



NORTH CAROLINA

OFFICE OF THE TREASURER

JANET COWELL, TREASURER

May 21, 2012

Joint Legislative Commission
on Governmental Operations
North Carolina General Assembly
Raleigh, North Carolina 27601

Re: Quarterly report on Investment Funds for the period ended March 31, 2012.

Commission Members:

Pursuant to G.S.147-68, we are providing a report on the investment activities of the State Treasurer. The report outlines investment activities in summary form for:

- The Cash Management Program – responsible for managing the operating funds of the State. The primary participants in this program are the State's General Fund and Highway Funds.
- The Trust Funds Investment Program – responsible for managing assets of the Teachers' and State Employees' Retirement System, the Consolidated Judicial Retirement System, the Firemen's and Rescue Workers' Pension Fund, the Local Governmental Employees' Retirement System, the Legislative Retirement System, and the North Carolina National Guard Pension Fund. Collectively, these systems and funds are referred to as the North Carolina Retirement Systems of the Pension Fund. The Trust Funds Investment Program also includes other participants such as, the State Health Plan, the Disability Income Plan, and the State Educational Assistance Authority.
- The Ancillary Investment Programs - as authorized by the General Assembly, responsible for managing assets for the Escheats Fund, Public Hospital Funds and the Local Government Other Post-Employment Benefits Fund.



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Cash Management Program

The Cash Management Program, composed mostly of the Short-Term Investment Fund (“STIF”), produced a one year return of 0.68% for the participants. It also includes the Bond Proceeds Fund which is a separate investment account for each state bond issue to comply with Internal Revenue Service regulations on bond arbitrage.

Short Term Investment Fund

<u>Historical T-Bill rates</u>	<u>3/31/11</u>	<u>9/30/11</u>	<u>3/30/12</u>
3-Mo. T-Bill	0.091%	0.020%	0.066%
6-Mo. T-Bill	0.169%	0.051%	0.132%

The Short-Term Investment Fund produced a one year return of 0.68% for the participants. The investable balances earning income for the General Fund were \$83 million lower than one year earlier based on book value. The investable balances, which earn income for the Highway Funds, were \$42 million lower than at the same time last year.

The investments held by the STIF on a particular date may be accruing income at different levels from current short-term interest rates. For example, if the investments were made when interest rates were lower, the earnings would continue to be at the lower rates of return, even though current interest rates may have moved higher. This happens in reverse as well.

The Bond Proceeds Fund are managed by a private investment company under contract with the Department of State Treasurer. The investments are valued at amortized cost, which approximates fair value.

Trust Funds Investment Program

The investment results for the Trust Funds Investment Program (“Trust Funds”) are managed and reported on a cumulative total return basis. Total return includes realized income and the appreciation or depreciation of fair market value. Two funds comprise the vast majority of the Trust Funds assets. They are the Long-Term Investment Fund (“LTIF”) and the Equity Investment Fund (“EIF”).

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
Total Trust Returns:	5.24%	8.36%	14.17%	3.68%

Long Term Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
LTIF Returns:	11.36%	9.45%	9.99%	8.28%



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The below table provides a trend comparison of the current Treasury yields to the previous quarter.

US Treasury Yields	<u>5 Year UST</u>	<u>10 Year UST</u>	<u>30 Year UST</u>
As of 12/31/11	0.83%	1.88%	2.89%
As of 3/30/12	1.04%	2.21%	3.34%

- Long Term assets (based on market value) ended the quarter approximately \$278 million lower than at the end of the prior reporting period.
- The realized earnings for the fiscal year to date are \$1.4 billion.
- Approximately \$350 million was used to pay benefits or was reallocated to other investment funds this quarter.

Equity Investment Fund

EIF Returns:	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
	0.28%	7.44%	21.12%	0.98%

The below table provides third quarter equity market returns as measured by major indices.

Quarterly Index Returns:	S&P 500	12.59%	DJIA	8.14%
	Russell 3000	12.87%	MSCI EAFE	10.86%

- Assets of the fund (based on market value) ended the quarter approximately \$3.61 billion higher than at the end of the prior reporting period.
- Approximately \$395 million was used to pay benefits or was reallocated to other investment funds this quarter.

Pursuant to Session Law 2009-98 and G.S.147-69.2, the Treasurer is now authorized to invest in credit and inflation-linked strategies. These new classifications are reflected in the attached report.

Ancillary Investment Programs

The Ancillary Investment Programs, as authorized by the General Assembly, is responsible for managing assets for the Escheats Fund, Public Hospital Funds and the Local Government Other Post-Employment Benefits Fund.

Pursuant to G.S. 116-37, deposits are held for the Watauga Medical Center, New Hanover Memorial Hospital, Margaret R. Pardee Hospital, and Columbus Regional Healthcare System, all subject to compliance with G.S. 147-69.2. The assets are allocated as follows: STIF, LTIF and authorized Equity funds. For the Quarter ending March 31, 2012, the invested assets were valued at \$76.5 million after returns in the domestic and international accounts of 16.48% and 11.52% respectively.



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Pursuant to G.S. 147-69.2(b)(12), up to 20% of the Escheat Fund's assets can be invested in authorized Equity, Real Estate, and Alternative Investments. For the Quarter ending March 31, 2012, \$40 million has been invested in equity, of which \$40.7 million has been received in distributions; \$20 million has been invested in real estate, of which \$15.7 million has been returned; and commitments totaling \$57 million have been made to private equity, of which, \$48.7 million has been contributed.

Pursuant to G.S. 159-30.1, 147-69.2(a)(17g), and 147-69.2(b4), deposits are held for the Local Government Other Post-Employment Benefits Fund. The assets are allocated as follows: STIF, LTIF, and authorized Equity funds. For the Quarter ending March 31, 2012, the externally invested assets were valued at \$52.8 million after returns in the domestic and international equity accounts of 16.48% and 11.52% respectively.

Other Reporting Requirements

Pursuant to Session Law 2007-323 Sec. 13.2.(b), G.S. 147-68(d1), the Treasurer "shall include a specific listing of all investments made with certified green managers and companies and funds that support sustainable practices, including the names of the companies, managers, and funds, the amount invested, and the State's return on investment." Based on currently available research, there is no validation group or process that certifies green managers for investments, and the statute provides no definition of the term "sustainable practices" that would enable the Treasurer to determine which companies and funds would fall under this provision. Thus, it is not possible to report any relevant data at this time.

Thank you for your attention. Please feel free to contact the Department of State Treasurer if you have any questions.

Sincerely,

A handwritten signature in blue ink that reads "Janet Cowell".

Janet Cowell

Attachments

cc: Bryan Lewis, Interim Chief Investment Officer
Fran Lawrence, Chief Financial Officer

DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF NET ASSETS AND PARTICIPANT EQUITY - ALL POOLS AND ACCOUNTS
MARCH 31, 2012

	*Cash Management Program			**Trust Funds Investment Program		All Pools	
	Short-term Investment Fund	Bond Proceeds Fund	Subtotal	Subtotal	Intrafund Eliminations	Total	
Net Assets:							
Investment Securities:							
Cash Equivalents	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	
Certificates of Deposit	39,300,000	-	39,300,000	-	-	39,300,000	
Repurchase Agreements	910,000,000	-	910,000,000	-	-	910,000,000	
Discount Notes/Bills	-	-	-	-	-	-	
U.S. Treasury Bills/ Notes/ Bonds	5,370,914,125	-	5,370,914,125	8,727,003,962	-	14,097,918,087	
U.S. Government Agency Notes/ Bonds	5,438,769,498	-	5,438,769,498	1,876,808,299	-	7,315,577,797	
GNMA Certificates	-	-	-	6,870,941,357	-	6,870,941,357	
Corporate Obligations	254,988,283	-	254,988,283	10,413,661,618	-	10,668,649,901	
Other Investments	-	-	-	10,041,536	-	10,041,536	
Investments in RMBS and CMBS	-	-	-	593,974,150	-	593,974,150	
Investments in Equity Securities	-	-	-	4,801,763	-	4,801,763	
Bond proceeds Advisory	-	71,811,381	71,811,381	-	-	71,811,381	
Investments in Equity Trusts	-	-	-	34,492,299,175	-	34,492,299,175	
Investments in Real Estate Trust Funds & Partnerships	-	-	-	5,587,381,319	-	5,587,381,319	
Investments in Alternative Partnerships	-	-	-	3,678,150,325	-	3,678,150,325	
Investments in Credit Partnerships	-	-	-	2,915,586,008	-	2,915,586,008	
Investments in Inflation Partnerships	-	-	-	1,263,957,927	-	1,263,957,927	
Total Investment Securities	\$ 12,013,971,906	\$ 71,811,381	\$ 12,085,783,287	\$ 76,434,607,439	\$ -	\$ 88,520,390,726	
Cash in Bank	170,431,305	-	170,431,305	-	-	170,431,305	
Deposits in Short-term Investment Fund	-	-	-	442,683,028	(442,683,028)	-	
Other Assets, Net of Liabilities	24,146,845	-	24,146,845	239,588,859	-	263,735,704	
Total Net Assets	\$ 12,208,550,056	\$ 71,811,381	\$ 12,280,361,437	\$ 77,116,879,326	\$ (442,683,028)	\$ 88,954,557,735	
Participant Equity:							
General Fund	\$ 1,330,815,389	\$ -	\$ 1,330,815,389	\$ -	\$ -	\$ 1,330,815,389	
Other Funds Which Earn Interest for General Fund	1,437,247,875	71,811,381	1,509,059,256	-	-	1,509,059,256	
Highway Fund	614,524,528	-	614,524,528	-	-	614,524,528	
Highway Trust Fund	350,977,888	-	350,977,888	-	-	350,977,888	
University Trust Funds	2,729,594,220	-	2,729,594,220	-	-	2,729,594,220	
Pension Trust Funds	112,862,566	-	112,862,566	75,921,382,043	-	76,034,244,609	
Other Independent Trust Funds	4,284,494,163	-	4,284,494,163	1,195,497,283	-	5,479,991,446	
Local Political Subdivisions	878,938,619	-	878,938,619	-	-	878,938,619	
Licensing Boards	26,411,779	-	26,411,779	-	-	26,411,779	
Other Investment Funds	442,683,029	-	442,683,029	-	(442,683,029)	-	
Total Participant Equity	\$ 12,208,550,056	\$ 71,811,381	\$ 12,280,361,437	\$ 77,116,879,326	\$ (442,683,029)	\$ 88,954,557,734	1.00
Percent of Total	13.72	0.08	13.81	86.69	-0.50	100.00	

* The Cash Management Program is presented at book value.

**The Trust Funds Investment Program is presented at market value. Trust Funds detail is included on Combining Statement of Net Assets and Participant Equity.

DEPARTMENT OF STATE TREASURER
COMBINING STATEMENT OF NET ASSETS AND PARTICIPANT EQUITY - TRUST FUNDS INVESTMENT PROGRAM
MARCH 31, 2012

	Long-term Investment Fund	External Fixed Inc. Investment Fund	Equity Investment Fund	Real Estate Investment Fund	Alternative Investment Fund	Credit Investment Fund	Inflation Investment Fund	Totals
Net Assets:								
Investment Securities:								
Cash and Cash Equivalents	\$						\$	
U.S. Treasury Bills/ Notes/ Bonds	8,067,642,055						659,361,907	8,727,003,962
U.S. Government Agency Notes/ Bonds	1,458,734,052	33,934,071					384,140,176	1,876,808,299
GNMA Certificates	6,870,941,357							6,870,941,357
Corporate Obligations	10,413,661,618							10,413,661,618
Other Investments		10,041,536						10,041,536
Investments in RMBS and CMBS		593,974,150						593,974,150
Investments in Equity Securities					4,801,763			4,801,763
Bond Proceeds Advisory								-
Investments in Equity Trusts			34,492,299,175					34,492,299,175
Investments in Real Estate Trust Funds & Partnerships				5,587,381,319				5,587,381,319
Investments in Alternative Partnerships					3,678,150,325			3,678,150,325
Investments in Credit Partnerships						2,915,586,008		2,915,586,008
Investments in Inflation Partnerships & Other Invest.							1,263,957,927	1,263,957,927
Total Investment Securities	\$ 26,810,979,082	\$ 637,949,757	\$ 34,492,299,175	\$ 5,587,381,319	\$ 3,682,952,088	\$ 2,915,586,008	\$ 2,307,460,010	\$ 76,434,607,439
Cash in Bank								-
Deposits in Short-term Investment Fund	128,963,100	237,714,845	2,367,590	19,932,721	8,555,322	36,297,146	8,852,304	442,683,028
Other Assets, Net of Liabilities	240,811,607	171,616					(1,394,364)	239,588,859
Total Net Assets	\$ 27,180,753,789	\$ 875,836,218	\$ 34,494,666,765	\$ 5,607,314,040	\$ 3,691,507,410	\$ 2,951,883,154	\$ 2,314,917,950	\$ 77,116,879,326
Participant Equity:								
Pension Trust Funds	25,985,256,506	875,836,218	34,494,666,765	5,607,314,040	3,691,507,410	2,951,883,154	2,314,917,950	75,921,382,043
Other Independent Trust Funds	1,195,497,283	-	-	-	-	-	-	1,195,497,283
Total Participant Equity	\$ 27,180,753,789	\$ 875,836,218	\$ 34,494,666,765	\$ 5,607,314,040	\$ 3,691,507,410	\$ 2,951,883,154	\$ 2,314,917,950	\$ 77,116,879,326
Percent of Total	35.25	1.14	44.72	7.27	4.79	3.83	3.00	100.00

**DEPARTMENT OF STATE TREASURER
ANCILLARY INVESTMENT PROGRAMS**

MARCH 31, 2012

	<u>Escheats External Investments</u>	<u>OPEB External Investments</u>	<u>Hospital External Investments</u>	<u>Totals</u>
Net Assets:				
Deposits in Equity Investment Fund	\$ 352,254	52,773,287	76,539,479	\$ 129,665,020
Deposits in Real Estate Investment Fund	799,814			799,814
Deposits in Alternative Investment Fund	38,685,629			38,685,629
Other Assets, Net of Liabilities				-
Total Net Assets	<u>\$ 39,837,697</u>	<u>\$ 52,773,287</u>	<u>\$ 76,539,479</u>	<u>\$ 169,150,463</u>

**DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF OPERATIONS - ALL POOLS AND ACCOUNTS
FOR THE PERIOD ENDED MARCH 31, 2012**

	Cash Management Program			*Trust Funds	Memorandum	
	Short-term	Bond	Subtotal	Investment Program	Intrafund	Total
	Investment	Proceeds		Subtotal		
Fund	Fund					
Revenues:						
Investment Income:						
Investment Earnings	\$ 69,177,448	45,453	\$ 69,222,901	\$ 2,263,839,142	\$ -	\$ 2,333,062,043
Intra-Pool Interest Earnings			-	5,194,956	(5,194,956)	-
Income from Security Lending			-	12,909,846	-	12,909,846
Commission Recapture			-	60,907	-	60,907
Other Income			-	1,559,065	-	1,559,065
Subtotal	69,177,448	45,453	69,222,901	2,283,563,916	(5,194,956)	2,347,591,861
Net Unrealized Appreciation/Depreciation				583,730,441	-	583,730,441
Total Investment Income	69,177,448	45,453	69,222,901	2,867,294,357	(5,194,956)	2,931,322,302
Expenditures:						
Treasurer's Allocated Cost	(1,452,240)		(1,452,240)	(3,263,406)	-	(4,715,646)
Management Fees		(31,738)	(31,738)	(194,526,334)	-	(194,558,072)
Dividend Withholding Tax			-	(15,704,595)	-	(15,704,595)
Other Cost	(1,187,161)		(1,187,161)	(26,640,092)	-	(27,827,253)
Total Expenditures	(2,639,401)	(31,738)	(2,671,139)	(240,134,427)	-	(242,805,566)
Net Investment Income (Loss)	\$ 66,538,047	\$ 13,715	\$ 66,551,762	\$ 2,627,159,930	\$ (5,194,956)	\$ 2,688,516,736
Total Investment Income Allocated:						
General Fund	\$ 9,673,913		9,673,913	\$ -	\$ -	\$ 9,673,913
Highway Fund	3,815,578		3,815,578	-	-	3,815,578
Highway Trust Fund	1,653,771		1,653,771	-	-	1,653,771
University Trust Funds	15,062,843		15,062,843	-	-	15,062,843
Pension Trust Funds	2,166,339		2,166,339	2,534,499,748	-	2,536,666,087
Other Independent Trust Funds	24,257,716		24,257,716	92,660,182	-	116,917,898
Local Political Subdivisions	4,555,855		4,555,855	-	-	4,555,855
Licensing Boards	157,075		157,075	-	-	157,075
Other Investment Funds	5,194,957	13,715	5,208,672	-	(5,194,956)	13,716
Total Investment Income Allocated	\$ 66,538,047	\$ 13,715	\$ 66,551,762	\$ 2,627,159,930	\$ (5,194,956)	\$ 2,688,516,736
Cash Return, Fiscal Year-to-Date (Annualized)	0.6820%	0.020%	0.6810%			

*Trust Funds detail is included on the Combining Statement of Operations-Trust Funds Investment Program.

**DEPARTMENT OF STATE TREASURER
COMBINING STATEMENT OF OPERATIONS - TRUST FUNDS INVESTMENT PROGRAM
FOR THE PERIOD ENDED MARCH 31, 2012**

Trust Funds Investment Program

	Long-term Investment Fund	External Fixed Inc. Investment Fund	Equity Investment Fund	Real Estate Investment Fund	Alternative Investment Fund	Credit Investment Fund	Inflation Investment Fund	Totals
Revenues:								
Investment Income:								
Investment Earnings	\$ 1,362,545,006	59,036,440	539,981,251	103,067,139	241,179,725	45,637,799	(87,608,218)	\$ 2,263,839,142
Intra-Pool Interest Earnings	1,335,337	3,204,571	16,477	172,784	326,119	88,891	50,777	5,194,956
Income from Security Lending			12,909,846					12,909,846
Commission Recapture			60,907					60,907
Other Income			1,559,065					1,559,065
Subtotal	<u>1,363,880,343</u>	<u>62,241,011</u>	<u>554,527,546</u>	<u>103,239,923</u>	<u>241,505,844</u>	<u>45,726,690</u>	<u>(87,557,441)</u>	<u>2,283,563,916</u>
Net Unrealized Appreciation/Depreciation	<u>862,769,386</u>	<u>(32,754,760)</u>	<u>(299,027,020)</u>	<u>254,013,840</u>	<u>(87,419,318)</u>	<u>(76,573,016)</u>	<u>(37,278,671)</u>	<u>583,730,441</u>
Total Investment Income	<u>2,226,649,729</u>	<u>29,486,251</u>	<u>255,500,526</u>	<u>357,253,763</u>	<u>154,086,526</u>	<u>(30,846,326)</u>	<u>(124,836,112)</u>	<u>2,867,294,357</u>
Expenditures:								
Treasurer's Allocated Cost	(1,210,978)	(53,484)	(1,402,963)	(215,843)	(160,415)	(119,788)	(99,935)	(3,263,406)
Management Fees		(6,828,767)	(76,300,083)	(49,073,776)	(32,403,057)	(11,627,793)	(18,292,858)	(194,526,334)
Dividend Withholding Tax			(15,572,325)	(132,270)				(15,704,595)
Other Cost	(816,751)	(991,935)	(1,642,960)	(9,491,243)	(7,055,484)	(3,786,916)	(2,854,803)	(26,640,092)
Total Expenditures	<u>(2,027,729)</u>	<u>(7,874,186)</u>	<u>(94,918,331)</u>	<u>(58,913,132)</u>	<u>(39,618,956)</u>	<u>(15,534,497)</u>	<u>(21,247,596)</u>	<u>(240,134,427)</u>
Net Investment Income (Loss)	\$ <u>2,224,622,000</u>	\$ <u>21,612,065</u>	\$ <u>160,582,195</u>	\$ <u>298,340,631</u>	\$ <u>114,467,570</u>	\$ <u>(46,380,823)</u>	\$ <u>(146,083,708)</u>	\$ <u>2,627,159,930</u>
Total Investment Income Allocated:								
General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	-
Highway Fund	-	-	-	-	-	-	-	-
Highway Trust Fund	-	-	-	-	-	-	-	-
University Trust Funds	-	-	-	-	-	-	-	-
Pension Trust Funds	2,131,961,818	21,612,065	160,582,195	298,340,631	114,467,570	(46,380,823)	(146,083,708)	2,534,499,748
Other Independent Trust Funds	92,660,182	-	-	-	-	-	-	92,660,182
Local Political Subdivisions	-	-	-	-	-	-	-	-
Licensing Boards	-	-	-	-	-	-	-	-
Other Investment Funds	-	-	-	-	-	-	-	-
Total Investment Income Allocated	\$ <u>2,224,622,000</u>	\$ <u>21,612,065</u>	\$ <u>160,582,195</u>	\$ <u>298,340,631</u>	\$ <u>114,467,570</u>	\$ <u>(46,380,823)</u>	\$ <u>(146,083,708)</u>	\$ <u>2,627,159,930</u>

Total Return, 12, 24, and 36 and 60 months:

12 months	11.36%	4.66%	0.28%	10.66%	7.92%	0.28%	-8.61%	5.24%
24 months	9.45%	7.85%	7.44%	10.32%	9.09%	9.15%	-11.14%	8.36%
36 months	9.99%	11.92%	21.12%	-1.71%	8.74%	N/A	N/A	14.17%
60 months	8.28%	N/A	0.98%	-4.56%	3.19%	N/A	N/A	3.68%