



NORTH CAROLINA

OFFICE OF THE TREASURER

JANET COWELL, TREASURER

June 15, 2011

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, 2011.

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, UNC and Public Hospital Funds, and the Local Government Other Post-Employment Benefits Fund.

Cash Management Program

The Cash Management Program, comprised mostly of the Short-Term Investment Fund ("STIF"), produced a fiscal year return of 0.989% 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>3/31/10</u>	<u>12/31/10</u>	<u>3/31/11</u>
3-Mo. T-Bill	0.15%	0.12%	0.09%
6-Mo. T-Bill	0.23%	0.18%	0.17%

The Short-Term Investment Fund produced a fiscal year return of 1.006% for the participants. The investable balances earning income for the General Fund were \$164 million higher than one year earlier based on book value. The investable balances, which earn income for the Highway Funds, were \$60 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:	11.58%	18.91%	3.69%	4.50%

Long Term Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
LTIF Returns:	7.57%	9.32%	7.11%	7.42%

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

<u>US Treasury Yields</u>	<u>5 Year UST</u>	<u>10 Year UST</u>	<u>30 Year UST</u>
As of 12/31/10	2.01%	3.29%	4.33%
As of 3/31/11	2.28%	3.47%	4.51%

- Long Term assets (based on market value) ended the quarter approximately \$656 million higher than at the end of the prior reporting period.
- The realized earnings for the fiscal year to date are \$1.11 billion.

Equity Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
EIF Returns:	15.11%	33.11%	2.92%	2.93%

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

Quarterly Index Returns:	S&P 500	5.92%	DJIA	6.41%
	Russell 3000	6.38%	MSCI EAFE	3.37%

- Assets of the fund (based on market value) ended the quarter approximately \$2.02 billion lower than at the end of the prior reporting period.
- Approximately \$3.7 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 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, UNC and Public Hospital Funds, and the Local Government Other Post-Employment Benefits Fund.

Pursuant to G.S. 116-37, deposits are held for the University of North Carolina Hospitals at Chapel Hill Trust, 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, 2011, the invested assets were valued at \$414 million after returns in the domestic and international accounts of 6.43% and 3.41% 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 March 31, 2011, \$40 million has been invested in equity; \$20 million has been invested in real estate, and commitments totaling \$57 million have been made to private equity, of which, \$43.5 million has been contributed.

Pursuant to G.S. 147-69.4, deposits are held for the Local Government Other Post-Employment Benefits Fund, 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, 2011, the externally invested assets were valued at \$35.7 million after returns in the domestic and international equity accounts of 6.43% and 3.41% 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.

During the second quarter of 2011, we anticipate reporting on a survey conducted with the managers of the real estate portfolio. With the survey the Department sought to better understand how real estate investment managers gauge sustainability practices in their investments.

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 black ink that reads "Janet Cowell". The signature is written in a cursive, flowing style.

Janet Cowell

Attachments

cc: Shawn Wischmeier, 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, 2011

	*Cash Management Program			**Trust Funds			All Pools	
	Short-term Investment Fund	Bond Proceeds Fund	Subtotal	Investment Program Subtotal	Intrafund Eliminations	Total		
Net Assets:								
Investment Securities:								
Cash Equivalents	\$ -	\$ -	\$ -	\$ -	-	\$ -		
Certificates of Deposit	37,100,000	-	37,100,000	-	-	37,100,000		
Repurchase Agreements	1,275,000,000	-	1,275,000,000	-	-	1,275,000,000		
Discount Notes/Bills	-	-	-	-	-	-		
U.S. Treasury Bills/ Notes/ Bonds	4,666,025,751	-	4,666,025,751	7,137,757,110	-	11,803,782,861		
U.S. Government Agency Notes/ Bonds	7,817,601,005	-	7,817,601,005	2,306,559,439	-	10,124,160,444		
GNMA Certificates	-	-	-	6,782,075,542	-	6,782,075,542		
Corporate Obligations	364,872,654	-	364,872,654	9,571,708,117	-	9,936,580,771		
Other Investments	-	-	-	60,925,532	-	60,925,532		
Investments in RMBS and CMBS	-	-	-	834,684,634	-	834,684,634		
Investments in Equity Securities	-	-	-	5,855,021	-	5,855,021		
Bond proceeds Advisory	-	123,107,086	123,107,086	-	-	123,107,086		
Investments in Equity Trusts	-	-	-	35,218,060,936	-	35,218,060,936		
Investments in Real Estate Trust Funds & Partnerships	-	-	-	3,923,766,118	-	3,923,766,118		
Investments in Alternative Partnerships	-	-	-	3,620,223,456	-	3,620,223,456		
Investments in Credit Partnerships	-	-	-	2,167,016,344	-	2,167,016,344		
Investments in Inflation Partnerships	-	-	-	629,158,768	-	629,158,768		
Total Investment Securities	\$ 14,160,599,410	\$ 123,107,086	\$ 14,283,706,496	\$ 72,257,791,017	\$ -	\$ 86,541,497,513		
Cash in Bank	117,930,999	-	117,930,999	2,595,060,825	(2,595,060,825)	117,930,999		
Deposits in Short-term Investment Fund	-	-	-	509,267,610	-	509,267,610		
Other Assets, Net of Liabilities	(158,297,106)	-	(158,297,106)	75,362,119,452	(2,595,060,825)	350,970,504		
Total Net Assets	\$ 14,120,233,303	\$ 123,107,086	\$ 14,243,340,389	\$ 75,362,119,452	\$ (2,595,060,825)	\$ 87,010,399,016		
Participant Equity:								
General Fund	\$ 1,334,659,399	\$ -	\$ 1,334,659,399	\$ -	\$ -	\$ 1,334,659,399		
Other Funds Which Earn Interest for General Fund	1,516,378,349	123,107,086	1,639,485,435	-	-	1,639,485,435		
Highway Fund	813,751,164	-	813,751,164	-	-	813,751,164		
Highway Trust Fund	193,944,490	-	193,944,490	-	-	193,944,490		
University Trust Funds	2,545,871,830	-	2,545,871,830	-	-	2,545,871,830		
Pension Trust Funds	144,246,119	-	144,246,119	74,278,810,075	-	74,423,056,194		
Other Independent Trust Funds	4,164,211,451	-	4,164,211,451	1,083,309,377	-	5,247,520,828		
Local Political Subdivisions	784,380,681	-	784,380,681	-	-	784,380,681		
Licensing Boards	27,728,995	-	27,728,995	-	-	27,728,995		
Other Investment Funds	2,595,060,825	-	2,595,060,825	-	(2,595,060,825)	-		
Total Participant Equity	\$ 14,120,233,303	\$ 123,107,086	\$ 14,243,340,389	\$ 75,362,119,452	\$ (2,595,060,825)	\$ 87,010,399,016		
Percent of Total	16.23	0.14	16.37	86.61	-2.98	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, 2011

	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	6,804,911,990						332,845,120	7,137,757,110
U.S. Government Agency Notes/ Bonds	2,306,559,439							2,306,559,439
GNMA Certificates	6,782,075,542							6,782,075,542
Corporate Obligations	9,571,708,117							9,571,708,117
Other Investments		60,925,532						60,925,532
Investments in RMBS and CMBS		834,684,634			5,855,021			834,684,634
Investments in Equity Securities								
Bond Proceeds Advisory								5,855,021
Investments in Equity Trusts			35,218,060,936					35,218,060,936
Investments in Real Estate Trust Funds & Partnerships				3,923,766,118				3,923,766,118
Investments in Alternative Partnerships					3,620,223,456			3,620,223,456
Investments in Credit Partnerships						2,167,016,344		2,167,016,344
Investments in Inflation Partnerships & Other Inv								
Total Investment Securities	\$ 25,465,255,088	\$ 895,610,166	\$ 35,218,060,936	\$ 3,923,766,118	\$ 3,620,078,477	\$ 2,167,016,344	\$ 962,003,888	\$ 72,257,791,017
Cash in Bank								
Deposits in Short-term Investment Fund	327,059,396	2,141,552,965	2,431,959	21,750,668	56,636,395	35,189,673	10,439,769	2,595,060,825
Other Assets, Net of Liabilities	245,034,082	(10,900,652)					275,134,180	509,267,610
Total Net Assets	\$ 26,037,348,566	\$ 3,026,262,479	\$ 35,220,492,895	\$ 3,945,516,786	\$ 3,682,714,872	\$ 2,202,206,017	\$ 1,247,577,837	\$ 75,362,119,452
Participant Equity:								
Pension Trust Funds	24,954,039,189	3,026,262,479	35,220,492,895	3,945,516,786	3,682,714,872	2,202,206,017	1,247,577,837	74,278,810,075
Other Independent Trust Funds	1,083,309,377							1,083,309,377
Total Participant Equity	\$ 26,037,348,566	\$ 3,026,262,479	\$ 35,220,492,895	\$ 3,945,516,786	\$ 3,682,714,872	\$ 2,202,206,017	\$ 1,247,577,837	\$ 75,362,119,452
Percent of Total	34.55	4.02	46.72	5.24	4.89	2.92	1.66	100.00

**DEPARTMENT OF STATE TREASURER
ANCILLARY INVESTMENT PROGRAMS**

MARCH 31, 2011

Net Assets:

Deposits in Equity Investment Fund
Deposits in Real Estate Investment Fund
Deposits in Alternative Investment Fund
Other Assets, Net of Liabilities
Total Net Assets

	Escheats External Investments	OPEB External Investments	Hospital Investment Fund	Totals
\$	36,834,450	35,744,492	414,183,201	\$ 486,762,143
	14,632,337			14,632,337
	33,741,683			33,741,683
\$	<u>85,208,470</u>	<u>\$ 35,744,492</u>	<u>\$ 414,183,201</u>	<u>\$ 535,136,163</u>

Participant Equity:

General Fund
Other Investment Funds
Total Participant Equity

\$	-	\$	-	\$	-
	85,208,470		35,744,492		414,183,201
\$	<u>85,208,470</u>	\$	<u>35,744,492</u>	\$	<u>414,183,201</u>
					535,136,163
					<u>535,136,163</u>

DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF OPERATIONS - ALL POOLS AND ACCOUNTS
FOR THE PERIOD ENDED MARCH 31, 2011

	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	\$ 96,399,434	456,130 \$	96,855,564	\$ 3,770,504,442	\$ -	\$ 3,867,360,006
Intra-Pool Interest Earnings	-	-	-	9,421,429	(9,421,429)	-
Income from Security Lending	-	-	-	15,340,041	-	15,340,041
Commission Recapture	-	-	-	105,601	-	105,601
Other Income	-	-	-	4,271,078	-	4,271,078
Subtotal	96,399,434	456,130	96,855,564	3,799,642,591	(9,421,429)	3,887,076,726
Net Unrealized Appreciation/Depreciation				7,158,405,055	-	7,158,405,055
Total Investment Income	96,399,434	456,130	96,855,564	10,958,047,646	(9,421,429)	11,045,481,781
Expenditures:						
Treasurer's Allocated Cost	(794,896)		(794,896)	(3,122,238)	-	(3,917,134)
Management Fees		(133,728)	(133,728)	(183,660,947)	-	(183,794,675)
Foreign Income Tax				(19,328,996)	-	(19,328,996)
Other Cost	(1,129,185)		(1,129,185)	(16,516,523)	-	(17,645,708)
Total Expenditures	(1,924,081)	(133,728)	(2,057,809)	(222,628,704)	-	(224,686,513)
Net Investment Income (Loss)	\$ 94,475,353	\$ 322,402	\$ 94,797,755	\$ 10,735,418,942	\$ (9,421,429)	\$ 10,820,795,268
Total Investment Income Allocated:						
General Fund	\$ 20,126,822	-	20,126,822	-	-	20,126,822
Highway Fund	5,709,887	-	5,709,887	-	-	5,709,887
University Trust Fund	486,225	-	486,225	-	-	486,225
Pension Trust Funds	19,221,420	-	19,221,420	-	-	19,221,420
Other Independent Trust Funds	2,839,590	-	2,839,590	10,735,418,942	-	10,738,258,532
Local Political Subdivisions	31,450,972	-	31,450,972	-	-	31,450,972
Licensing Boards	4,977,148	-	4,977,148	-	-	4,977,148
Other Investment Funds	241,860	-	241,860	-	-	241,860
Total Investment Income Allocated	\$ 94,475,353	\$ 322,402	\$ 94,797,755	\$ 10,735,418,942	\$ (9,421,429)	\$ 10,820,795,268

Cash Return, Fiscal Year-to-Date (Annualized) 1.006% 0.210% 0.989%

* 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, 2011

	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	\$ 1,109,356,656	242,531,592	2,110,752,819	106,227,003	131,320,070	62,296,800	8,019,522	\$ 3,770,504,442
Intra-Pool Interest Earnings	1,902,156	6,341,347	73,694	371,435	435,708	219,235	77,854	9,421,429
Income from Security Lending			15,340,041					15,340,041
Commission Recapture			105,601					105,601
Other Income			4,271,078					4,271,078
Subtotal	1,111,258,792	248,872,939	2,130,543,233	106,598,438	131,755,778	62,516,035	8,097,376	3,799,642,591
Net Unrealized Appreciation/Depreciation	(521,125,479)	(39,087,545)	7,126,774,592	346,074,973	237,321,347	100,415,358	(71,968,191)	7,158,405,055
Total Investment Income	590,133,313	189,785,394	9,257,317,825	432,673,411	369,077,125	162,931,393	(63,870,815)	10,958,047,646
Expenditures:								
Treasurer's Allocated Cost	(1,128,424)	(92,207)	(1,517,951)	(144,858)	(156,968)	(50,931)	(30,899)	(3,122,238)
Management Fees		(34,358,477)	(72,161,060)	(21,833,070)	(42,277,383)	(1,761,141)	(11,269,816)	(183,660,947)
Foreign Income Tax			(10,899,059)	(125,451)	(8,304,486)			(19,328,996)
Other Cost	(571,856)	(440,374)	(1,092,470)	(4,576,798)	(524,159)	(7,311,843)	(1,999,023)	(16,516,523)
Total Expenditures	(1,700,280)	(34,891,058)	(85,670,540)	(26,680,177)	(51,262,996)	(9,123,915)	(13,299,738)	(222,628,704)
Net Investment Income (Loss)	\$ 588,433,033	\$ 154,894,336	\$ 9,171,647,285	\$ 425,993,234	\$ 317,814,129	\$ 153,807,478	\$ (77,170,553)	\$ 10,735,418,942
Total Investment Income Allocated:								
General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Highway Fund	-	-	-	-	-	-	-	-
Highway Trust Fund	-	-	-	-	-	-	-	-
University Trust Funds	-	-	-	-	-	-	-	-
Pension Trust Funds	564,410,747	154,894,336	9,171,647,285	425,993,234	317,814,129	153,807,478	(77,170,553)	10,711,396,656
Other Independent Trust Funds	24,022,286	-	-	-	-	-	-	24,022,286
Local Political Subdivisions	-	-	-	-	-	-	-	-
Licensing Boards	-	-	-	-	-	-	-	-
Other Investment Funds	-	-	-	-	-	-	-	-
Total Investment Income Allocated	\$ 588,433,033	\$ 154,894,336	\$ 9,171,647,285	\$ 425,993,234	\$ 317,814,129	\$ 153,807,478	\$ (77,170,553)	\$ 10,735,418,942
Total Return, 12, 24, and 36 and 60 months:								
12 months	7.57%	11.13%	15.11%	9.98%	10.27%	18.81%	-13.61%	11.58%
24 months	9.32%	15.73%	33.11%	-7.37%	9.16%	N/A	N/A	18.91%
36 months	7.11%	12.40%	2.92%	-13.79%	-0.73%	N/A	N/A	3.69%
60 months	7.42%	N/A	2.93%	-2.83%	4.03%	N/A	N/A	4.50%