The investment cycle, explained

Have you ever been stuck with an unflattering school portrait? Still photographs sometimes freeze in time a pretty bad look.

We can relate. This is similar to what happened with pension system investments for fiscal year 2016.

TRA has received inquiries from members wondering how it is that our fiscal 2016 investment returns were so poor at a time when the stock market has been setting records. There is a common misunderstanding about our low return (-0.1 percent) last fiscal year. It is important to point out that that reported return was for the fiscal year ending June 30, 2016, not the calendar year ending Dec. 31, 2016.

Fiscal year returns were depressed by the Brexit vote, which happened just a few days before the end of June and caused the Dow to plummet 900 points in just two days – taking a chunk of our portfolio with it. Since then, markets have improved, and our investment return for the calendar year ending Dec. 31, 2016, was 7.6 percent.

In order to dampen volatility, the State Board of Investment maintains a diversified portfolio – assets are not invested totally in stocks. For diversification, a large portion of the portfolio (25 percent) is in bonds and another 13 percent is in alternative assets such as private equity and real estate.

The stock market has its ups and downs, and there is always the possibility that the market will be in a downswing when our fiscal year ends, locking in a poor number that must be reflected in our financial reports. But pension systems are very long-term investors, and it's important to take the long view. In fact, SBI has averaged annual compound returns of 8.6 percent over 25 years and 8.7 percent over 30 years, outperforming its private and public pension fund peers nationally.

We're hoping for a much better look on "picture retake day" this coming June 30.