



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

Teachers' Retirement System

Invested Assets

Schedules

June 30, 2004 and 2003

(With Independent Auditors' Report Thereon)

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

Teachers' Retirement System

Invested Assets

Schedules

June 30, 2004 and 2003

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KPMG LLP
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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 Teachers' Retirement System as of June 30, 2004 and 2003 and of investment income (loss) and changes in invested assets of the Teachers' 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 Teachers' Retirement System, which is established under the State of Alaska Teachers Retirement System (TRS). The schedules are not intended to present the financial status of TRS.

In our opinion, the schedules referred to above present fairly, in all material respects, the invested assets of the Teachers' 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
TEACHERS' RETIREMENT SYSTEM**

SCHEDULES OF INVESTED ASSETS

June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Investments (at Fair Value) (Notes 4, 8)		
Cash and Cash Equivalents (Note 3)		
Short-term Fixed Income Pool	\$ <u>522,580</u>	\$ <u>562,637</u>
Marketable Debt Securities (Note 3)		
Retirement Fixed Income Pool	705,056,898	688,460,269
External Domestic Fixed Income Pool	361,318,017	380,442,778
International Fixed Income Pool	<u>142,128,648</u>	<u>133,608,738</u>
Total Marketable Debt Securities	<u>1,208,503,563</u>	<u>1,202,511,785</u>
Equity Securities (Note 3)		
Domestic Equity Pool	1,575,443,964	1,443,740,937
International Equity Pool	642,588,831	556,055,258
Emerging Markets Equity Pool	53,407,169	40,133,330
Private Equity Pool	128,570,997	104,895,604
Other Investments Pool	<u>3,896,845</u>	<u>-</u>
Total Equity Securities	<u>2,403,907,806</u>	<u>2,144,825,129</u>
Real Estate Investments		
Real Estate Pool (Note 3)	295,894,158	251,138,858
Mortgages (Note 2)	<u>60,808</u>	<u>73,850</u>
Total Real Estate Investments	<u>295,954,966</u>	<u>251,212,708</u>
Total Invested Assets	<u>\$ 3,908,888,915</u>	<u>\$ 3,599,112,259</u>

See accompanying notes to schedules

**STATE OF ALASKA
DEPARTMENT OF REVENUE
TREASURY DIVISION
TEACHERS' 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>
Investment Income (Loss) (Note 5)		
Short-term Fixed Income Pool	\$ 14,687	\$ 24,141
Retirement Fixed Income Pool	4,576,852	72,864,202
External Domestic Fixed Income Pool	2,816,646	38,399,352
International Fixed Income Pool	9,995,319	28,632,985
Domestic Equity Pool	277,097,385	4,473,488
International Equity Pool	169,390,801	(35,969,857)
Emerging Markets Equity Pool	13,442,934	2,428,745
Private Equity Pool	22,639,016	(16,099,167)
Other Investments Pool	18,508	-
Real Estate Pool	23,310,945	24,839,329
Mortgages	<u>7,602</u>	<u>39,226</u>
Total Investment Income	523,310,695	119,632,444
Total Invested Assets, Beginning of Year	3,599,112,259	3,684,378,183
Net Withdrawals	<u>(213,534,039)</u>	<u>(204,898,368)</u>
Total Invested Assets, End of Year	<u>\$ 3,908,888,915</u>	<u>\$ 3,599,112,259</u>

See accompanying notes to schedules

Teachers' Retirement System

Invested Assets

Notes to Schedules June 30, 2004 and 2003

(1) THE ACCOUNTING ENTITY

The Teachers' Retirement System Invested Assets (TRS Invested Assets) is the investment portfolio of the State of Alaska Teachers' Retirement System (TRS). TRS 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 TRS Invested Assets and not TRS taken as a whole. Fiduciary responsibility for TRS Invested Assets resides with the Alaska State Pension Investment Board (Board), pursuant to Alaska Statutes 37.10.210-390.

Alaska Statutes 14.25.180 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 TRS 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.

Teachers' 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 \$29,683 and \$31,023, 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

TRS 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, TRS Invested Assets included a 0.03% direct ownership in the Short-term Fixed Income Pool which included interest receivable of \$3,631 and \$4,077, respectively.

Teachers' Retirement System

Invested Assets

Notes to Schedules

June 30, 2004 and 2003

(3) POOLED INVESTMENTS (Cont.)

Retirement Fixed Income Pool

TRS 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 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, TRS Invested Assets included a 32.39% and 32.74% ownership in the Retirement Fixed Income Pool, respectively.

External Domestic Fixed Income Pool

TRS 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, TRS Invested Assets included a 32.14% and 32.54% ownership in the External Domestic Fixed Income Pool, respectively.

International Fixed Income Pool

TRS 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, TRS Invested Assets included a 32.17% and 32.51% ownership in the International Fixed Income Pool, respectively.

Domestic Equity Pool

TRS 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, TRS Invested Assets included a 32.09% and 32.44% ownership in the Domestic Equity Pool, respectively.

Teachers' Retirement System

Invested Assets

Notes to Schedules

June 30, 2004 and 2003

(3) POOLED INVESTMENTS (Cont.)

International Equity Pool

TRS 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, TRS Invested Assets included a 31.78% and 32.31% ownership in the International Equity Pool, respectively.

Emerging Markets Equity Pool

TRS 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, TRS Invested Assets included a 35.00% ownership in the Emerging Markets Equity Pool.

Private Equity Pool

TRS 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, TRS Invested Assets included a 32.32% and 32.68% ownership in the Private Equity Pool, respectively.

Teachers' Retirement System

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Notes to Schedules

June 30, 2004 and 2003

(3) POOLED INVESTMENTS (Cont.)

Other Investments Pool

TRS 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, TRS Invested Assets included a 32.32% ownership in the Other Investments Pool.

Real Estate Pool

TRS 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, TRS Invested Assets included a 31.80% and 32.46% ownership in the Real Estate Pool, respectively.

Teachers' Retirement System

Invested Assets

Notes to Schedules

June 30, 2004 and 2003

(4) DEPOSIT AND INVESTMENT RISK

At June 30, 2004, TRS 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	Equity 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	<u>1,954,800</u>	<u>2,089,174</u>	<u>1,296,222</u>	<u>428,460</u>	<u>8,343,700</u>	<u>14,112,356</u>
Net Pending Security						
Receivables (Payables)	(14,419)	(75,880)	(187,780)	8,963	12,113	(257,003)
Deposits	<u>14,240</u>	<u>163,323</u>	<u>15,901</u>	<u>4,442</u>	<u>68,534</u>	<u>266,440</u>
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	(586)	(1,471,560)	(763,025)	(299,737)	(5,724,484)	(8,259,392)
TRS Invested Assets	<u>\$ 523</u>	<u>\$ 705,057</u>	<u>\$ 361,318</u>	<u>\$ 142,128</u>	<u>\$ 2,699,863</u>	<u>\$ 3,908,889</u>

Teachers' 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.

Teachers' 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, TRS 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	\$ 1,597
International Bank for Reconstruction and Development	Japanese Yen	12/20/2004	3,013
Kreditanstalt Fuer Wiederaufbau International Finance	Japanese Yen	12/20/2004	3,555
Asian Development Bank	Japanese Yen	6/29/2005	4,558
Export Import Bank	Japanese Yen	7/28/2005	1,215
European Investment Bank	Japanese Yen	9/20/2007	1,058
International American Development Bank	Japanese Yen	7/8/2009	5,588
Osterreichische Kontrollbank	Japanese Yen	3/22/2010	3,075
Kreditanstalt Fuer Wiederaufbau International Finance	Japanese Yen	3/23/2010	7,674
SL Finance PLC	Euro Currency	7/12/2022	711
Zurich Finance USA	Euro Currency	10/2/2023	406
Foreign Government:			
Queensland Treasury Corporation	Australian Dollar	6/14/2005	453
Kingdom of Spain	Japanese Yen	9/20/2006	942
Kingdom of Netherlands	Euro Currency	2/15/2007	5,437
New South Wales Treasury Corporation	Australian Dollar	3/1/2008	2,404
Federal National Mortgage Association	Japanese Yen	3/26/2008	1,077
Republic of Italy	Japanese Yen	3/27/2008	3,799
Republic of Poland	Polish Zloty	6/24/2008	2,705
Kingdom of Sweden	Swedish Krona	1/28/2009	6,004
Republic of Italy	Euro Currency	5/1/2009	4,059
Federal Republic of Germany	Euro Currency	7/4/2009	3,578
Kingdom of Spain	Euro Currency	7/30/2009	9,828
Republic of France	Euro Currency	10/25/2009	873
Government of Poland	Polish Zloty	11/24/2009	1,873
Republic of France	Euro Currency	4/25/2010	5,104
Government of Poland	Polish Zloty	11/24/2010	1,609
Republic of Finland	Euro Currency	2/23/2011	3,661
Government of Australia	Australian Dollar	6/15/2011	2,011
Bundesrepublik Deutschland	Euro Currency	7/4/2011	7,047
Japan Financial Corporation	Japanese Yen	2/21/2012	2,078
Kingdom of Sweden	Swedish Krona	10/8/2012	3,409
Federal Republic of Germany	Euro Currency	1/4/2013	6,187
Commonwealth of Australia	Australian Dollar	5/15/2013	4,443
Queensland Treasury Corporation	Australian Dollar	8/14/2013	4,462
Government of Poland	Polish Zloty	10/24/2013	6,308
Kingdom of Sweden	Swedish Krona	5/5/2014	5,939
Kingdom of Sweden	Swedish Krona	12/1/2020	1,277
Bundesrepublik Deutschland	Euro Currency	7/4/2027	8,819
Total International Fixed Income			\$ 137,836

Teachers' 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.

Teachers' 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, TRS Invested Assets consisted of securities with credit quality ratings issued by nationally recognized statistical rating organizations as follows:

	<u>Rating¹</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 ²	-	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%

¹Rating modifiers are not disclosed.

²TBA's issued by U.S. Government Agencies allowed by policy.

Teachers' 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, TRS Invested Assets had the following uncollateralized and uninsured deposits:

	<u>Amount</u> <u>(in thousands)</u>
International Fixed Income Pool	\$ 376
International Equity Pool	1,234
	<u>\$ 1,610</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 TRS 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, TRS invested assets included 3.64% in international fixed income and 17.81% in international equity.

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

<u>Currency</u>	<u>Amount</u> <u>(in thousands)</u>
Australian Dollar	\$ 92
Canadian Dollar	2
Euro Currency	372
Japanese Yen	504
Polish Zloty	165
Pound Sterling	290
South Korean Won	102
Swiss Franc	83
	<u>\$ 1,610</u>

Teachers' 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, TRS had exposure to foreign currency risk with the following investments (stated in thousands):

Currency	Foreign Government	Corporate	Convertible Bonds	Equity
Australian Dollar	\$ 13,772	\$ -	\$ -	\$ 5,223
Canadian Dollar	-	-	-	7,055
Danish Krone	-	-	-	505
Euro Currency	54,593	1,117	107	235,371
Hong Kong Dollar	-	-	-	8,388
Japanese Yen	7,895	31,333	1,216	117,699
New Zealand Dollar	-	-	-	4,906
Norwegian Krone	-	-	-	3,404
Polish Zloty	12,497	-	-	-
Pound Sterling	-	-	-	135,856
Singapore Dollar	-	-	-	10,488
South Korean Won	-	-	-	8,394
Swedish Krona	16,629	-	-	4,496
Swiss Franc	-	-	145	51,514
	\$ 105,386	\$ 32,450	\$ 1,468	\$ 593,299

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, TRS invested assets included \$392,055,890 in Federal National Mortgage Association securities which represented 9.89% of total TRS invested assets.

Teachers' 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	\$ 14,687	\$ -	\$ 14,687
Retirement Fixed Income Pool	36,037,008	(31,460,156)	4,576,852
External Domestic Fixed Income Pool	13,769,570	(10,952,924)	2,816,646
International Fixed Income Pool	6,214,295	3,781,024 (1)	9,995,319
Domestic Equity Pool	22,710,912	254,386,473	277,097,385
International Equity Pool	15,356,573	154,034,228 (2)	169,390,801
Emerging Markets Equity Pool	754,436	12,688,498	13,442,934
Private Equity Pool	3,373,186	19,265,830	22,639,016
Other Investments Pool	-	18,508	18,508
Real Estate Pool	18,070,642	5,240,303	23,310,945
Mortgages	7,602	-	7,602
Total	<u>\$ 116,308,911</u>	<u>\$ 407,001,784</u>	<u>\$ 523,310,695</u>

(1) Includes net realized gains of \$7,873,612 and net unrealized gains of \$1,523 on foreign currency.

(2) Includes net realized gains of \$34,093,119 and net unrealized gains of \$7,651 on foreign currency. Also includes net realized gains of \$38,950 on foreign exchange contracts.

Teachers' Retirement System

Invested Assets

Notes to Schedules

June 30, 2004 and 2003

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

	2003		
	Interest and/or dividends	Net increase (decrease) in the fair value of investments	Total
Short-term Fixed Income Pool	\$ 24,141	\$ -	\$ 24,141
Retirement Fixed Income Pool	39,568,371	33,295,831	72,864,202
External Domestic Fixed Income Pool	14,201,433	24,197,919	38,399,352
International Fixed Income Pool	6,592,145	22,040,840 (1)	28,632,985
Domestic Equity Pool	21,124,243	(16,650,755)	4,473,488
International Equity Pool	13,946,288	(49,916,145) (2)	(35,969,857)
Emerging Markets Equity Pool	357,385	2,071,360	2,428,745
Private Equity Pool	420,226	(16,519,393)	(16,099,167)
Real Estate Pool	21,345,354	3,493,975	24,839,329
Mortgages	39,226	-	39,226
Total	<u>\$ 117,618,812</u>	<u>\$ 2,013,632</u>	<u>\$ 119,632,444</u>

(1) Includes net realized gains of \$6,554,828 and net unrealized gains of \$60 on foreign currency.

(2) Includes net realized gains of \$7,828,324 and net unrealized losses of \$9,721 on foreign currency. Also includes net realized losses of \$534,228 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. TRS had net unrealized gains (losses) with respect to such contracts, calculated using forward rates at June 30, as follows:

	<u>2004</u>	<u>2003</u>
Net Contract Sales	\$ 2,412,498	\$ 426,973
Less: Fair Value	<u>2,571,117</u>	<u>421,496</u>
Net unrealized gains (losses) on contracts	<u>\$ (158,619)</u>	<u>\$ 5,477</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.

Teachers' 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, TRS Invested Asset's share of these unfunded commitments totaled \$153,577,900 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, TRS Invested Asset's share of this unfunded commitment totaled \$21,977,260 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, TRS Invested Asset's share of these unfunded commitments totaled \$31,242,446 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 TRS Invested Assets totaled \$459,195,625 and \$303,477,504, 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.