



NORTH CAROLINA

OFFICE OF THE TREASURER

JANET COWELL, TREASURER

August 5, 2010

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

Re: Quarterly report on Investment Funds for the period
ended June 30, 2010.

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 1.54% 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>6/30/09</u>	<u>12/31/09</u>	<u>6/30/10</u>
3-Mo. T-Bill	0.18%	0.05%	0.17%
6-Mo. T-Bill	0.34%	0.19%	0.22%

The Short-Term Investment Fund produced a fiscal year return of 1.57% for the participants. The investable balances earning income for the General Fund were \$61 million higher than one year earlier based on book value. The investable balances, which earn income for the Highway Funds, were \$18 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 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:	11.99%	-1.81%	-1.85%	3.03%

Long Term Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
LTIF Returns:	13.29%	10.43%	9.73%	6.49%

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 3/31/10	2.54%	3.83%	4.71%
As of 6/30/10	1.77%	2.93%	3.89%

- Long Term assets (based on market value) ended the quarter approximately \$466 million higher than at the end of the prior reporting period.
- Approximately \$769 million was used to pay benefits or was reallocated to other investment funds this quarter.
- The realized earnings for the fiscal year to date are \$1.4 billion.

Equity Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
EIF Returns:	14.31%	-8.40%	-8.91%	0.40%

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

Quarterly Index Returns:	S&P 500	-11.43%	DJIA	- 9.97%
	Russell 3000	-11.32%	MSCI EAFE	-13.97%

- Assets of the fund (based on market value) ended the quarter approximately \$4.1 billion lower than at the end of the prior reporting period.
- Approximately \$30 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, 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 June 30, 2010, the invested assets were valued at \$315 million after returns in the domestic and international accounts of -13.13% and -11.94% 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 June 30, 2010, \$40 million has been invested in equity; \$20 million has been invested in real estate, and commitments totaling \$67 million have been made to private equity, of which, \$41 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 June 30, 2010, the externally invested assests were valued at \$25 million after returns in the domestic and international equity accounts of -13.13% and -11.94% 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.

It is our pleasure to present this quarterly report to you and we offer additional information upon request.

Sincerely,



Janet Cowell

Attachments

cc: Pamela J. Wortham, CPA, Deputy Treasurer - Financial Operations Division
Shawn Wischmeier, Chief Investment Officer

DEPARTMENT OF STATE TREASURER
ANCILLARY INVESTMENT PROGRAMS
JUNE 30, 2010

	Escheats External Investments	OPEB External Investments	Hospital Investment Fund	Totals
Net Assets:				
Deposits in Equity Investment Fund	\$ 33,847,359	\$ 24,992,683	\$ 315,145,106	\$ 373,985,148
Deposits in Real Estate Investment Fund	12,982,365	-	-	12,982,365
Deposits in Alternative Investment Fund	34,642,114	-	-	34,642,114
Other Assets, Net of Liabilities	-	-	-	-
Total Net Assets	<u>\$ 81,471,838</u>	<u>\$ 24,992,683</u>	<u>\$ 315,145,106</u>	<u>\$ 421,609,627</u>
Participant Equity:				
General Fund	\$ -	\$ -	\$ -	\$ -
Other Investment Funds	<u>81,471,838</u>	<u>24,992,683</u>	<u>315,145,106</u>	<u>421,609,627</u>
Total Participant Equity	<u>\$ 81,471,838</u>	<u>\$ 24,992,683</u>	<u>\$ 315,145,106</u>	<u>\$ 421,609,627</u>

DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF NET ASSETS AND PARTICIPANT EQUITY - ALL POOLS AND ACCOUNTS
JUNE 30, 2010

	*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	41,600,000	-	41,600,000	-	-	41,600,000
Repurchase Agreements	1,350,000,000	-	1,350,000,000	-	-	1,350,000,000
Discount Notes/Bills	-	-	-	-	-	-
U.S. Treasury Bills/ Notes/ Bonds	4,115,586,881	-	4,115,586,881	6,296,083,405	-	10,411,670,286
U.S. Government Agency Notes/ Bonds	5,594,575,644	-	5,594,575,644	2,665,645,288	-	8,260,220,932
GNMA Certificates	-	-	-	6,366,647,681	-	6,366,647,681
Corporate Obligations	404,750,342	-	404,750,342	9,363,886,545	-	9,768,636,887
Investments in RMBS and CMBS	-	-	-	1,482,492,065	-	1,482,492,065
Investments in Equity Securities	-	-	-	9,535,084	-	9,535,084
Bond proceeds Advisory	-	533,602,868	533,602,868	-	-	533,602,868
Investments in Equity Trusts	-	-	-	31,235,332,145	-	31,235,332,145
Investments in Real Estate Trust Funds & Partnerships	-	-	-	2,902,010,423	-	2,902,010,423
Investments in Alternative Partnerships	-	-	-	3,345,301,699	-	3,345,301,699
Investments in Credit Partnerships	-	-	-	832,104,762	-	832,104,762
Investments in Inflation Partnerships	-	-	-	708,781,836	-	708,781,836
	-	-	-	-	-	-
Total Investment Securities	\$ 11,506,512,867	\$ 533,602,868	\$ 12,040,115,735	\$ 65,207,820,933	\$ -	\$ 77,247,936,668
Cash in Bank	137,988,051	-	137,988,051	-	-	137,988,051
Deposits in Short-term Investment Fund	-	-	-	812,655,865	(812,655,865)	-
Other Assets, Net of Liabilities	(117,939,566)	-	(117,939,566)	261,453,693	-	143,514,127
Total Net Assets	\$ 11,526,561,352	\$ 533,602,868	\$ 12,060,164,220	\$ 66,281,930,491	\$ (812,655,865)	\$ 77,529,438,846
Participant Equity:						
General Fund	\$ 1,549,856,060	\$ -	\$ 1,549,856,060	\$ -	\$ -	\$ 1,549,856,060
Other Funds Which Earn Interest						
for General Fund	1,438,614,565	533,602,868	1,972,217,433	-	-	1,972,217,433
Highway Fund	782,035,668	-	782,035,668	-	-	782,035,668
Highway Trust Fund	154,682,216	-	154,682,216	-	-	154,682,216
University Trust Funds	2,313,547,367	-	2,313,547,367	-	-	2,313,547,367
Pension Trust Funds	161,219,592	-	161,219,592	65,253,442,417	-	65,414,662,009
Other Independent Trust Funds	3,683,164,926	-	3,683,164,926	1,028,488,074	-	4,711,653,000
Local Political Subdivisions	598,957,426	-	598,957,426	-	-	598,957,426
Licensing Boards	31,827,667	-	31,827,667	-	-	31,827,667
Other Investment Funds	812,655,865	-	812,655,865	-	(812,655,865)	-
Total Participant Equity	\$ 11,526,561,352	\$ 533,602,868	\$ 12,060,164,220	\$ 66,281,930,491	\$ (812,655,865)	\$ 77,529,438,846
Percent of Total	14.86	0.69	15.56	85.49	-1.05	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
JUNE 30, 2010

	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	6,296,083,405	-	-	-	-	-	-	6,296,083,405
U.S. Government Agency Notes/ Bonds	2,665,645,288	-	-	-	-	-	-	2,665,645,288
GNMA Certificates	6,366,647,681	-	-	-	-	-	-	6,366,647,681
Corporate Obligations	9,265,778,353	98,108,192	-	-	-	-	-	9,363,886,545
Investments in RMBS and CMBS	-	1,482,492,065	-	-	-	-	-	1,482,492,065
Investments in Equity Securities	-	-	-	-	9,535,084	-	-	9,535,084
Bond Proceeds Advisory	-	-	-	-	-	-	-	-
Investments in Equity Trusts	-	-	31,235,332,145	-	-	-	-	31,235,332,145
Investments in Real Estate Trust Funds & Partnerships	-	-	-	2,902,010,423	-	-	-	2,902,010,423
Investments in Alternative Partnerships	-	-	-	-	3,345,301,699	-	-	3,345,301,699
Investments in Credit Partnerships	-	-	-	-	-	832,104,762	-	832,104,762
Investments in Inflation Partnerships	-	-	-	-	-	-	708,781,836	708,781,836
Total Investment Securities	\$ 24,594,154,727	\$ 1,580,600,257	\$ 31,235,332,145	\$ 2,902,010,423	\$ 3,354,836,783	\$ 832,104,762	\$ 708,781,836	\$ 65,207,820,933
Cash in Bank	-	-	-	-	-	-	-	-
Deposits in Short-term Investment Fund	222,555,901	551,892,081	6,870,465	12,513,128	5,063,959	7,793,777	5,966,554	812,655,865
Other Assets, Net of Liabilities	276,405,888	(14,952,195)	-	-	-	-	-	261,453,693
Total Net Assets	<u>\$ 25,093,116,516</u>	<u>\$ 2,117,540,143</u>	<u>\$ 31,242,202,610</u>	<u>\$ 2,914,523,551</u>	<u>\$ 3,359,900,742</u>	<u>\$ 839,898,539</u>	<u>\$ 714,748,390</u>	<u>\$ 66,281,930,491</u>
Participant Equity:								
Pension Trust Funds	24,064,628,442	2,117,540,143	31,242,202,610	2,914,523,551	3,359,900,742	839,898,539	714,748,390	65,253,442,417
Other Independent Trust Funds	1,028,488,074	-	-	-	-	-	-	1,028,488,074
Total Participant Equity	<u>\$ 25,093,116,516</u>	<u>\$ 2,117,540,143</u>	<u>\$ 31,242,202,610</u>	<u>\$ 2,914,523,551</u>	<u>\$ 3,359,900,742</u>	<u>\$ 839,898,539</u>	<u>\$ 714,748,390</u>	<u>\$ 66,281,930,491</u>
Percent of Total	37.86	3.19	47.14	4.40	5.07	1.27	1.08	100.00

DEPARTMENT OF STATE TREASURER
COMBINED STATEMENT OF OPERATIONS - ALL POOLS AND ACCOUNTS
FOR THE PERIOD ENDED JUNE 30, 2010

	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	\$ 185,180,607	\$ 335,660	\$ 185,516,267	\$ 4,091,113,867	\$ -	\$ 4,276,630,134
Intra-Pool Interest Earnings	-	-	-	14,745,961	(14,745,961)	-
Income from Security Lending	-	-	-	33,951,587	-	33,951,587
Commission Recapture	-	-	-	137,536	-	137,536
Other Income	-	-	-	13,049,660	-	13,049,660
Subtotal	185,180,607	335,660	185,516,267	4,152,998,611	(14,745,961)	4,323,768,917
Net Unrealized Appreciation/Depreciation				3,470,814,089	-	3,470,814,089
Total Investment Income	185,180,607	335,660	185,516,267	7,623,812,700	(14,745,961)	7,794,583,006
Expenditures:						
Treasurer's Allocated Cost	(1,840,062)	-	(1,840,062)	(25,142,271)	-	(26,982,333)
Management Fees	-	(56,301)	(56,301)	(263,762,997)	-	(263,819,298)
Foreign Income Tax	-	-	-	(19,503,395)	-	(19,503,395)
Other Cost	(1,244,834)	-	(1,244,834)	(7,126,912)	-	(8,371,746)
Total Expenditures	(3,084,896)	(56,301)	(3,141,197)	(315,535,575)	-	(318,676,772)
Net Investment Income (Loss)	\$ 182,095,711	\$ 279,359	\$ 182,375,070	\$ 7,308,277,125	\$ (14,745,961)	\$ 7,475,906,234
Total Investment Income Allocated:						
General Fund	\$ 37,951,185	-	37,951,185	\$ -	\$ -	\$ 37,951,185
Highway Fund	15,234,733	-	15,234,733	-	-	15,234,733
Highway Trust Fund	1,029,013	-	1,029,013	-	-	1,029,013
University Trust Funds	36,221,633	-	36,221,633	-	-	36,221,633
Pension Trust Funds	6,204,096	-	6,204,096	7,308,277,125	-	7,314,481,221
Other Independent Trust Funds	61,212,144	-	61,212,144	-	-	61,212,144
Local Political Subdivisions	8,994,148	-	8,994,148	-	-	8,994,148
Licensing Boards	502,799	-	502,799	-	-	502,799
Other Investment Funds	14,745,960	279,359	15,025,319	-	(14,745,961)	279,358
Total Investment Income Allocated	\$ 182,095,711	\$ 279,359	\$ 182,375,070	\$ 7,308,277,125	\$ (14,745,961)	\$ 7,475,906,234

Cash Return, Fiscal Year-to-Date (Annualized) 1.568% 0.160% 1.543%

* 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 JUNE 30, 2010

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	\$ 1,430,336,409	\$ 280,083,844	\$ 2,248,760,206	\$ 20,676,298	\$ 93,352,636	\$ 17,904,474	\$ -	\$ 4,091,113,867
Intra-Pool Interest Earnings	4,150,184	8,994,301	132,972	377,897	925,130	128,781	36,696	14,745,961
Income from Security Lending	-	-	33,951,587	-	-	-	-	33,951,587
Commission Recapture	-	-	137,536	-	-	-	-	137,536
Other Income	-	-	13,049,660	-	-	-	-	13,049,660
Subtotal	1,434,486,593	289,078,145	2,296,031,961	21,054,195	94,277,766	18,033,255	36,696	4,152,998,611
Net Unrealized Appreciation/Depreciation	1,621,708,488	68,337,032	1,877,321,931	(551,825,581)	397,856,893	46,932,173	10,483,153	3,470,814,089
Total Investment Income	3,056,195,081	357,415,177	4,173,353,892	(530,771,386)	492,134,659	64,965,428	10,519,849	7,623,812,700
Expenditures:								
Treasurer's Allocated Cost	(1,509,144)	(420,509)	(2,170,277)	(9,559,146)	(11,389,328)	(50,232)	(43,635)	(25,142,271)
Management Fees	-	(41,276,827)	(91,391,737)	(58,495,527)	(65,327,303)	(3,380,283)	(3,891,320)	(263,762,997)
Foreign Income Tax	-	-	(19,400,852)	(102,543)	-	-	-	(19,503,395)
Other Cost	(722,616)	(727,017)	(854,601)	(845,538)	(483,735)	(2,737,038)	(756,367)	(7,126,912)
Total Expenditures	(2,231,760)	(42,424,353)	(113,817,467)	(69,002,754)	(77,200,366)	(6,167,553)	(4,691,322)	(315,535,575)
Net Investment Income (Loss)	\$ 3,053,963,321	\$ 314,990,824	\$ 4,059,536,425	\$ (599,774,140)	\$ 414,934,293	\$ 58,797,875	\$ 5,828,527	\$ 7,308,277,125
Total Investment Income Allocated:								
General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	-
Highway Fund	-	-	-	-	-	-	-	-
Highway Trust Fund	-	-	-	-	-	-	-	-
University Trust Funds	-	-	-	-	-	-	-	-
Pension Trust Funds	2,931,532,792	314,990,824	4,059,536,425	(599,774,140)	414,934,293	58,797,875	5,828,527	7,185,846,596
Other Independent Trust Funds	122,430,529	-	-	-	-	-	-	122,430,529
Local Political Subdivisions	-	-	-	-	-	-	-	-
Licensing Boards	-	-	-	-	-	-	-	-
Other Investment Funds	-	-	-	-	-	-	-	-
Total Investment Income Allocated	\$ 3,053,963,321	\$ 314,990,824	\$ 4,059,536,425	\$ (599,774,140)	\$ 414,934,293	\$ 58,797,875	\$ 5,828,527	\$ 7,308,277,125
Total Return, 12, 24, and 36 and 60 months:								
12 months	13.29%	16.07%	14.31%	-16.74%	12.46%	N/A	N/A	11.99%
24 months	10.43%	13.71%	-8.40%	-24.44%	-5.92%	N/A	N/A	-1.81%
36 months	9.73%	10.25%	-8.91%	-14.69%	-1.61%	N/A	N/A	-1.85%
60 months	6.49%	N/A	0.40%	-2.18%	4.35%	N/A	N/A	3.03%