



## NORTH CAROLINA

OFFICE OF THE TREASURER

JANET COWELL, TREASURER

November 4, 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  
September 30, 2014.

### Commission Members:

Pursuant to statutory reporting requirements<sup>1</sup>, 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.

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<sup>1</sup> The requirements include those found in G.S. 147-68(d) & (d1), 147-69.1(e), 147-69.2(b)(10a), 147-69.3(h), 147-69.3(i), and 147-86.11(c).

Cash Management Program

The Cash Management Program, composed mostly of the Short-Term Investment Fund (“STIF”), produced a one year return of 0.42% 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>9/30/13</u>	<u>3/31/14</u>	<u>9/30/14</u>
3-Mo. T-Bill	0.008%	0.033%	0.018%
6-Mo. T-Bill	0.030%	0.056%	0.033%

The Short-Term Investment Fund produced a one year return of 0.42% for the participants. The investable balances earning income for the General Fund were \$486 million lower than one year earlier based on book value. The investable balances, which earn income for the Highway Funds, were \$82 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:	9.31%	9.54%	10.96%	9.01%

Long Term Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
LTIF Returns:	5.90%	1.29%	3.65%	5.87%

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 9/30/14	1.757%	2.490%	3.197%
As of 6/30/14	1.631%	2.531%	3.360%

- Long Term assets (based on market value) ended the quarter approximately \$2.526 billion lower than at the end of the prior reporting period.
- The realized earnings for the fiscal year to date are \$627 million.
- Approximately \$2.64 billion was used to pay benefits or was reallocated to other investment funds this quarter.

Equity Investment Fund

	<u>1 Year</u>	<u>2 Year</u>	<u>3 Year</u>	<u>5 Year</u>
EIF Returns:	10.82%	15.95%	18.06%	11.42%

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

Quarterly Index Returns:	S&P 500	1.13%	DJIA	1.29%
	Russell 3000	0.01%	MSCI EAFE	-5.88%

- Assets of the fund (based on market value) ended the quarter approximately \$3.267 billion lower than at the end of the prior reporting period.
- Approximately \$699 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 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 September 30, 2014, the invested assets were valued at \$171 million after returns in the domestic and international equity accounts of 0.51% and -4.75% 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 September 30, 2014, \$40 million has been invested in equity, of which \$41 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 \$54.5 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 September 30, 2014, the externally invested assets were valued at \$105 million after returns in the domestic and international equity accounts of 0.51% and -4.75% respectively.

Reporting Requirements for Green Managers and Funds

Pursuant to 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.

Investment Policy

Pursuant to G.S. 147-69.3(i) the following link is provided for ease of access to the current Investment Policy:

<https://www.nctreasurer.com/inv/Policies/InvestmentPolicyForNCRetirementSystems.pdf>

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

Sincerely,



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**  
**SEPTEMBER 30, 2014**

	*Cash Management Program			**Trust Funds Investment Program	Intrafund Eliminations	All Pools
	Short-term Investment Fund	Bond Proceeds Fund	Subtotal	Subtotal		Total
	Net Assets:					
Investment Securities:						
Cash Equivalents	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Certificates of Deposit	13,600,000		13,600,000	-	-	13,600,000
Repurchase Agreements	1,940,000,000		1,940,000,000	-	-	1,940,000,000
Discount Notes/Bills				-	-	-
U.S. Treasury Bills/ Notes/ Bonds	7,405,878,955		7,405,878,955	6,404,644,380	-	13,810,523,335
U.S. Government Agency Notes/ Bonds	6,591,481,008		6,591,481,008	1,246,769,595	-	7,838,250,603
GNMA Certificates				8,821,770,290	-	8,821,770,290
Corporate Obligations	54,928,713		54,928,713	9,404,547,310	-	9,459,476,023
Other Investments				9,392,089		9,392,089
Investments in RMBS and CMBS				260,373,570		260,373,570
Investments in Equity Securities				12,184,643		12,184,643
Bond proceeds Advisory		37,276,548	37,276,548			37,276,548
Investments in Equity Trusts				38,954,432,107		38,954,432,107
Investments in Real Estate Trust Funds & Partnerships				6,990,756,089		6,990,756,089
Investments in Alternative Partnerships				5,585,639,938		5,585,639,938
Investments in Credit Partnerships				4,875,615,519		4,875,615,519
Investments in Inflation Partnerships				3,064,548,737		3,064,548,737
<b>Total Investment Securities</b>	<b>\$ 16,005,888,676</b>	<b>\$ 37,276,548</b>	<b>\$ 16,043,165,224</b>	<b>\$ 85,630,674,267</b>	<b>\$ -</b>	<b>\$ 101,673,839,491</b>
Cash in Bank	200,823,850		200,823,850			200,823,850
Deposits in Short-term Investment Fund				3,927,151,364	(3,927,151,364)	
Other Assets, Net of Liabilities	30,296,961		30,296,961	181,107,943		211,404,904
<b>Total Net Assets</b>	<b>\$ 16,237,009,487</b>	<b>\$ 37,276,548</b>	<b>\$ 16,274,286,035</b>	<b>\$ 89,738,933,574</b>	<b>\$ (3,927,151,364)</b>	<b>\$ 102,086,068,245</b>
Participant Equity:						
General Fund	\$ 2,245,245,406		\$ 2,245,245,406	\$ -	\$ -	\$ 2,245,245,406
Other Funds Which Earn Interest for General Fund	1,389,202,937	37,276,548	1,426,479,485			1,426,479,485
Highway Fund	369,127,972		369,127,972			369,127,972
Highway Trust Fund	872,519,708		872,519,708			872,519,708
University Trust Funds	2,445,331,829		2,445,331,829			2,445,331,829
Pension Trust Funds	248,012,127		248,012,127	88,463,848,132		88,711,860,259
Other Independent Trust Funds	3,941,864,546		3,941,864,546	1,275,085,442		5,216,949,988
Local Political Subdivisions	767,600,692		767,600,692			767,600,692
Licensing Boards	30,952,906		30,952,906			30,952,906
Other Investment Funds	3,927,151,364		3,927,151,364		(3,927,151,364)	
<b>Total Participant Equity</b>	<b>\$ 16,237,009,487</b>	<b>\$ 37,276,548</b>	<b>\$ 16,274,286,035</b>	<b>\$ 89,738,933,574</b>	<b>\$ (3,927,151,364)</b>	<b>\$ 102,086,068,245</b>
Percent of Total	15.91	0.04	15.95	87.91	-3.86	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**  
**SEPTEMBER 30, 2014**

	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		5,810,367,579						594,276,801	6,404,644,380
U.S. Government Agency Notes/ Bonds		926,467,492	9,905,811					310,396,292	1,246,769,595
GNMA Certificates		8,821,770,290							8,821,770,290
Corporate Obligations		9,404,547,310							9,404,547,310
Other Investments	1,597,981		7,794,108						9,392,089
Investments in RMBS and CMBS			260,373,570						260,373,570
Investments in Equity Securities						12,184,643			12,184,643
Bond Proceeds Advisory									-
Investments in Equity Trusts				38,954,432,107					38,954,432,107
Investments in Real Estate Trust Funds & Partnerships					6,990,756,089				6,990,756,089
Investments in Alternative Partnerships						5,585,639,938			5,585,639,938
Investments in Credit Partnerships							4,875,615,519		4,875,615,519
Investments in Inflation Partnerships & Other Invest.								3,064,548,737	3,064,548,737
Total Investment Securities	\$ 1,597,981	24,963,152,671	\$ 278,073,489	\$ 38,954,432,107	\$ 6,990,756,089	\$ 5,597,824,581	\$ 4,875,615,519	\$ 3,969,221,830	\$ 85,630,674,267
Cash in Bank									-
Deposits in Short-term Investment Fund	1,008,575,053	148,903,927	2,769,672,384						3,927,151,364
Other Assets, Net of Liabilities	69	189,015,549	(8,281,146)					373,471	181,107,943
Total Net Assets	\$ 1,010,173,103	25,301,072,147	\$ 3,039,464,727	38,954,432,107	6,990,756,089	5,597,824,581	4,875,615,519	3,969,595,301	89,738,933,574
Participant Equity:									
Pension Trust Funds	\$ 1,010,173,103	24,025,986,705	3,039,464,727	38,954,432,107	6,990,756,089	5,597,824,581	4,875,615,519	3,969,595,301	88,463,848,132
Other Independent Trust Funds		1,275,085,442	-	-	-	-	-	-	1,275,085,442
Total Participant Equity	\$ 1,010,173,103	25,301,072,147	\$ 3,039,464,727	38,954,432,107	6,990,756,089	5,597,824,581	4,875,615,519	3,969,595,301	89,738,933,574
Percent of Total	1.13	28.19	3.39	43.41	7.79	6.24	5.43	4.42	100.00

**DEPARTMENT OF STATE TREASURER  
 ANCILLARY INVESTMENT PROGRAMS  
 SEPTEMBER 30, 2014**

	<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	\$	105,162,750	170,883,816	\$ 276,046,566
Deposits in Alternative Investment Fund	41,374,421			41,374,421
Total Net Assets	<u>\$ 41,374,421</u>	<u>\$ 105,162,750</u>	<u>\$ 170,883,816</u>	<u>\$ 317,420,987</u>

**DEPARTMENT OF STATE TREASURER  
COMBINED STATEMENT OF OPERATIONS - ALL POOLS AND ACCOUNTS  
FOR THE PERIOD ENDED SEPTEMBER 30, 2014**

	Cash Management Program			*Trust Funds	Memorandum	
	Short-term	Bond	Subtotal	Investment Program	Intrafund	Total
	Investment	Proceeds		Subtotal		
	Fund	Fund				
<b>Revenues:</b>						
Investment Income:						
Investment Earnings	\$ 16,921,426	5,229	\$ 16,926,655	\$ 1,550,628,391	\$ -	\$ 1,567,555,046
Intra-Pool Interest Earnings			-	3,234,078	(3,234,078)	-
Income from Security Lending			-	2,822,340	-	2,822,340
Commission Recapture			-	21,126	-	21,126
Other Income			-	1,128,952	-	1,128,952
Subtotal	16,921,426	5,229	16,926,655	1,557,834,887	(3,234,078)	1,571,527,464
Net Unrealized Appreciation/Depreciation				(2,408,086,805)	-	(2,408,086,805)
Total Investment Income	16,921,426	5,229	16,926,655	(850,251,918)	(3,234,078)	(836,559,341)
<b>Expenditures:</b>						
Treasurer's Allocated Cost	(132,594)		(132,594)	(1,335,151)	-	(1,467,745)
Management Fees		(4,933)	(4,933)	(26,597,767)	-	(26,602,700)
Placement Fees				-	-	-
Dividend Withholding Tax			-	(7,014,169)	-	(7,014,169)
Other Cost	(413,005)		(413,005)	(7,487,277)	-	(7,900,282)
Total Expenditures	(545,599)	(4,933)	(550,532)	(42,434,364)	-	(42,984,896)
Net Investment Income (Loss)	\$ 16,375,827	\$ 296	\$ 16,376,123	\$ (892,686,282)	\$ (3,234,078)	\$ (879,544,237)
<b>Total Investment Income Allocated:</b>						
General Fund	\$ 3,766,214		3,766,214	\$ -	\$ -	\$ 3,766,214
Highway Fund	401,512		401,512	-	-	401,512
Highway Trust Fund	916,639		916,639	-	-	916,639
University Trust Funds	2,512,293		2,512,293	-	-	2,512,293
Pension Trust Funds	471,551		471,551	(897,722,860)	-	(897,251,309)
Other Independent Trust Funds	4,227,391		4,227,391	5,036,578	-	9,263,969
Local Political Subdivisions	813,895		813,895	-	-	813,895
Licensing Boards	32,254		32,254	-	-	32,254
Other Investment Funds	3,234,078	296	3,234,374	-	(3,234,078)	296
Total Investment Income Allocated	\$ 16,375,827	\$ 296	\$ 16,376,123	\$ (892,686,282)	\$ (3,234,078)	\$ (879,544,237)
<b>Cash Return, Fiscal Year-to-Date (Annualized)</b>	0.417%	0.016%	0.416%			

\*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 SEPTEMBER 30, 2014**

	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	
<b>Revenues:</b>									
<b>Investment Income:</b>									
Investment Earnings	\$ 485	627,101,727	5,551,718	615,635,113	139,989,402	176,781,720	10,503,171	(24,934,945)	\$ 1,550,628,391
Intra-Pool Interest Earnings	887,350	210,982	2,135,746						3,234,078
Income from Security Lending				2,822,340					2,822,340
Commission Recapture				21,126					21,126
Other Income				1,128,952					1,128,952
Subtotal	887,835	627,312,709	7,687,464	619,607,531	139,989,402	176,781,720	10,503,171	(24,934,945)	1,557,834,887
Net Unrealized Appreciation/Depreciation		(513,308,851)	(1,446,069)	(1,786,024,034)	73,914,577	(121,052,961)	(35,903,120)	(24,266,347)	(2,408,086,805)
Total Investment Income	887,835	114,003,858	6,241,395	(1,166,416,503)	213,903,979	55,728,759	(25,399,949)	(49,201,292)	(850,251,918)
<b>Expenditures:</b>									
Treasurer's Allocated Cost	(11,226)	(393,761)	(25,396)	(600,628)	(104,797)	(76,129)	(70,668)	(52,546)	(1,335,151)
Management Fees				(5,884,773)	(7,967,475)	(10,444,025)	(992,340)	(1,309,154)	(26,597,767)
Placement Fees									-
Dividend Withholding Tax				(6,990,214)	(23,955)				(7,014,169)
Other Cost		(289,256)	(68,575)	(549,158)	1,830,382	(4,891,978)	(1,719,763)	(1,798,929)	(7,487,277)
Total Expenditures	(11,226)	(683,017)	(93,971)	(14,024,773)	(6,265,845)	(15,412,132)	(2,782,771)	(3,160,629)	(42,434,364)
Net Investment Income (Loss)	\$ 876,609	113,320,841	6,147,424	(1,180,441,276)	207,638,134	40,316,627	(28,182,720)	(52,361,921)	\$ (892,686,282)
<b>Total Investment Income Allocated:</b>									
General Fund	\$ -	-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	-
Highway Fund	-	-	-	-	-	-	-	-	-
Highway Trust Fund	-	-	-	-	-	-	-	-	-
University Trust Funds	-	-	-	-	-	-	-	-	-
Pension Trust Funds	876,609	108,284,263	6,147,424	(1,180,441,276)	207,638,134	40,316,627	(28,182,720)	(52,361,921)	(897,722,860)
Other Independent Trust Funds		5,036,578	-	-	-	-	-	-	5,036,578
Local Political Subdivisions	-	-	-	-	-	-	-	-	-
Licensing Boards	-	-	-	-	-	-	-	-	-
Other Investment Funds	-	-	-	-	-	-	-	-	-
Total Investment Income Allocated	\$ 876,609	113,320,841	\$ 6,147,424	\$ (1,180,441,276)	\$ 207,638,134	\$ 40,316,627	\$ (28,182,720)	\$ (52,361,921)	\$ (892,686,282)
<b>Total Return, 12, 24, and 36 and 60 months:</b>									
12 months	0.45%	5.90%	4.30%	10.82%	12.85%	15.48%	9.71%	3.94%	9.31%
24 months	N/A	1.29%	4.57%	15.95%	12.33%	11.53%	12.80%	-1.15%	9.54%
36 months	N/A	3.65%	7.90%	18.06%	10.60%	9.19%	11.40%	0.79%	10.96%
60 months	N/A	5.87%	7.81%	11.42%	8.09%	10.23%	N/A	N/A	9.01%