



**STATE OF ALASKA  
DEPARTMENT OF REVENUE  
TREASURY DIVISION**

**Public Employees' Retirement System**

**Invested Assets**

**Schedules**

**June 30, 2004 and 2003**

**(With Independent Auditors' Report Thereon)**

**STATE OF ALASKA  
DEPARTMENT OF REVENUE  
TREASURY DIVISION**

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**June 30, 2004 and 2003**

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## **Independent Auditors' Report**

Alaska State Pension Investment Board and  
State of Alaska, Department of Revenue  
Division of Treasury:

We have audited the accompanying schedules of invested assets of the Public Employees' Retirement System as of June 30, 2004 and 2003 and of investment income (loss) and changes in invested assets of the Public Employees' Retirement System for the years then ended (schedules). These schedules are the responsibility of the Division of Treasury's management. Our responsibility is to express an opinion on these schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall schedule presentation. We believe that our audits provide a reasonable basis for our opinion.

The accompanying schedules were prepared to present the invested assets of the Public Employees' Retirement System, which is established under the State of Alaska Public Employees Retirement System (PERS). The schedules are not intended to present the financial status of PERS.

In our opinion, the schedules referred to above present fairly, in all material respects, the invested assets of the Public Employees' Retirement System as of June 30, 2004 and 2003, and the investment income (loss) and changes in invested assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

**KPMG LLP**

September 10, 2004

**STATE OF ALASKA  
DEPARTMENT OF REVENUE  
TREASURY DIVISION  
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

**SCHEDULES OF INVESTED ASSETS**

**June 30, 2004 and 2003**

	<u>2004</u>	<u>2003</u>
<b>Investments (at Fair Value)</b> (Notes 4, 8)		
<b>Cash and Cash Equivalents</b> (Note 3)		
Short-term Fixed Income Pool	\$ <u>510,556</u>	\$ <u>523,685</u>
<b>Marketable Debt Securities</b> (Note 3)		
Retirement Fixed Income Pool	1,459,056,670	1,402,391,645
External Domestic Fixed Income Pool	750,293,368	775,378,644
International Fixed Income Pool	<u>297,481,250</u>	<u>275,270,800</u>
Total Marketable Debt Securities	<u>2,506,831,288</u>	<u>2,453,041,089</u>
<b>Equity Securities</b> (Note 3)		
Domestic Equity Pool	3,298,973,034	2,974,228,762
International Equity Pool	1,364,094,145	1,153,385,203
Emerging Markets Equity Pool	99,177,084	74,527,573
Private Equity Pool	269,232,951	216,125,487
Other Investments Pool	<u>8,160,418</u>	<u>-</u>
Total Equity Securities	<u>5,039,637,632</u>	<u>4,418,267,025</u>
<b>Real Estate Investments</b>		
Real Estate Pool (Note 3)	628,393,630	517,432,671
Mortgages (Note 2)	<u>118,650</u>	<u>141,537</u>
Total Real Estate Investments	<u>628,512,280</u>	<u>517,574,208</u>
<b>Total Invested Assets</b>	<u>\$ 8,175,491,756</u>	<u>\$ 7,389,406,007</u>

See accompanying notes to schedules

**STATE OF ALASKA  
DEPARTMENT OF REVENUE  
TREASURY DIVISION  
PUBLIC EMPLOYEES' RETIREMENT SYSTEM**

**SCHEDULES OF INVESTMENT INCOME (LOSS)  
AND CHANGES IN INVESTED ASSETS**

**Years ended June 30, 2004 and 2003**

	<u>2004</u>	<u>2003</u>
<b>Investment Income (Loss)</b> (Note 5)		
Short-term Fixed Income Pool	\$ 33,195	\$ 58,923
Retirement Fixed Income Pool	10,162,114	149,325,681
External Domestic Fixed Income Pool	5,818,767	77,393,675
International Fixed Income Pool	20,743,633	58,323,742
Domestic Equity Pool	573,087,888	16,289,983
International Equity Pool	353,320,814	(70,057,223)
Emerging Markets Equity Pool	24,963,546	4,510,195
Private Equity Pool	47,088,265	(32,692,525)
Other Investments Pool	38,756	-
Real Estate Pool	48,438,019	50,245,968
Mortgages	<u>12,976</u>	<u>87,789</u>
<b>Total Investment Income</b>	1,083,707,973	253,486,208
<b>Total Invested Assets, Beginning of Year</b>	7,389,406,007	7,410,166,481
<b>Net Withdrawals</b>	<u>(297,622,224)</u>	<u>(274,246,682)</u>
<b>Total Invested Assets, End of Year</b>	<u>\$ 8,175,491,756</u>	<u>\$ 7,389,406,007</u>

See accompanying notes to schedules

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (1) THE ACCOUNTING ENTITY

The Public Employees' Retirement System Invested Assets (PERS Invested Assets) is the investment portfolio of the State of Alaska Public Employees' Retirement System (PERS). PERS is a multiple employer, joint contributory, agent-defined benefit system established for the payment of retirement, disability and death benefits to, or on behalf of, qualified employees of the State of Alaska (State) or a political subdivision within the State. These schedules are those of PERS Invested Assets and not PERS taken as a whole. Fiduciary responsibility for PERS Invested Assets resides with the Alaska State Pension Investment Board (Board), pursuant to Alaska Statutes 37.10.210-390.

Alaska Statutes 39.35.080 and 37.10.071 provide that investments shall be made with the judgment and care under circumstances then prevailing that an institutional investor of ordinary professional prudence, discretion and intelligence exercises in managing large investment portfolios.

The Department of Revenue, Treasury Division (Treasury) provides staff for the Board. Treasury has created a pooled environment by which it manages the investments the Board has fiduciary responsibility for. Actual investing is performed by investment officers in Treasury or by contracted external investment managers. The Board has developed investment guidelines, policies and procedures for Treasury staff and external investment managers to adhere to when managing investments. Specifically, the External Domestic Fixed Income Pool, International Fixed Income Pool, Domestic Equity Pool, International Equity Pool, Emerging Markets Equity Pool, Private Equity Pool, Other Investments Pool and the Real Estate Pool are managed by external management companies. Treasury manages the Alaska Retirement Fixed Income Pool and cash holdings of certain external domestic equity managers in addition to acting as oversight manager for all externally managed investments.

The Short-term Fixed Income Pool is a State pool managed by Treasury.

### (2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### **Basis of Accounting**

The schedules are prepared using the accrual basis of accounting for investment income. Assets are reported at fair value in accordance with Governmental Accounting Standards Board (GASB) Statement No. 31. Net withdrawals represent contributions from employers and employees, net of benefits paid to PERS participants as well as administrative and investment management expenses. Contributions, benefits paid and all expenses are recorded on a cash basis.

In fiscal year 2004, Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposits and Investment Risk Disclosures* was implemented. GASB Statement No. 40 addresses disclosures on deposits and investments, focusing on common investment risks related to interest rate risk, credit risk, custodial credit risk, foreign currency risk and concentration of credit risk.

#### **Valuation**

Fixed income securities are valued each business day using prices obtained from a pricing service when such prices are available; otherwise, such securities are valued at the mid-point between the bid and asked price or at prices for securities of comparable maturity, quality and type.

Domestic and international equity securities are valued each business day using prices obtained from a pricing service or prices quoted by one or more independent brokers. Equity securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates or, in the absence of a sale, at the last reported bid price.

Emerging markets securities are valued on the last business day of each month by the investment managers.

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules

#### June 30, 2004 and 2003

#### (2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

##### Valuation (Cont.)

Private equity securities are valued quarterly by the general partners and investment sponsors. The private equity oversight manager is held to a standard of reasonable care in verifying that the valuations reasonably reflect the underlying fair value of the investments.

Securities expressed in terms of foreign currencies are translated into U.S. dollars at the prevailing exchange rates. Forward currency contracts are valued at the mid-point of representative quoted bid and asked prices.

The other investment security is valued quarterly by the general partner.

Real estate investments are valued quarterly by investment managers based on market conditions and their knowledge of industry trends. Real estate investments are valued once every three years, in conjunction with the purchase date anniversary, by independent appraisers.

Mortgage loans are valued at their principal balance (cost) less an allowance for loan loss, the net result of which approximates fair value. At June 30, 2004 and 2003, the allowance for loan loss totaled \$16,221 and \$16,222, respectively, and is considered by management to be sufficient to cover any losses to the mortgage loan portfolio.

##### Income Allocation

Income, which includes interest and realized and unrealized gains and losses, in the fixed income pools is allocated to pool participants daily on a pro rata basis.

Income, which includes interest, dividends and realized and unrealized gains and losses, in the Domestic and International Equity Pools is allocated to pool participants daily on a pro rata basis.

Income, which includes interest, dividends and realized and unrealized gains and losses, in the Emerging Market Equity Pool, Private Equity Pool and the Other Investments Pool is allocated to pool participants monthly on a pro rata basis.

Income, which includes interest, income from operations and realized and unrealized gains and losses in the Real Estate Investment Pool is allocated to pool participants monthly on a pro rata basis.

#### (3) POOLED INVESTMENTS

##### Short-term Fixed Income Pool

PERS Invested Assets include participation in the State's internally managed Short-term Fixed Income Pool which was established March 15, 1993, with a start up and maintained share price of \$1. Treasury staff determines the allocation between permissible securities. Each participant owns shares in the pool, the number of which fluctuates daily with contributions and withdrawals. Participant shares also change at the beginning of each month when income is paid. At June 30, 2004 and 2003, PERS Invested Assets included a 0.03% direct ownership in the Short-term Fixed Income Pool which included interest receivable of \$5,103 and \$7,582, respectively.

##### Retirement Fixed Income Pool

PERS Invested Assets include participation in the Board's internally managed Retirement Fixed Income Pool which was established March 1, 1996, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,723. Treasury staff determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules June 30, 2004 and 2003

#### (3) POOLED INVESTMENTS (Cont.)

##### Retirement Fixed Income Pool (Cont.)

the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.03% and 66.69% ownership in the Retirement Fixed Income Pool, respectively.

##### External Domestic Fixed Income Pool

PERS Invested Assets include participation in the Board's externally managed Domestic Fixed Income Pool which was established June 25, 1999, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,448. Each manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 66.73% and 66.32% ownership in the External Domestic Fixed Income Pool, respectively.

##### International Fixed Income Pool

PERS Invested Assets include participation in the Board's externally managed International Fixed Income Pool which was established March 3, 1997, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,630. The manager independently determines the allocation between permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.32% and 66.98% ownership in the International Fixed Income Pool, respectively.

##### Domestic Equity Pool

PERS Invested Assets include participation in the Board's externally managed Domestic Equity Pool which was established July 1, 1991, with a start up share price of \$1,000. The share price at June 30, 2004 was \$4,086. Each manager independently determines the allocation between equities and other permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.20% and 66.84% ownership in the Domestic Equity Pool, respectively.

##### International Equity Pool

PERS Invested Assets include participation in the Board's externally managed International Equity Pool which was established January 1, 1992, with a start up share price of \$1,000. The share price at June 30, 2004 was \$2,312. Each manager independently determines the allocation between equities and other permissible securities. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.46% and 67.01% ownership in the International Equity Pool, respectively.



# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules June 30, 2004 and 2003

#### (3) POOLED INVESTMENTS (Cont.)

##### Emerging Markets Equity Pool

PERS Invested Assets include participation in the Board's externally managed Emerging Markets Equity Pool which was established May 2, 1994, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,438. The pool participates in two externally managed commingled investment funds through ownership of equity shares. The commingled funds, comprised of various institutional investors, invest in the securities markets of developing countries. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 65.00% ownership in the Emerging Markets Equity Pool.

##### Private Equity Pool

PERS Invested Assets include participation in the Board's externally managed Private Equity Pool which was established April 24, 1998, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,156. Underlying assets in the pool are composed of venture capital, buyouts and special situation investments through limited partnership agreements. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.68% and 67.32% ownership in the Private Equity Pool, respectively.

##### Other Investments Pool

PERS Invested Assets include participation in the Board's externally managed Other Investments Pool which was established March 18, 2004, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,006. The underlying asset in the pool is composed of a limited partnership interest in a venture capital operating company. The venture capital operating company invests in oil, gas and other hydrocarbon properties, operations or projects as well as electric and other forms of power generation, transmission and distribution and other power-related projects or operations. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004, PERS Invested Assets included a 67.68% ownership in the Other Investments Pool.

##### Real Estate Pool

PERS Invested Assets include participation in the Board's externally managed Real Estate Pool which was established June 27, 1997, with a start up share price of \$1,000. The share price at June 30, 2004 was \$1,807. Ownership in the pool is based on the number of shares held by each participant. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of shares of the pool outstanding on the valuation date. Contributions to and withdrawals from the pool are based on the beginning of the day net asset value per share on the day of the transaction. At June 30, 2004 and 2003, PERS Invested Assets included a 67.54% and 66.88% ownership in the Real Estate Pool, respectively.

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (4) DEPOSIT AND INVESTMENT RISK

At June 30, 2004, PERS Invested Assets included the following (stated in thousands):

	Short-term Fixed Income Pool	Retirement Fixed Income Pool	External Domestic Fixed Income Pool	Internat- ional Fixed Income Pool	Equities and Other	Total
Commercial Paper	\$ 356,409	\$ -	\$ -	\$ -	\$ -	\$ 356,409
U.S. Treasury Notes	132,644	149,846	191,188	-	-	473,678
U.S. Treasury Bonds	-	120,358	55,410	-	-	175,768
U.S. Treasury Strips	-	31,210	5,264	-	-	36,474
U. S. Government Agency Discount Notes	-	-	210,132	-	-	210,132
U. S. Government Agency	39,932	94,097	98,938	-	-	232,967
Foreign Government	-	-	-	327,591	-	327,591
Mortgage-related	154,138	1,081,936	463,823	-	-	1,699,897
Asset-backed	805,164	67,855	37,395	-	-	910,414
Corporate	466,513	525,012	213,034	100,869	-	1,305,428
Yankees	-	18,860	21,038	-	-	39,898
Domestic Equity Pool:						
Convertible Bonds	-	-	-	-	783	783
Equity	-	-	-	-	4,859,726	4,859,726
International Equity Pool:						
Convertible Bonds	-	-	-	-	4,619	4,619
Equity	-	-	-	-	1,986,354	1,986,354
Emerging Markets Equity Pool	-	-	-	-	152,584	152,584
Private Equity Pool:						
Limited Partnerships	-	-	-	-	396,994	396,994
Other Investments Pool:						
Limited Partnership	-	-	-	-	12,057	12,057
Real Estate Pool:						
Real Estate Holdings	-	-	-	-	930,404	930,404
Mortgages	-	-	-	-	179	179
Total Fair Value	1,954,800	2,089,174	1,296,222	428,460	8,343,700	14,112,356
Net Pending Security						
Receivables (Payables)	(14,419)	(75,880)	(187,780)	8,963	12,113	(257,003)
Deposits	14,240	163,323	15,901	4,442	68,534	266,440
Total Net Assets at Fair Value before earnings distribution to participants	1,954,621	2,176,617	1,124,343	441,865	8,424,347	14,121,793
Earnings payable to participants	(1,828)	-	-	-	-	(1,828)
Ownership by the Retirement Fixed Income Pool	(163,323)	-	-	-	-	(163,323)
Ownership by Funds Under Other Fiduciary Responsibility	(1,788,361)	-	-	-	-	(1,788,361)
Ownership by Other Retirement Systems under ASPIB's Fiduciary Responsibility	(598)	(717,560)	(374,050)	(144,384)	(2,756,197)	(3,992,789)
PERS Invested Assets	\$ 511	\$ 1,459,057	\$ 750,293	\$ 297,481	\$ 5,668,150	\$ 8,175,492

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules

#### June 30, 2004 and 2003

#### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

##### Interest Rate Risk

##### **Short-term Fixed Income Pool**

As a means of limiting its exposure to fair value losses arising from increasing interest rates in the Short-term Fixed Income Pool, Treasury's investment policy limits individual fixed rate securities to fourteen months in maturity or fourteen months expected average life. Floating rate securities are limited to three years in maturity or three years expected average life. When evaluating fixed rate securities, Treasury utilizes the actual maturity date for commercial paper and twelve-month prepay speeds for other securities. At June 30, 2004, the expected average life of individual fixed rate securities in the Short-term Fixed Income Pool ranged from one to six months and the expected average life of floating rate securities ranged from less than one year to 2.85 years.

##### **Retirement and External Domestic Fixed Income Pools (domestic fixed income)**

Through the Board's investment policy, Treasury manages the exposure to fair value losses arising from increasing interest rates by limiting the effective duration of the domestic fixed income portfolio to  $\pm 20\%$  of the Lehman Brothers Aggregate Bond Index. The effective duration for the Lehman Brothers Aggregate Bond Index at June 30, 2004, was 4.77 years.

At June 30, 2004, the effective duration of the domestic fixed income portfolio, by investment type, was as follows:

	<u>Effective Duration (in years)</u>
U.S. Treasury Notes	4.11
U.S. Treasury Bonds	8.71
U.S. Treasury Strips	21.14
U.S. Government Agency	5.31
Mortgage-related	4.02
Asset-backed	2.36
Corporate	5.54
Yankees	7.96
Portfolio Effective Duration	4.76

Treasury uses industry-standard analytical software developed by The Yield Book Inc. to calculate effective duration. The software takes into account various possible future interest rates, historical and estimated prepayment rates, call options and other variable cash flows for purposes of the effective duration calculation.

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

#### Interest Rate Risk (Cont.)

#### International Fixed Income Pool

It is the Board's policy that external managers select and retain securities based solely on the managers' independent judgment. The Board does not specifically provide risk limitations to these managers. At June 30, 2004, PERS Invested Assets included the following:

	<u>Currency</u>	<u>Maturity</u>	<u>Fair Value</u> (in thousands)
Corporate:			
European Investment Bank	Japanese Yen	11/8/2004	\$ 3,342
International Bank for Reconstruction and Development	Japanese Yen	12/20/2004	6,304
Kreditanstalt Fuer Wiederaufbau International Finance	Japanese Yen	12/20/2004	7,438
Asian Development Bank	Japanese Yen	6/29/2005	9,538
Export Import Bank	Japanese Yen	7/28/2005	2,543
European Investment Bank	Japanese Yen	9/20/2007	2,215
International American Development Bank	Japanese Yen	7/8/2009	11,692
Osterreichische Kontrollbank	Japanese Yen	3/22/2010	6,435
Kreditanstalt Fuer Wiederaufbau International Finance	Japanese Yen	3/23/2010	16,060
SL Finance PLC	Euro Currency	7/12/2022	1,488
Zurich Finance USA	Euro Currency	10/2/2023	850
Foreign Government:			
Queensland Treasury Corporation	Australian Dollar	6/14/2005	947
Kingdom of Spain	Japanese Yen	9/20/2006	1,970
Kingdom of Netherlands	Euro Currency	2/15/2007	11,378
New South Wales Treasury Corporation	Australian Dollar	3/1/2008	5,031
Federal National Mortgage Association	Japanese Yen	3/26/2008	2,253
Republic of Italy	Japanese Yen	3/27/2008	7,949
Republic of Poland	Polish Zloty	6/24/2008	5,663
Kingdom of Sweden	Swedish Krona	1/28/2009	12,564
Republic of Italy	Euro Currency	5/1/2009	8,494
Federal Republic of Germany	Euro Currency	7/4/2009	7,488
Kingdom of Spain	Euro Currency	7/30/2009	20,566
Republic of France	Euro Currency	10/25/2009	1,826
Government of Poland	Polish Zloty	11/24/2009	3,920
Republic of France	Euro Currency	4/25/2010	10,681
Government of Poland	Polish Zloty	11/24/2010	3,368
Republic of Finland	Euro Currency	2/23/2011	7,661
Government of Australia	Australian Dollar	6/15/2011	4,208
Bundesrepublik Deutschland	Euro Currency	7/4/2011	14,746
Japan Financial Corporation	Japanese Yen	2/21/2012	4,348
Kingdom of Sweden	Swedish Krona	10/8/2012	7,134
Federal Republic of Germany	Euro Currency	1/4/2013	12,947
Commonwealth of Australia	Australian Dollar	5/15/2013	9,298
Queensland Treasury Corporation	Australian Dollar	8/14/2013	9,337
Government of Poland	Polish Zloty	10/24/2013	13,201
Kingdom of Sweden	Swedish Krona	5/5/2014	12,428
Kingdom of Sweden	Swedish Krona	12/1/2020	2,672
Bundesrepublik Deutschland	Euro Currency	7/4/2027	18,456
Total International Fixed Income			\$ 288,439

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules

#### June 30, 2004 and 2003

#### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

##### Credit Risk

Treasury's investment policy has the following limitations with regard to credit risk:

Short-term Fixed Income Pool investments are limited to instruments with a long-term credit rating of at least A3 or equivalent and instruments with a short-term credit rating of at least P1 or equivalent. In addition, Treasury's investment policy limits investments with regard to credit risk for the following investment types:

- Corporate debt must be investment grade and comprise those issued in the U.S. capital market by U.S. companies, Euro-dollar debt, or Yankee debt;
- Asset-backed securities must be investment grade; and
- Mortgage-related securities must be issued or securitized by one of the following U.S. Government Agencies: Government National Mortgage Association; Federal National Mortgage Association; or the Federal Home Loan Mortgage Corporation.

The Board's investment policy has the following limitations with regard to credit risk:

##### Domestic Fixed Income:

- Commercial paper must carry a rating of at least P1 or equivalent;
- Corporate debt securities must be investment grade and comprise those issued in the U.S. capital market by U.S. companies, Euro-dollar debt, or Yankee debt;
- Corporate, asset-backed and non-agency mortgage securities must have a minimum rating of BBB or equivalent. For asset-backed and non-agency mortgage securities that are solely rated by Fitch or Duff & Phelps, they must have a AAA rating.

##### International Fixed Income:

- Commercial paper and euro commercial paper must be rated at least A-1 or equivalent and
- Corporate and asset-backed obligations must be investment grade.

##### Domestic and International Equity:

- Commercial paper must bear the highest rating assigned and
- Corporate debt obligations must carry a rating of at least A or equivalent.

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

#### Credit Risk (Cont.)

At June 30, 2004, PERS Invested Assets consisted of securities with credit quality ratings issued by nationally recognized statistical rating organizations as follows:

	<u>Rating<sup>1</sup></u>	<u>Short-term Fixed Income Pool</u>	<u>Domestic Fixed Income Pools</u>	<u>International Fixed Income Pool</u>	<u>Internat- ional Equity Pool</u>
Short-term Investment					
Account (Deposit)	Not Rated	1%	-	-	-
Government Short-term					
Investment Fund (Deposit)	Not Rated	-	-	1%	1%
Commercial Paper	A	18%	-	-	-
U. S. Government Agency					
Discount Notes	AAA	-	6%	-	-
U. S. Government Agency	AAA	2%	5%	-	-
Foreign Government	AAA	-	-	47%	-
Foreign Government	AA	-	-	15%	-
Foreign Government	A	-	-	8%	-
Foreign Government	Not Rated	-	-	6%	-
Mortgage-related	AAA	7%	32%	-	-
Mortgage-related	Not Rated <sup>2</sup>	-	8%	-	-
Asset-backed	AAA	41%	3%	-	-
Corporate	AAA	2%	3%	22%	-
Corporate	AA	8%	3%	1%	-
Corporate	A	14%	7%	-	-
Corporate	BAA	-	1%	-	-
Corporate	BBB	-	8%	-	-
Investments with no credit exposure		7%	24%	-	99%

<sup>1</sup>Rating modifiers are not disclosed.

<sup>2</sup>TBA's issued by U.S. Government Agencies allowed by policy.

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

#### Custodial Credit Risk – Deposits

Custodial credit risk is the risk that in the event of a bank failure, the deposits may not be returned. The Board does not have a formal policy for custodial credit risk. At June 30, 2004, PERS Invested Assets had the following uncollateralized and uninsured deposits:

	<u>Amount</u> (in thousands)
International Fixed Income Pool	\$ 787
International Equity Pool	2,620
	<u>\$ 3,407</u>

#### Foreign Currency Risk

The Board's policy with regard to foreign currency risk is to restrict obligations to those issued in the currencies of countries represented in the family of Solomon Brothers World Government Bond Indices. The Board's asset allocation policy permits PERS to hold up to five percent of total investments in international fixed income and up to eighteen percent of total investments in international equity. At June 30, 2004, PERS invested assets included 3.64% in international fixed income and 17.90% in international equity.

At June 30, 2004, PERS had exposure to foreign currency risk with the following deposits:

<u>Currency</u>	<u>Amount</u> (in thousands)
Australian Dollar	\$ 193
Canadian Dollar	3
Euro Currency	790
Hong Kong Dollar	1
Japanese Yen	1,065
Polish Zloty	346
Pound Sterling	615
South Korean Won	216
Swiss Franc	176
	<u>\$ 3,405</u>

# Public Employees' Retirement System Invested Assets

## Notes to Schedules June 30, 2004 and 2003

### (4) DEPOSIT AND INVESTMENT RISK (Cont.)

#### Foreign Currency Risk (Cont.)

At June 30, 2004, PERS had exposure to foreign currency risk with the following investments (stated in thousands):

<u>Currency</u>	<u>Foreign Government</u>	<u>Corporate</u>	<u>Convertible Bonds</u>	<u>Equity</u>
Australian Dollar	\$ 28,820	\$ -	\$ -	\$ 11,085
Canadian Dollar	-	-	-	14,975
Danish Krone	-	-	-	1,072
Euro Currency	114,242	2,337	227	499,627
Hong Kong Dollar	-	-	-	17,806
Japanese Yen	16,521	65,568	2,582	249,841
New Zealand Dollar	-	-	-	10,414
Norwegian Krone	-	-	-	7,226
Polish Zloty	26,153	-	-	-
Pound Sterling	-	-	-	288,384
Singapore Dollar	-	-	-	22,264
South Korean Won	-	-	-	17,818
Swedish Krona	34,798	-	-	9,544
Swiss Franc	-	-	308	109,350
	<u>\$ 220,534</u>	<u>\$ 67,905</u>	<u>\$ 3,117</u>	<u>\$ 1,259,406</u>

#### Concentration of Credit Risk

Treasury does not have a policy with regard to concentration of credit risk for the Short-term Fixed Income Pool.

The Board's policy limits with regard to concentration of credit risk are as follows:

##### Domestic Fixed Income:

No more than ten percent of the currently outstanding par value of any corporate bond issue can be purchased.

##### International Fixed Income:

No more than ten percent of an outstanding non-government issue or non-government agency issue may be purchased.

At June 30, 2004, PERS invested assets included \$812,565,790 in Federal National Mortgage Association securities which represented 9.80% of total PERS invested assets.



## Public Employees' Retirement System Invested Assets

### Notes to Schedules June 30, 2004 and 2003

#### (5) INVESTMENT INCOME (LOSS)

For the years ended June 30, investment income (loss) for each investment type includes the following components:

	2004		Total
	Interest and/or dividends	Net increase (decrease) in the fair value of investments	
Short-term Fixed Income Pool	\$ 33,195	\$ -	\$ 33,195
Retirement Fixed Income Pool	75,323,479	-65,161,365	10,162,114
External Domestic Fixed Income Pool	28,266,337	-22,447,570	5,818,767
International Fixed Income Pool	12,907,133	7,836,500 (1)	20,743,633
Domestic Equity Pool	47,171,958	525,915,930	573,087,888
International Equity Pool	32,250,797	321,070,017 (2)	353,320,814
Emerging Markets Equity Pool	1,401,011	23,562,535	24,963,546
Private Equity Pool	7,035,698	40,052,567	47,088,265
Other Investments Pool	-	38,756	38,756
Real Estate Pool	37,641,946	10,796,073	48,438,019
Mortgages	12,976	-	12,976
Total	<u>\$ 242,044,530</u>	<u>\$ 841,663,443</u>	<u>\$ 1,083,707,973</u>

(1) Includes net realized gains of \$16,361,373 and net unrealized gains of \$3,164 on foreign currency.

(2) Includes net realized gains of \$71,442,331 and net unrealized gains of \$16,237 on foreign currency. Also includes net realized gains of \$82,142 on foreign exchange contracts.

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules

#### June 30, 2004 and 2003

#### (5) INVESTMENT INCOME (LOSS) (Cont.)

	<b>2003</b>		
	<b>Interest and/or dividends</b>	<b>Net increase (decrease) in the fair value of investments</b>	<b>Total</b>
Short-term Fixed Income Pool	\$ 58,923	\$ -	\$ 58,923
Retirement Fixed Income Pool	80,954,603	68,371,078	149,325,681
External Domestic Fixed Income Pool	28,673,193	48,720,482	77,393,675
International Fixed Income Pool	13,416,776	44,906,966 (1)	58,323,742
Domestic Equity Pool	43,011,840	(26,721,857)	16,289,983
International Equity Pool	28,626,620	(98,683,843) (2)	(70,057,223)
Emerging Markets Equity Pool	663,681	3,846,514	4,510,195
Private Equity Pool	858,591	(33,551,116)	(32,692,525)
Real Estate Pool	43,317,116	6,928,852	50,245,968
Mortgages	87,789	-	87,789
Total	<u>\$ 239,669,132</u>	<u>\$ 13,817,076</u>	<u>\$ 253,486,208</u>

(1) Includes net realized gains of \$13,380,117 and net unrealized losses of \$17 on foreign currency.

(2) Includes net realized gains of \$16,068,761 and net unrealized losses of \$20,350 on foreign currency. Also includes net realized losses of \$1,083,455 on foreign exchange contracts.

#### (6) FOREIGN EXCHANGE CONTRACTS AND OFF-BALANCE SHEET RISK

The International Equity and International Fixed Income Pools include foreign currency forward contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing security positions. The maturity periods for these contracts range from forty-five to ninety-six days. PERS had net unrealized gains (losses) with respect to such contracts, calculated using forward rates at June 30, as follows:

	<b>2004</b>	<b>2003</b>
Net Contract Sales	\$ 4,980,969	\$ 1,002,565
Less: Fair Value	5,312,169	989,706
Net unrealized gains (losses) on contracts	<u>\$ (331,200)</u>	<u>\$ 12,859</u>

The counterparties to the foreign currency forward contracts consist of a diversified group of financial institutions. Credit risk exposure exists to the extent of non-performance by these counterparties; however, the risk of default is considered to be remote. The market risk is limited to the difference between contractual rates and forward rates at the balance sheet date.

# Public Employees' Retirement System

## Invested Assets

### Notes to Schedules

#### June 30, 2004 and 2003

#### (7) COMMITMENTS AND CONTINGENCIES

The Board entered into agreements through external investment managers to provide capital funding for limited and general partnerships as it continues to build the private equity portfolio. At June 30, 2004, PERS Invested Asset's share of these unfunded commitments totaled \$321,598,303 to be paid through the year 2009.

The Board entered into an agreement through an external investment manager to provide capital funding for a limited partnership as it continues to build the other investment portfolio. At June 30, 2004, PERS Invested Asset's share of this unfunded commitment totaled \$46,022,740 to be paid through the year 2014.

The Board entered into agreements through external investment managers to provide capital funding for real estate investments as it continues to build the real estate portfolio. At June 30, 2004, PERS Invested Asset's share of these unfunded commitments totaled \$66,350,007 to be paid through the year 2007.

#### (8) SECURITIES LENDING

Alaska Statute 37.10.071 authorizes the Board to lend assets, under an agreement and for a fee, against deposited collateral of equivalent market value. In January 2001, the Board entered into an agreement with State Street Corporation (the Bank) to lend fixed income, domestic equity and international equity securities. The Bank, acting as the Board's agent under the agreement, transfers securities to broker agents or other entities for collateral in the form of cash or securities and simultaneously agrees to return the collateral for the same securities in the future.

At June 30, 2004 and 2003, the fair value of securities on loan allocable to PERS Invested Assets totaled \$960,292,029 and \$624,927,717, respectively. There is no limit to the amount that can be loaned and the Board is able to sell securities on loan. International equity security loans are fully collateralized at not less than 105 percent of their fair value. All other security loans are fully collateralized at not less than 102 percent of their fair value. The Bank invests the cash collateral in a commingled investment pool; maturities of these investments generally did not match the maturities of the loaned securities because the lending agreements are terminable at will. The Bank may pledge or sell collateral upon borrower default. Since the Board does not have the ability to pledge or sell the collateral unless the borrower defaults, no assets or liabilities are recorded on the financial schedules. There is limited credit risk associated with the lending transactions since the Board is indemnified by the Bank against any loss resulting from counterparty failure or default on a loaned security subject to limitation relating to war, civil unrest or revolution, or beyond the reasonable control of the Bank. The Bank and the borrower receive a fee from earnings on invested collateral.

For the year ended June 30, 2004 and 2003, there were no losses incurred as a result of securities lending transactions and there were no significant violations of legal or contractual provisions nor failures by any borrowers to return loaned securities.