB invests in seven broad-based asset classes: public equity, fixed income, private equity, real estate, tangible assets, treasury inflation protected securities, and cash. A strategic allocation is established for each fund managed by the Board which includes the asset classes used by that fund, long-term policy targets for those asset classes, and the acceptable ranges within which those targets can vary. The WSIB formally reviews the strategic asset allocations at least every four years.

Highlights

- The Board completed an asset allocation study for the CTF in 2013. As a result of the study, the allocation to real estate was increased from 13 percent to 15 percent and the allocation to private equity was decreased from 25 percent to 23 percent.
- The Board also completed a review of the asset allocation for the Labor & Industries' (L&I) funds in 2013. The L&I funds' allocations to Treasury Inflation Protection Securities were eliminated and each funds' allocation to fixed income was increased accordingly. Additionally, the sector allocation to credit bonds within the overall fixed income allocation was increased.

Retirement Funds

To more efficiently manage investments, reduce administrative costs, and minimize investment fees, the defined benefit retirement fund assets are pooled into the CTF. Over the past 10 years, the fund has grown from $47.5 billion to $79.4 billion including employer and employee contributions, plus net investment returns, less benefit payments and fund transfers (this does not include Plan 3 self-directed defined contribution funds). This year, the market value stated in the audited financials for the retirement funds is significantly different than the market value that is reported through the custodian bank for the same time period. Historically, there has always been a disrepancy, it just happens to be larger this year. This is due to updated year end alternative asset valuations that are received after the unit price for the CTF is published. The retirement funds' audited financials are issued approximately 3 months after that price is established. Accordingly, the values in the audited financials can vary from the prices used to value the CTF as both have different pricing policies.

The WSIB measures fund performance by comparing the performance of investment returns of each asset class in the CTF to appropriate benchmarks. Although quarterly and yearly returns change, long-term realizations should meet or exceed the 7.9 percent actuarially assumed rate of return.

It is important to remember that individual asset classes differ in their behavior and volatility from one year to the next. The fair value of most public market investments can be determined and priced instantly. However, real estate and private equity investments are very illiquid and not easily priced, so it may take years before expected returns are apparent and realized.

Fixed Income

The fixed income program for the CTF is actively managed by WSIB staff against a performance benchmark of the Barclays Universal Index. The main sectors in the portfolio are U.S. governments, credit, and structured.

During fiscal year 2014, $3.0 billion in cash was moved into the portfolio. At the beginning and end of the fiscal year the yield on the 10-year treasury barely changed, starting at 2.48 percent and ending at 2.52 percent. It reached a high of 3.01 percent on the last day of December 2013 and a low of 2.44 percent in end of May 2014.

Highlights

- The portfolio outperformed the Barclays Universal Index for the year, returning 5.96 percent versus 5.20 percent for the Universal Index.
- Within the portfolio, credit and U.S. government bonds were overweighted, while structured bonds were underweighted.
- Transactions totaled $6.2 billion in purchases and $0.9 billion in sales.

Tangible Assets

The tangible asset portfolio invests in non-financial assets having physical substance that are used in the production or supply of goods and services. The portfolio focuses on upstream and midstream segments in four main industries: minerals and mining, energy, agriculture, and society essentials. Each has a different return attribute which provides diversification benefits to the overall CTF portfolio.

The externally-managed partnerships are expected to generate returns, on whole, higher than fixed income but lower than equities. It is anticipated that the assets will have a large portion of the return attributed to annual distributions of income generated by the assets with the remainder due to capital appreciation commensurate with inflation.

Tangible assets were established as a separate asset class in 2007 and implemented in 2008. Over time, we expect to create a well-diversified, global tangible asset portfolio with a variety of partners spread among the target sectors noted above, each with their own level of investment risks, style, and geographic diversification.

Highlights

- This asset class is still relatively new and is in a ramp-up phase.
- The Board approved investments in eight funds totaling $1.2 billion during FY 2014.
- $368 million of committed capital was drawn during the fiscal year.
- $179 million in distributions were returned to the WSIB.

Real Estate

The WSIB's real estate program focuses primarily on creating high-quality, long-term, stable income streams for the CTF. Our partnership investments target risk-adjusted returns consistent with our long-term expectations for the asset class. The majority of these externally-managed partnerships invest in properties leased to third-parties. The steady income from lease payments, combined with potential appreciation, generate returns that are expected to fall between performance for fixed income and equities over the long-term.

Many of the WSIB's real estate partnerships do not involve co-investment with other financial investors. This provides us with superior governance provisions related to acquisition, disposition, and annual business planning processes. The majority of our partners own real estate assets as private market investments and, as a result, better reflect the actual attributes of real estate investing rather than the potential volatility of public markets. Capital is widely diversified among a variety of partners, each with their own investment style, and real estate assets are geographically diversified, including outside the U.S. Investments are made in a variety of property types to provide further diversification. Finally, diversification is enhanced by our partners investing at different points in the real estate capital structure and at different times in the property life cycle. These varying kinds of diversification provide a degree of stability within a cyclical investment class.

The portfolio continues to produce attractive income yields—the primary goal of the program. The importance of having a long-term investment horizon is evident in the attractive returns for the real estate portfolio over a 10-year period.

Highlights

- Over the past year, positive returns were driven by several factors, including appreciation due to strong investor demand and completion of a number of properties previously under development. Investments in the U.K. and U.S were the strongest contributors.
- The 10-year return for the WSIB's real estate portfolio was 9.78 percent versus the WSIB's return benchmark for real estate of 8.00 percent over a rolling 10-year period. The portfolio's 10-year return also exceeded the 8.65 percent 10-year return of the NCREIF Index (lagged a quarter).
- The strongest drivers of the good long-term returns were the WSIB's investments in real estate operating companies (REOCs), diversification by market and property type, and an emphasis on high-quality micro-locations in major markets.

Public Equity

The public equity program uses a global benchmark, the Morgan Stanley All Country World with USA Gross Investable Market Index, reflecting the globalization of capital markets. In a world where American companies like Coca-Cola get most of their revenue from overseas and many foreign companies serve mainly the U.S., distinctions between "U.S. stocks" and "international stocks" have become increasingly blurred. The WSIB believes the future success of the program depends on investment managers finding the most attractive opportunities wherever they are in the world.

Because U.S. equity markets are generally efficient and international equity markets are increasingly efficient, most of the WSIB's public equity investments are in low-cost, broad-based passive index funds. We employ both passive U.S. equity and passive international equity in order to maintain policy weights in both areas. Global equity mandates, in which investment firms can pick the most attractive stocks wherever they are in the world (U.S. or international), and emerging markets equity mandates are primarily actively managed.

For the second consecutive year, in FY 2014, equity markets delivered extremely strong positive returns, with the global equity market rising 23.71 percent after a 17.45 percent rise the previous fiscal year. Meanwhile, the U.S. equity market rose 25.23 percent after a 21.38 percent rise last year. Emerging markets continued to lag developed markets, but still posted a 14.31 percent rise for the fiscal year. Despite numerous macro-political and economic challenges in many parts of the world and despite somewhat sluggish growth in most developed nations, the consensus in equity markets is that positive growth will continue. While this is good news, it has put most equity markets at record highs and vulnerable to disappointing news should positive economic growth falter or interest rates rise faster than anticipated.

The public equity program aims to protect during downward equity market moves. Vice versa, during strong equity markets, the program aims to deliver strong absolute returns but may lag the market benchmarks somewhat. This fiscal year, the program performed exceptionally well, delivering returns modestly better than the already very strong benchmark returns, and with most parts of the program outperforming. Overall, the CTF's program performed 49 basis points better than its benchmark return, returning 24.20 percent versus the benchmark return of 23.71 percent.

Highlights

- The U.S. equity program outperformed its benchmark by 3 basis points (bps) with a return of 25.23 percent versus the benchmark's 25.20 percent return.
- The developed international equity program returned 100 bps more than its benchmark with the portfolio returning 25.52 percent while the benchmark rose 24.52 percent.
- The global equity program performed 220 bps better than the benchmark, returning 25.91 percent versus the benchmark return of 23.71 percent.
- The emerging markets equity program underperformed its benchmark by 171 bps, returning 12.60 percent versus the benchmark return of 14.31 percent.
- The public equity portfolio within the CTF is conservatively structured. The aim is to adopt strategies that protect capital when markets decline, but remain close to market returns when there is a strong market upswing. Despite this conservative structure, the overall program and most components outperformed this past fiscal year.

Private Equity

As of June 30, 2014, the private equity portfolio was valued at $18.3 billion, or 23.11 percent of the CTF, compared with $16.1 billion and 23.63 percent at the previous fiscal year-end. The $2.2 billion increase in the value of the portfolio was achieved despite the fact that distributions received by the WSIB from fund investments exceeded capital drawn for investments by nearly $1.8 billion during the fiscal year. In other words, the portfolio's investments appreciated in value by nearly $4.0 billion during the year.

During the fiscal year, the WSIB closed on $2.5 billion of new commitments across 11 private equity funds. In addition to eight "re-up" commitments with existing partners, the program added three new general partner relationships during the year to address portfolio needs. Capital drawn for investment was approximately $1.0 billion higher than in the previous year, reflecting attractive debt markets and a strong pipeline of investment opportunities. Distribution activity from portfolio company liquidations was up by $0.8 billion from the prior year, reflecting a continuing robust environment for achieving liquidity at attractive valuations.

The objective of the private equity program continues to be to generate a significant premium above the returns of the public equity markets over the long term, by investing in a well-diversified portfolio of funds managed by a stable of high-quality general partners.

Highlights

- $2.5 billion in new commitments to funds were closed during FY 2014 compared to $2.6 billion in FY 2013.
- $3.1 billion of capital was drawn for investment during the fiscal year compared to $2.1 billion in the prior year.
- $4.9 billion in distributions were returned to the CTF in FY 2014 compared with $4.1 billion in FY 2013.

Innovation Portfolio

The primary investment strategy of the innovation portfolio gives staff the ability to make investments that fall outside the established asset class programs currently used by the Board. Secondly, this portfolio provides the Board with comfort and demonstrated success before committing larger dollar amounts to different investment strategies.

Highlights

- No new investment strategies were added to or removed from the innovation portfolio during the fiscal year.

OTHER PLANS UNDER MANAGEMENT

Defined Contribution Retirement Plans

The WSIB oversees the investment options in Plan 3 (Teachers' Retirement System/School Employees' Retirement System/Public Employees' Retirement System), the Deferred Compensation Program (DCP), and the Judicial Retirement Account (JRA). However, these programs are accounted for and reported on by the Department of Retirement Systems (DRS). Therefore, performance information and the financial statements are provided by DRS.

PERS 3: $2.3 Billion

SERS 3: $1.6 Billion

TRS 3: $6.9 Billion

Deferred Compensation Program: $3.6 Billion

Judicial Retirement Account: $13.0 Million

Daily-Valued Funds for Self-Directed Investment Programs

Bond Market Fund $1.5 Billion

The goal of this daily-valued fund is to provide participants of the self-directed defined contribution retirement plans (TRS/SERS/PERS Plan 3s, DCP, and JRA) attractive returns while controlling risk by investing in high-quality corporate bonds. The fund is internally managed by the WSIB and is intended for those who want an intermediate-term investment designed to match or moderately exceed the returns of the Lehman Intermediate Credit Index.

Savings Pool $942 Million

The savings pool is intended as a conservative, short-term investment opportunity where the primary objective is to protect current income and preserve principal. The savings pool is a diversified portfolio of guaranteed investment contracts (GICs) and short-term cash funds.

Labor and Industries' Funds

$14.5 Billion

The WSIB manages Industrial Insurance funds on behalf of the Department of Labor and Industries (L&I). The L&I portfolio consists of four separate funds:

- The Accident Fund primarily pays disability benefits.
- The Medical Aid Fund pays for services required by injured workers and L&I administrative costs.
- The Pension Reserve Fund is maintained by transfers of money from the Accident Fund at the time that a new pensioner is setup.
- The Supplemental Pension Fund supplements time loss and compensates for cost-of-living increases.

Permanent Funds

$979 Million

The permanent funds are non-expendable trusts. The principal for each fund remains intact and investment earnings, less expenses, are reinvested or distributed to a beneficiary fund. Five of these funds were established through federal government land grants to help Washington's schools and colleges with bond repayment, capital development, and facilities maintenance. The Department of Natural Resources transfers proceeds from the sale of land and timber to the WSIB for investment purposes. Fund proceeds are invested in fixed income, short-term holdings, and U.S. equity depending on each funds' policy regulations.

Guaranteed Education Tuition Fund

$2.7 Billion

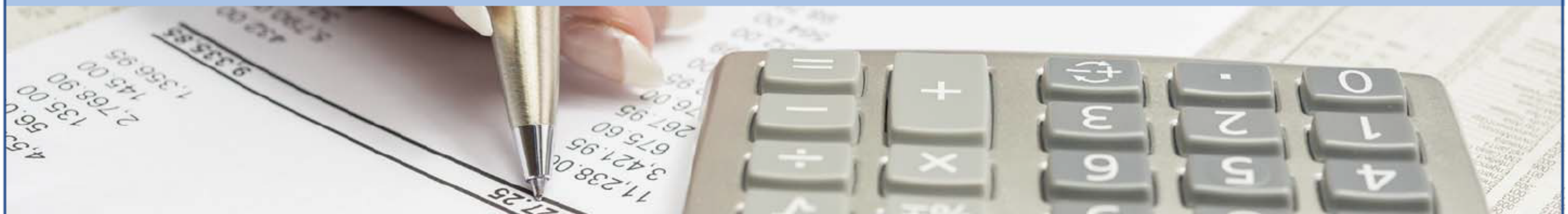
The Guaranteed Education Tuition (GET) program allows individuals or groups to purchase state college and university tuition units for future use at current prices. Program administration is under the authority of the Advanced Tuition Payment Program Committee. The WSIB serves as trustee for the funds and invests them in a mix of short-term holdings, TIPS, U.S. Equity, and International Equity.

Developmental Disabilities Endowment Trust Fund

$45.7 Million

The Developmental Disabilities Endowment Trust Fund (DDEF) supports individuals with developmental disabilities through private contributions and public appropriations. The WSIB invests the fund in a mix of short-term holdings, TIPS, fixed income, and U.S. equity.

ANNUAL BUDGET



June 30, 2014

OBJECTS OF EXPENDITURE APPROPRIATED	Budget	Expenditures	Budget Variance
Salaries	$ 10,051,654	$ 9,233,414	$ 818,240
Benefits	2,439,250	2,305,152	134,098
Personal Service Contracts	529,300	132,571	396,729
Goods & Services	3,016,656	2,862,408	154,248
Travel	997,171	587,614	409,557
Equipment	131,405	23,049	108,356
Treasury Note	157,595	157,595	-
Subtotal Appropriated	$ 17,323,031	$ 15,301,803	$ 2,021,228

NON-APPROPRIATED	Budget	Expenditures	Budget Variance
Public Equity	$ 49,900,000	$ 50,700,270	$ (800,270)
Private Equity	214,648,000	199,034,558	15,613,442
Real Estate	47,246,000	33,310,955	13,935,045
Tangible Assets	10,899,000	15,072,208	(4,173,208)
Innovation Portfolio	3,769,000	1,130,595	2,638,405
General Consultants	1,015,000	553,980	461,020
Staff Consultants	895,000	592,555	302,445
Advisory Services Consultants	500,000	-	500,000
Legal Fees	930,000	1,342,193	(412,193)
Custodian Bank Fees	500,000	49,017	450,983
Securities Lending	7,111,437	6,770,656	340,781
Cash Management	4,092,578	3,652,263	440,315
Cash Overlay	500,000	474,167	25,833
Investment Accounting Data System	1,546,100	1,531,238	14,862
Memberships	77,350	59,140	18,210
Research Services	2,424,000	2,524,879	(100,879)
Subtotal Non Appropriated	346,053,465	316,798,674	29,254,791
TOTAL	$ 363,376,496	$ 332,100,477	$ 31,276,019

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