



JANET COWELL
TREASURER

NORTH CAROLINA
DEPARTMENT OF STATE TREASURER
INVESTMENT MANAGEMENT DIVISION

KEVIN SIGRIST
STATE INVESTMENT OFFICER

February 7, 2014

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

Re: Quarterly report on Investment Funds for the period ended
December 31, 2013.

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 Squad Workers' Pension Fund, the Local Governmental Employees' Retirement System, the Legislative Retirement System, the North Carolina National Guard Pension Fund and the Retiree Health Benefit Trust Fund. Collectively, these systems and funds are referred to as the North Carolina Retirement Systems or 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, CEEF and the Local Government Other Post-Employment Benefits Fund.

Cash Management Program

The Cash Management Program, composed mostly of the Short-Term Investment Fund ("STIF"), produced a one year return of 0.46% 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>12/31/12</u>	<u>6/30/13</u>	<u>12/31/13</u>
3-Mo. T-Bill	0.043%	0.033%	0.068%
6-Mo. T-Bill	0.114%	0.094%	0.089%

The Short-Term Investment Fund produced a one year return of 0.46% for the participants. The investable balances earning income for the General Fund were \$804 million higher than one year earlier based on book value. The investable balances, which earn income for the Highway Funds, were \$48 million higher 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 is 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:	12.03%	11.90%	8.59%	10.43%

Long Term Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
LTIF Returns:	-3.74%	1.52%	4.79%	6.07%

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 9/30/13	1.382%	2.611%	3.686%
As of 12/31/13	1.743%	3.029%	3.969%

- Long Term assets (based on market value) ended the quarter approximately \$60 million lower than at the end of the prior reporting period.
- The realized earnings for the fiscal year to date are \$638 million.

Equity Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
EIF Returns:	26.24%	21.84%	11.35%	16.12%

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

Quarterly Index Returns:	S&P 500	10.51%	DJIA	9.56%
	Russell 3000	10.10%	MSCI EAFE	5.71%

- Assets of the fund (based on market value) ended the quarter approximately \$1.9 billion higher than at the end of the prior reporting period.
- Approximately \$1.1 billion 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 authorized to invest in credit and inflation-linked strategies. These classifications are reflected in the attached report.

Ancillary Investment Programs

The Ancillary Investment Programs, as authorized by the General Assembly, are responsible for managing assets for the Escheats Fund, Public Hospital Funds, the Local Government Other Post-Employment Benefits Fund and the Conservation Easement Endowment 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 December 31, 2013, the invested assets were valued at \$113 million after returns in the domestic and international equity accounts of 10.53% and 5.36% respectively.

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 December 31, 2013, \$40 million has been invested in equity, of which \$40.8 million has been received in distributions; \$20 million has been invested in real estate, of which \$16.5 million has been returned; and commitments totaling \$57.1 million have been made to private equity, of which \$51.3 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 December 31, 2013, the externally invested

assets were valued at \$94.5 million after returns in the domestic and international equity accounts of 10.53% and 5.36% 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". The signature is written in a cursive style with a large initial "J" and "C".

Janet Cowell

Attachments

cc: Kevin SigRist, Chief Investment Officer
Fran Lawrence, Chief Financial Officer

**DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF NET POSITION - ALL POOLS AND ACCOUNTS
DECEMBER 31, 2013**

	*Cash Management Program			**Trust Funds Investment Program		All Pools
	Short-term	Bond	Subtotal	Subtotal	Intrafund Eliminations	Total
	Investment Fund	Proceeds Fund				
Net Assets:						
Investment Securities:						
Cash Equivalents	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Certificates of Deposit	13,600,000	-	13,600,000	-	-	13,600,000
Repurchase Agreements	1,650,000,000	-	1,650,000,000	-	-	1,650,000,000
Discount Notes/Bills	-	-	-	-	-	-
U.S. Treasury Bills/ Notes/ Bonds	5,503,507,061	-	5,503,507,061	8,546,755,340	-	14,050,262,401
U.S. Government Agency Notes/ Bonds	6,305,447,583	-	6,305,447,583	1,753,145,558	-	8,058,593,141
GNMA Certificates	-	-	-	6,820,630,926	-	6,820,630,926
Corporate Obligations	4,992,059	-	4,992,059	9,931,916,368	-	9,936,908,427
Other Investments	-	-	-	4,175,189	-	4,175,189
Investments in RMBS and CMBS	-	-	-	347,523,066	-	347,523,066
Investments in Equity Securities	-	-	-	2,129,664	-	2,129,664
Bond proceeds Advisory	-	40,705,990	40,705,990	-	-	40,705,990
Investments in Equity Trusts	-	-	-	41,490,720,074	-	41,490,720,074
Investments in Real Estate Trust Funds & Partnerships	-	-	-	7,118,767,672	-	7,118,767,672
Investments in Alternative Partnerships	-	-	-	3,863,206,599	-	3,863,206,599
Investments in Credit Partnerships	-	-	-	4,083,452,126	-	4,083,452,126
Investments in Inflation Partnerships	-	-	-	1,721,702,128	-	1,721,702,128
Total Investment Securities	\$ 13,477,546,703	\$ 40,705,990	\$ 13,518,252,693	\$ 85,684,124,710	\$ -	\$ 99,202,377,403
Cash in Bank	248,521,828	-	248,521,828	-	-	248,521,828
Deposits in Short-term Investment Fund	-	-	-	1,269,395,059	(1,269,395,059)	-
Other Assets, Net of Liabilities	21,079,632	-	21,079,632	272,321,071	-	293,400,703
Total Net Assets	\$ 13,747,148,163	\$ 40,705,990	\$ 13,787,854,153	\$ 87,225,840,840	\$ (1,269,395,059)	\$ 99,744,299,934
Participant Equity:						
General Fund	\$ 2,575,575,773	-	\$ 2,575,575,773	\$ -	\$ -	\$ 2,575,575,773
Other Funds Which Earn Interest for General Fund	1,235,615,114	40,705,990	1,276,321,104	-	-	1,276,321,104
Highway Fund	252,870,583	-	252,870,583	-	-	252,870,583
Highway Trust Fund	717,351,922	-	717,351,922	-	-	717,351,922
University Trust Funds	2,681,031,121	-	2,681,031,121	-	-	2,681,031,121
Pension Trust Funds	191,362,714	-	191,362,714	86,019,298,984	-	86,210,661,698
Other Independent Trust Funds	4,017,725,813	-	4,017,725,813	1,206,541,856	-	5,224,267,669
Local Political Subdivisions	778,511,333	-	778,511,333	-	-	778,511,333
Licensing Boards	27,708,731	-	27,708,731	-	-	27,708,731
Other Investment Funds	1,269,395,059	-	1,269,395,059	-	(1,269,395,059)	-
Total Participant Equity	\$ 13,747,148,163	\$ 40,705,990	\$ 13,787,854,153	\$ 87,225,840,840	\$ (1,269,395,059)	\$ 99,744,299,934
Percent of Total	13.78	0.04	13.82	87.45	-1.27	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 Position.

DEPARTMENT OF STATE TREASURER
COMBINING STATEMENT OF NET POSITION - TRUST FUNDS INVESTMENT PROGRAM
DECEMBER 31, 2013

	Cash Investment Fund	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		7,956,317,228						590,438,112	8,546,755,340
U.S. Government Agency Notes/ Bonds		1,423,763,180	12,384,756					316,997,622	1,753,145,558
GNMA Certificates		6,820,630,926							6,820,630,926
Corporate Obligations		9,931,916,368							9,931,916,368
Other Investments			4,175,189						4,175,189
Investments in RMBS and CMBS			347,523,066						347,523,066
Investments in Equity Securities						2,129,664			2,129,664
Bond Proceeds Advisory									-
Investments in Equity Trusts				41,490,720,074					41,490,720,074
Investments in Real Estate Trust Funds & Partnerships					7,118,767,672				7,118,767,672
Investments in Alternative Partnerships						3,863,206,599			3,863,206,599
Investments in Credit Partnerships							4,083,452,126		4,083,452,126
Investments in Inflation Partnerships & Other Invest.								1,721,702,128	1,721,702,128
Total Investment Securities	\$	26,132,627,702	\$ 364,083,011	\$ 41,490,720,074	\$ 7,118,767,672	\$ 3,865,336,263	\$ 4,083,452,126	\$ 1,721,702,128	\$ 85,684,124,710
Cash in Bank									-
Deposits in Short-term Investment Fund	423,795,933	845,599,126							1,269,395,059
Other Assets, Net of Liabilities	4,261,418	273,137,897	848,890					(5,927,134)	272,321,071
Total Net Assets	\$ 428,057,351	27,251,364,725	\$ 364,931,901	\$ 41,490,720,074	\$ 7,118,767,672	\$ 3,865,336,263	\$ 4,083,452,126	\$ 2,623,210,728	\$ 87,225,840,840
Participant Equity:									
Pension Trust Funds	\$ 428,057,351	26,044,822,869	364,931,901	41,490,720,074	7,118,767,672	3,865,336,263	4,083,452,126	2,623,210,728	86,019,298,984
Other Independent Trust Funds		1,206,541,856							1,206,541,856
Total Participant Equity	\$ 428,057,351	27,251,364,725	\$ 364,931,901	\$ 41,490,720,074	\$ 7,118,767,672	\$ 3,865,336,263	\$ 4,083,452,126	\$ 2,623,210,728	\$ 87,225,840,840
Percent of Total	0.49	31.24	0.42	47.57	8.16	4.43	4.68	3.01	100.00

**DEPARTMENT OF STATE TREASURER
ANCILLARY INVESTMENT PROGRAMS
DECEMBER 31, 2013**

	<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	\$ 7,321	94,489,486	113,097,260	\$ 207,594,067
Deposits in Alternative Investment Fund	37,515,864			37,515,864
Total Net Assets	<u>\$ 37,523,185</u>	<u>\$ 94,489,486</u>	<u>\$ 113,097,260</u>	<u>\$ 245,109,931</u>

**DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF OPERATIONS - ALL POOLS AND ACCOUNTS
FOR THE PERIOD ENDED DECEMBER 31, 2013**

	Cash Management Program			*Trust Funds Investment Program	Memorandum	
	Short-term Investment Fund	Bond Proceeds Fund	Subtotal	Subtotal	Intrafund Eliminations	Total
Revenues:						
Investment Income:						
Investment Earnings	\$ 34,328,224	11,586	\$ 34,339,810	\$ 4,697,661,062	\$ -	\$ 4,732,000,872
Intra-Pool Interest Earnings			-	1,406,889	(1,406,889)	-
Income from Security Lending			-	5,938,945	-	5,938,945
Commission Recapture			-	53,434	-	53,434
Other Income			-	1,649,242	-	1,649,242
Subtotal	34,328,224	11,586	34,339,810	4,706,709,572	(1,406,889)	4,739,642,493
Net Unrealized Appreciation/Depreciation				2,652,837,204	-	2,652,837,204
Total Investment Income	34,328,224	11,586	34,339,810	7,359,546,776	(1,406,889)	7,392,479,697
Expenditures:						
Treasurer's Allocated Cost	(656,166)		(656,166)	(2,456,167)	-	(3,112,333)
Management Fees		(6,218)	(6,218)	(77,900,814)	-	(77,907,032)
Dividend Withholding Tax			-	(10,597,849)	-	(10,597,849)
Other Cost	(1,079,762)		(1,079,762)	(25,055,108)	-	(26,134,870)
Total Expenditures	(1,735,928)	(6,218)	(1,742,146)	(116,009,938)	-	(117,752,084)
Net Investment Income (Loss)	\$ 32,592,296	\$ 5,368	\$ 32,597,664	\$ 7,243,536,838	\$ (1,406,889)	\$ 7,274,727,613
Total Investment Income Allocated:						
General Fund	\$ 9,398,975		9,398,975	\$ -	\$ -	\$ 9,398,975
Highway Fund	904,762		904,762	-	-	904,762
Highway Trust Fund	1,499,153		1,499,153	-	-	1,499,153
University Trust Funds	6,367,887		6,367,887	-	-	6,367,887
Pension Trust Funds	929,830		929,830	7,239,478,967	-	7,240,408,797
Other Independent Trust Funds	8,982,128		8,982,128	4,057,871	-	13,039,999
Local Political Subdivisions	1,814,934		1,814,934	-	-	1,814,934
Licensing Boards	63,623		63,623	-	-	63,623
Other Investment Funds	2,631,004	5,368	2,636,372	-	(1,406,889)	1,229,483
Total Investment Income Allocated	\$ 32,592,296	\$ 5,368	\$ 32,597,664	\$ 7,243,536,838	\$ (1,406,889)	\$ 7,274,727,613

Cash Return, Fiscal Year-to-Date (Annualized) 0.4580% 0.010% 0.4570%

*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 DECEMBER 31, 2013**

	Trust Funds Investment Program								Totals
	Cash Investment Fund	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	
Revenues:									
Investment Income:									
Investment Earnings	\$ 1,225,827	633,765,197	11,718,402	3,716,824,881	188,775,389	142,069,817	10,063,514	(6,781,965)	\$ 4,697,661,062
Intra-Pool Interest Earnings		1,406,889							1,406,889
Income from Security Lending				5,938,945					5,938,945
Commission Recapture				53,434					53,434
Other Income	34,030			1,615,212					1,649,242
Subtotal	1,259,857	635,172,086	11,718,402	3,724,432,472	188,775,389	142,069,817	10,063,514	(6,781,965)	4,706,709,572
Net Unrealized Appreciation/Depreciation		(541,893,173)	2,020,105	2,650,560,631	95,527,620	135,214,304	227,658,719	83,748,998	2,652,837,204
Total Investment Income	1,259,857	93,278,913	13,738,507	6,374,993,103	284,303,009	277,284,121	237,722,233	76,967,033	7,359,546,776
Expenditures:									
Treasurer's Allocated Cost	(13,977)	(798,760)	(14,113)	(1,147,698)	(190,701)	(109,567)	(108,380)	(72,971)	(2,456,167)
Management Fees			(905,477)	(25,753,697)	(17,610,175)	(19,594,326)	(1,002,967)	(13,034,172)	(77,900,814)
Dividend Withholding Tax				(10,543,834)	(54,015)				(10,597,849)
Other Cost	(101)	(828,154)	(191,509)	(926,186)	(1,186,311)	(13,888,006)	(2,479,364)	(5,555,477)	(25,055,108)
Total Expenditures	(14,078)	(1,626,914)	(1,111,099)	(38,371,415)	(19,041,202)	(33,591,899)	(3,590,711)	(18,662,620)	(116,009,938)
Net Investment Income (Loss)	\$ 1,245,779	91,651,999	12,627,408	6,336,621,688	265,261,807	243,692,222	234,131,522	58,304,413	\$ 7,243,536,838
Total Investment Income Allocated:									
General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Highway Fund	-	-	-	-	-	-	-	-	-
Highway Trust Fund	-	-	-	-	-	-	-	-	-
University Trust Funds	-	-	-	-	-	-	-	-	-
Pension Trust Funds	1,245,779	87,594,128	12,627,408	6,336,621,688	265,261,807	243,692,222	234,131,522	58,304,413	7,239,478,967
Other Independent Trust Funds		4,057,871							4,057,871
Local Political Subdivisions	-	-	-	-	-	-	-	-	-
Licensing Boards	-	-	-	-	-	-	-	-	-
Other Investment Funds	-	-	-	-	-	-	-	-	-
Total Investment Income Allocated	\$ 1,245,779	91,651,999	12,627,408	6,336,621,688	265,261,807	243,692,222	234,131,522	58,304,413	\$ 7,243,536,838
Total Return, 12, 24, and 36 and 60 months:									
12 months	N/A	-3.74%	4.64%	26.24%	11.56%	11.54%	16.56%	-3.05%	12.03%
24 months	N/A	1.52%	10.47%	21.84%	10.21%	8.48%	15.24%	-1.05%	11.90%
36 months	N/A	4.79%	7.17%	11.35%	10.89%	9.60%	10.73%	-2.57%	8.59%
60 months	N/A	6.07%	10.85%	16.12%	-1.79%	6.34%	N/A	N/A	10.43%