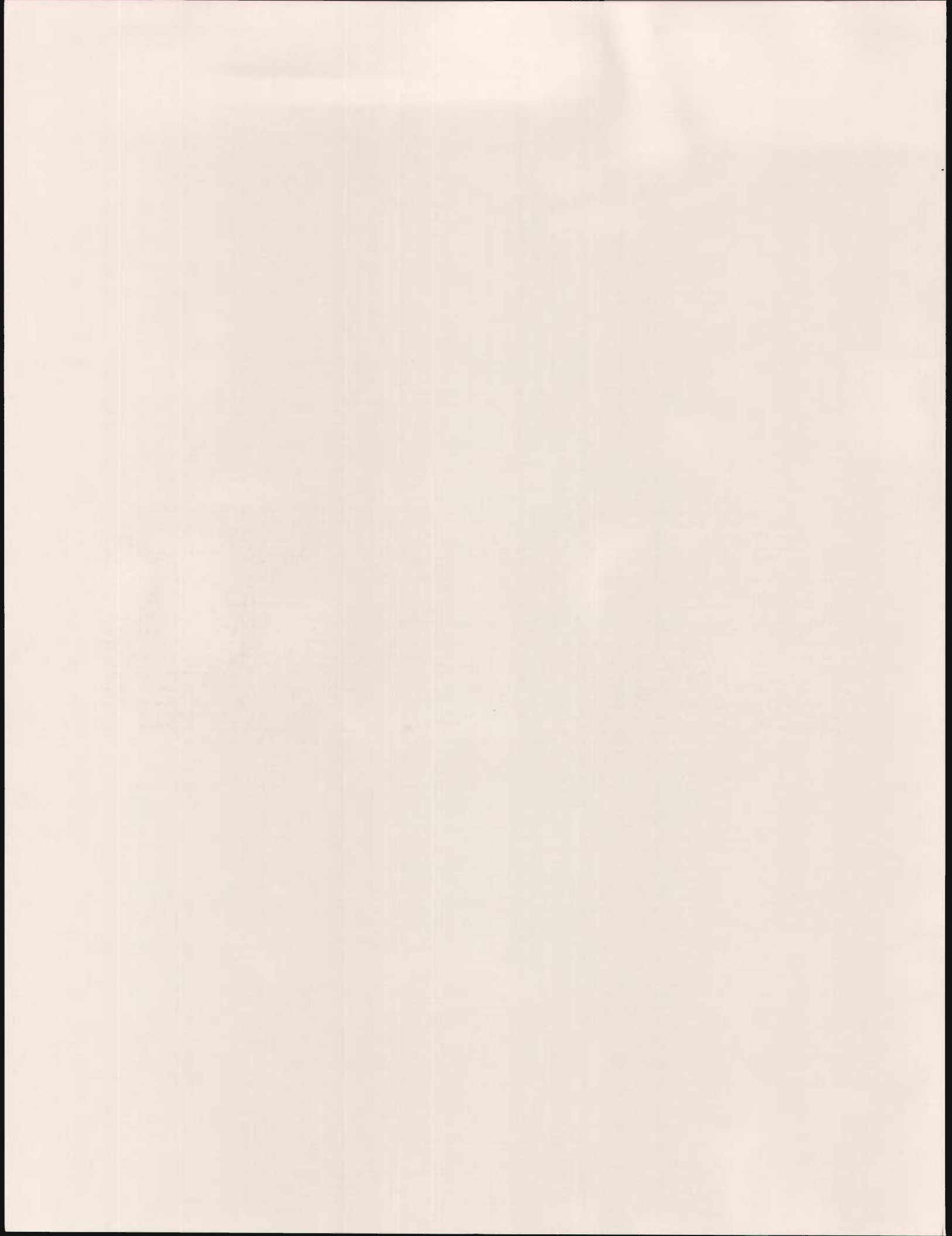

Alaska Permanent Fund Corporation

A Public Trust Investing For Alaska's Future

1984 Annual Report
and Financial Statements



Alaska Permanent Fund Corporation

Members of the Board of Trustees

Stephen C. Cowper, Chairman
Arnold G. Espe, Vice-Chairman
Norman C. Gorsuch
Robert D. Heath
Byron I. Mallott
Clyde M. Sherwood



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Officers

Fiscal Year 1984

Chairman
Vice-Chairman
Secretary and Treasurer

Stephen C. Cowper
Arnold G. Espe
David A. Rose

Fiscal Year 1985

Chairman
Vice-Chairman
Secretary and Treasurer

Arnold G. Espe
Byron I. Mallott
David A. Rose

Staff

Executive Director
David A. Rose

Chief Investment Officer
William L. Means
Investment Officers
Richard E. Alexander
Robert D. Storer

Comptroller
Peter A. Bushre
Accountants
Joyce St. Clair
Drusilla Westall

Office Manager
Alison Farnan
Secretary
Becky Mitchell
Receptionist
Barbara Nides

Research & Liaison Officer
James B. Rhode



Stephen C. Cowper
Chairman
Board of Trustees
July 1983 through July 1984

Chairman's Message

On behalf of the trustees of the Alaska Permanent Fund Corporation, I am pleased to forward the Annual Report and Financial Statements for the fiscal year ending on June 30, 1984.

While the chairman normally submits a message to accompany the annual report, it is important to emphasize that the trustees are a team, and that the policy decisions made by the board were carefully considered not only by each member, but in most instances by an extraordinarily competent group of four advisors. If history judges our decisions as correct, these advisors — and our very able staff — deserve much of the credit.

Your Permanent Fund has had quite a year. As of June 30, 1984, total assets were over \$5.5 billion. The fund earned \$529,457,000 for the year, which represents a real rate of return (after inflation) of 7.67 percent. While the fund's record in Fiscal Year 1984 was impressive by any rational standard, the ability of the trustees to maintain a high level of performance depends to a large extent on political considerations.

Unlike many government-created institutions, the Alaska Permanent Fund operates under a clear set of rules. The laws governing the fund were adopted by the 1980 legislature after three years of hearings and deliberations. Amendments which provided for "inflation-proofing" were added in 1982. The trustees believe that these laws are wise, and that they should not be changed without a full and vigorous public debate.

In the long run, the integrity of the Permanent Fund depends on a lasting consensus as to its purpose. Most Alaskans realize that a certain level of government is necessary, and that the oil revenues which provide about 90 percent of the cost of both state and municipal government will decline in a few short years.

Because of the imminent decline in Prudhoe Bay production, other forms of state and local taxation will have to be imposed. The amount of these new taxes will depend directly on the income then available from the Permanent Fund. That is why the trustees advocate a substantial increase in the rate of contribution to the fund.

A stable, moderate level of taxation will encourage the entrepreneurial activity which is necessary in a dynamic society. Given Alaska's climate and the distance to its major markets, a low tax rate is probably the most important achievable legacy of Prudhoe Bay. That legacy can still be provided, but only if the citizens of Alaska clearly demand that discipline be imposed on public spending habits.



Stephen Cowper
Chairman
Board of Trustees



The Year In Review

While Fiscal Year 1983 was characterized as a year of major organizational and policy change, Fiscal Year 1984 can be described as an “implementation” year. It was a period during which the separation of the Fund from the State Treasury became a reality; extensive internal controls were documented and implemented; new investment policies were executed; and an accounting system was firmly established.

It was the first complete year that the Fund operated as a fully self-contained and independent institution.

During the year, the Fund grew by approximately one billion dollars. It posted the highest realized real rate of return (actual return after adjusting for inflation) in its history and fulfilled its triple mandate of maintaining principal while maximizing return, conserving mineral resource revenue, and preserving the Fund as a true savings device for the citizens of Alaska.

Management

The Alaska Permanent Fund is established as an inviolate trust fund under the direction and management of a public corporation. This organization, known as the Alaska Permanent Fund Corporation, operates independently of the State Treasury to insure that state spending programs are widely separated from the savings function.

Corporate policy is formulated by six Trustees. Four are members of the public who are appointed by the Governor for staggered four-year terms. The others are the Commissioner of Revenue and one cabinet officer of the Governor’s choice.

The Trustees, except for the two cabinet officers, are citizen volunteers who are fully employed in the private sector. The cabinet members have major public responsibilities and are engaged in operating large state departments. Trustees and their fields of expertise are as follows:

<u>Members</u>	<u>Expertise</u>
Stephen C. Cowper	Legal, elected public service
Arnold G. Espe	Management, banking, accounting
Norman C. Gorsuch	Management, legal
Robert D. Heath	Corporate finance and administration, accounting
Byron I. Mallott	Corporate and government programs, personnel and funds management
Clyde M. Sherwood	Management, auditing and accounting

During this fiscal year, the membership of the Board of Trustees remained unchanged, which contrasts sharply with the complete turnover among Trustees in the prior year. However, Robert Heath, Commissioner of Revenue, resigned in June 1984. His successor, Mary A. Nordale, will assume her position in September 1984.

Stephen Cowper served as Chairman of the Trustees this past year. Arnold Espe was Vice-Chairman. The posts of Secretary and Treasurer were held by David Rose, who also served as Executive Director, responsible for all daily operations of the Fund. The Chairman and Vice-Chairman are elected annually by the Trustees.

Officers elected to serve during Fiscal Year 1985 are Arnold Espe, Chairman, and Byron Mallott, Vice-Chairman. Mr. Rose will continue to serve as Secretary and Treasurer.

Because they are not full-time employees of the Permanent Fund Corporation, the Trustees recognize a need to seek advice, to evaluate their own performance as policy-makers and to confer with others in a similar role. To this end, they have sought out peers who are responsible for overseeing other major trust funds or who are either recognized economists or financial managers.

Organization

As the result of efforts expended this past year, the Alaska Permanent Fund Corporation has a simple but functional organization which is staffed by eleven professional and clerical personnel. All duties are performed within formal, written descriptions of each position and in accordance with detailed operating procedures. Care is given to insure that the integrity of the various operations within the organization is maintained. This provides necessary internal controls to insure that all assets are properly accounted for and protected and that investment transactions are properly managed.

Finalizing The Move Toward Independence

During Fiscal Year 1983, the Trustees and staff made substantial progress in moving the Fund from the status of a ward of the State Treasury to a self-contained, independent entity. During the past year, this transition was completed. On April 1, 1984, the portfolio of home mortgages owned by the Fund and managed by the State Treasury was physically transferred to the Corporation. A comprehensive accounting and reporting system for these mortgages was devised and operational on the transfer date.

Upon conclusion of this action and in conjunction with the annual audit performed by the independent auditing firm of Price Waterhouse, the transfer of all assets, including the transfer of home mortgages, was reviewed. They concluded that the total assets reflected in the accounting records of the State Treasury pertaining to the Corporation were properly transferred to the accounting records of the Corporation.

Provision For Inflation

By law, an amount equal to the impact of inflation on principal is transferred each year to the corpus of the Fund. These funds come from current year earnings or, if earnings are insufficient, from a reserve account established for this purpose. Inflation-proofing is inherent in any well-managed trust in that it preserves the buying power of the Fund and protects it from the ravages of inflation.

Last year the Trustees resolved that it is the balance of principal at the *end* of the fiscal year, not the average balance *during* the fiscal year, that is to be protected from inflation. The propriety of this action was presented to both the Office of the Attorney General and the Legislative Budget and Audit Committee for review. The Attorney General's Office interposed no objections, and the Legislative Budget and Audit Committee adopted a resolution concurring with the Trustees' action.

Consequently, the end-of-year balance approach has been used, as it was last year, in computing the amount of funds to be added to principal to offset the impact of inflation.

Alaska Permanent Fund Earnings Used For Inflation-Proofing		
<u>Year</u>	<u>Amount</u>	<u>Inflation Rate Used</u>
FY 1984	\$150,935,000	3.22 percent
FY 1983	231,192,000	6.10 percent

Public Information Program

This year the Trustees entered the initial stage of a comprehensive public information and education program. The program is designed to ensure that the Alaskan public understands the history underlying the formation of the Fund, how it works, the importance of its maintenance as a Trust, and the financial and legal reasons for the Fund's investment policies.

The Trustees have, and will continue to pursue, the fundamental questions of: What are we going to ask the Fund to do, and how big must it be to get the job done?

During the past year, Trustees and staff have appeared before civic and educational groups and organizations, have participated in forums and debates, and testified before legislative committees.

The Fund has co-hosted and sponsored speakers and symposiums during the year to include discussions of such topics as the national economic outlook, the international overview and outlook for the petroleum industry, potential oil revenue for Alaska, development of Alaska's natural resources, the public sector and the economy, the Alberta Heritage Savings Trust Fund, the arithmetic of "front loading" the Permanent Fund, and the need for a state financial plan.

Additionally, the Fund maintains an extensive mailing list which is utilized to distribute notices of regular and special meetings, annual reports and financial statements, and monthly financial reports with a narrative analysis of each month's activity.

The Fund publishes its financial statements in newspapers in each judicial district and both financial and descriptive material in the biennial election pamphlet, mailed to each registered voter.

The Fund distributes and has available to the public, on request, brochures describing its home mortgage program and its Alaska bank certificate of deposit program. Also available is a brief two-page descriptive cameo of the Fund and projections of Fund revenues, earnings and balances.

The Fund will publish a brochure describing its history, management and investment policy along with answers to frequently asked questions. This brochure will be mailed to each Alaskan receiving a dividend check during Fiscal Year 1985.

Payments To The State Of Alaska

Alaska Permanent Fund Dividends

The Alaska Permanent Fund dividend program is not administered by the Corporation. Receipt of dividend applications, their review and ultimate payment of dividends are functions of state government and not the Alaska Permanent Fund Corporation.

This year, a portion of the Fund's earnings was turned over to the State of Alaska, Department of Revenue, in accordance with legislative appropriation and in an amount determined by a mathematical computation set forth by Alaska statutes.

Payments to the State

Payments to the State of Alaska from earnings in accord with legislated appropriation action have been as follows:

Alaska Permanent Fund Distributions of Earnings to the State of Alaska 1984-1978		
<u>Year</u>	<u>To The General Fund</u>	<u>To The Dividend Program</u>
1984	\$ —	\$155,130,000
1983	109,535,000	127,730,000*
1982	71,145,000	71,146,000
1981	27,466,000	27,466,000
1980	11,838,000	11,838,000
1979	6,547,000	—
1978	1,298,000	—

*Includes contingent liability of \$19,855,000 paid in FY84

Long range projections of future payments to the State from earnings are updated and refined periodically. Current projections for the next five years are as follows:

Projections of Future Payments to the State	
<u>Year</u>	<u>Amount</u>
1985	\$199,700,000
1986	240,600,000
1987	265,200,000
1988	288,700,000
1989	315,700,000

Legislation

Although over thirty pieces of legislation affecting the Permanent Fund itself were pending this past session, none were enacted into law.

The Trustees, as in the prior year, did not ask for or support any legislative changes, desiring to have more experience both with independence and the 1982 amendments to the Permanent Fund Act. Of legislative proposals made, two deserve special mention. One in the Senate would have amended the State Constitution to compel investing 25

percent of the Permanent Fund in Alaska. The other, in the House, would have suspended the "Prudent Investor Rule" in order to compel investment of 50 percent of the Fund in Alaska. The proposals were opposed for reasons which the Trustees have set out on numerous occasions; chiefly, that the Fund would be forced into substandard investments to meet its quotas, that it would bring a dangerous concentration of investments within a single economy, and that it would involve the Fund in state politics. Neither proposal appeared to have wide public support; the first was left under study in the first committee of referral while the second was never put to a floor vote.

Meetings

Four regular meetings, two special meetings, and eleven subcommittee worksessions were held during Fiscal Year 1984. Summary minutes are available for all regular and special meetings. The public is always encouraged to attend and is given an opportunity to address agenda items or express their convictions or concerns.

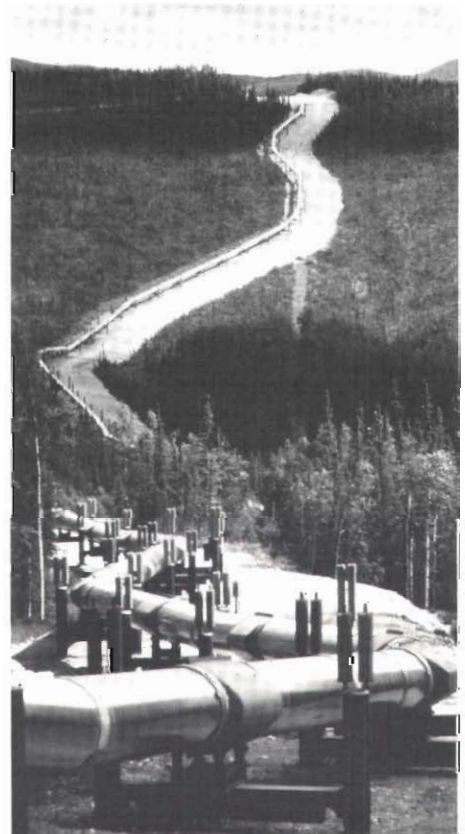
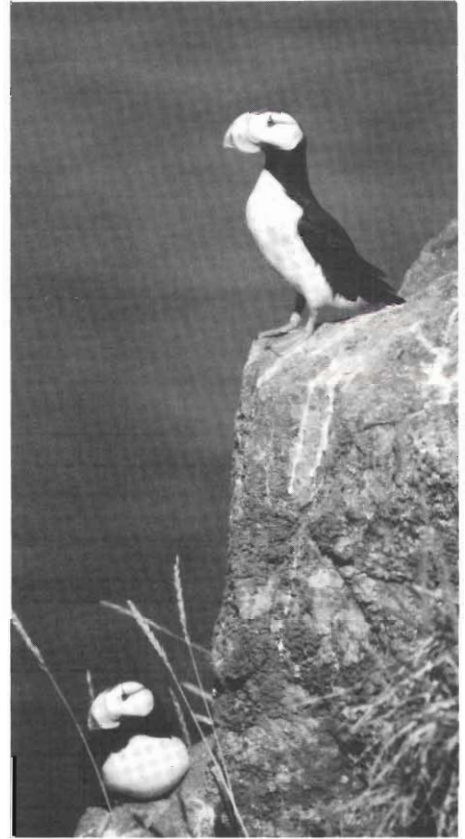
Subcommittee and worksession meetings focused on intense discussions of investment strategies and programs. Formal motions and resolutions were not made. Official corporate action was only taken at regular and special meetings.

<u>Regular Meetings</u>	<u>Special Meetings</u>
September 26-27, 1983 - Anchorage	July 22, 1983 - Anchorage
December 2, 1983 - Anchorage	April 7, 1984 - Anchorage
March 23, 1984 - Juneau	
June 22, 1984 - Fairbanks	

Audit

Price Waterhouse, independent public accountants, audited the Fund for the 1984 Fiscal Year. The auditors expressed an unqualified opinion as to the Statements of Assets, Liabilities and Fund Equity, and the related Statements of Revenues and Expenses, Changes in Financial Position, and Changes in Fund Equity. The auditors' opinion and the financial statements are included as part of this report.

In a special report to the Trustees, Price Waterhouse disclosed that the final transfer of invested funds and account balances from the State of Alaska, Department of Revenue, to the Alaska Permanent Fund Corporation, had been completed without error. In a separate report to the Trustees, they further disclosed that they had found no exceptions in their review of internal accounting controls and that the system was, in their opinion, suitable to safeguard the assets of the Permanent Fund.



Fund Performance

Performance Versus Goals

State law requires that the annual report include a comparison of the Fund's performance with its goals: 1) conservation of a portion of the state's mineral resource revenue to benefit all generations of Alaskans; 2) maintenance of safety of principal while maximizing total return; and 3) management of the Fund as a savings device to allow maximum use of disposable income for the purposes defined by law. Each goal and performance against that goal is discussed below.

Conservation of Mineral Resource Revenue

During the fiscal year, the equity of the Permanent Fund grew from \$4,375,036,000 on July 1, 1983 to a total of \$5,374,820,000 on June 30, 1984 (including reserves for future inflation and dividends).

This substantial increase of \$999,784,000 was generated primarily from contributions of revenues derived from the state's mineral resources; \$366,183,000 directly from these revenues as provided for by the 1976 constitutional amendment which created the Fund and by the Permanent Fund Act of 1980, and \$300,000,000 indirectly from mineral resource revenues through the legislative appropriation process.

Maintenance of Principal While Maximizing Total Return

All principal contributions since inception have been retained in the Fund's balance. These amounts have been preserved and enhanced by additions for inflation-proofing. An allowance has been created to show current, temporary declines in the value of stock holdings as of June 30, 1984. The realized rate of return earned during the year was 10.89 percent, which is 7.67 percent above inflation. Total net income for the year was \$529,457,000 which is greater than the prior year's earnings of \$471,125,000.

Management As A Savings Device To Allow Use Of Disposable Income

In order to preserve the Fund as a true savings device, it is necessary to protect its purchasing power from the future ravages of inflation. In accordance with law, the Trustees have retained, and placed into the principal of the Fund, an amount equal to the rate of inflation multiplied by the balance of contributed equity as of June 30, 1984. The rate of inflation utilized is the calendar year average rate of change, 1982 to 1983, of the U.S. Consumer Price Index for all urban consumers, and amounted to 3.22 percent. The amount retained was \$150,935,000. Income to be transferred from the Fund (as the result of Fiscal Year 1984 operations as prescribed by statute) to the State of Alaska, Department of Revenue, for dividends is \$155,130,000. Additional appropriations of \$11,869,000 as a supplement to 1983 dividends and \$7,986,000 for 1984 dividends were made by the Legislature to absorb the shortfall in the amount appropriated for the last fiscal year. The Fund had set aside \$19,855,000 as a contingent liability at the end of Fiscal Year 1983 in expectation that these funds would be appropriated.

Rates Of Return

This year the Fund earned the greatest realized real rate of return in its history. This was due, primarily, to high nominal returns on fixed income securities such as U.S. Government Treasury bills, bonds and notes coupled with an extremely low inflation rate. The chart below depicts the returns actually realized by the Fund (not "paper" gains or losses) since its inception.

Alaska Permanent Fund Realized Rates of Return 1984 - 1977 (Percent)			
<u>Year</u>	<u>Nominal</u>	<u>Inflation</u>	<u>Real</u>
1984	10.89	3.22	7.67
1983	12.76	6.10	6.66
1982	15.10	10.37	4.73
1981	16.00	13.52	2.48
1980	11.29	11.26	.03
1979	8.24	7.66	.58
1978	7.53	6.45	1.08
1977*	5.54	5.77	(.23)

*Four months ended June 30.

The inflation rate used consistently by the Trustees is the published U. S. Consumer Price Index previous calendar year average for all urban consumers.

Net Income

Despite a drop in market yields during the past year, the Fund posted the largest net income in its history. Although the predominant source of income was derived from earnings on fixed-income investments, it is noteworthy that there was a gain of \$476,000 on the purchase and sale of debt securities, a gain of \$1,650,000 on the purchase and sale of common stock, earnings of \$394,000 on securities loaned to financial institutions, and \$7,164,000 earned in common stock and real estate equity pools dividends. The following chart portrays the rapid growth in net income of the Fund. It may be interesting to note that, other than the petroleum industry, the Alaska Permanent Fund is the largest producer of net income in the state.

Alaska Permanent Fund Net Income 1984 - 1977	
<u>Year</u>	<u>Net Income</u>
1984	\$529,457,000
1983	471,125,000
1982	368,426,000
1981	149,867,000
1980	32,427,000
1979	7,967,000
1978	1,791,000
1977	36,000

Assets

As the result of Fiscal Year 1984 activity, Fund assets have increased by approximately one billion dollars. This increase stems from four sources:

- Mineral lease rentals, royalties, royalty sale proceeds and net profit sales in accordance with the constitutional amendment which created the Fund, and implementing State statute;
- Special appropriations made by the Legislature and paid over by the Executive Branch;
- Contributions from citizens; and
- A portion of earnings retained and added to the corpus of the Fund to offset the impact of inflation.

The following chart depicts the total assets of the Fund as of the end of each fiscal year.

Alaska Permanent Fund Total Assets 1984 - 1977	
<u>Year</u>	<u>Total Assets</u>
1984	\$5,530,799,000
1983	4,592,994,000
1982	3,301,655,000
1981	1,874,638,000
1980	502,877,000
1979	140,496,000
1978	54,997,000
1977	3,966,000

Included in the equity of the Permanent Fund is a "Reserve for Inflation and Dividends" account.

This reserve account, formally defined by statute as an "undistributed income account", is composed of residual earnings which remain with the Fund after current payments are made for dividends and inflation-proofing.

If, in any year, there are insufficient earnings to both inflation-proof and pay dividends, the shortfall is made up by drawing down the reserve. Conversely, if earnings are more than sufficient to both inflation-proof and pay dividends, the excess is placed into the reserve. As of the end of the fiscal year, there was a balance in the "Reserve for Inflation and Dividends" account in the amount of \$557,347,000. The existence of this substantial balance is attributed to the unusually high realized rates of return earned by the Fund during the past two years.

Investment Strategy And Execution

During Fiscal Year 1984, the Trustees adopted a cautious investment strategy, recognizing that it was unlikely Congress would come to grips with the problem of the federal budget deficit before the 1984 elections. It was the opinion of the Trustees that a rapidly improving economy, combined with continuing large budget deficits, would inevitably result in upward pressures on interest rates.

Accordingly, the Trustees directed the staff of the Alaska Permanent Fund, during the last three quarters of Fiscal Year 1984, to place marketable fixed-income investment emphasis on "... securities with maturities of four years or less. In addition, not more than 40 percent of the marketable fixed income portfolio shall be invested in maturities longer than four years, and no new investments shall be made in fixed income securities

with maturities in excess of ten years. . . .” As of June 30, 1984, 75.0 percent of marketable fixed-income investments mature within four years, 18.2 percent mature between four and ten years, and 6.8 percent mature over ten years.

Investments in Alaskan residential mortgages continued throughout the year with \$80 million allocated for this purpose. At year end, \$34,549,000 was invested. In addition to mortgages, the Fund held mortgage-backed securities issued by the Alaska Housing Finance Corporation. These taxable bonds, in the amount of \$23.5 million, met the investment criteria of “AA” corporate bonds as set forth in statute, had attractive yields, and offered a reasonable degree of liquidity. A new deposit program was instituted for Alaska banks, savings and loan associations, and credit unions. The Alaska Permanent Fund has agreed to purchase three-year floating rate certificates of deposit from these institutions. The rate is adjusted quarterly and is $\frac{1}{2}$ of 1 percent above the investment yield afforded by three-month U.S. Treasury bills. Substantial interest has been expressed in this program, and \$200 million has been allocated to it.

The Trustees recognize the need for diversification of investment instruments and the probability that high real rates of return on U. S. government securities will not prevail over the long run. Therefore, on March 30, 1983, the Trustees allocated 15 percent of portfolio assets to the purchase of common stock over two years. At year end, \$329,735,424 had been placed with common stock managers and an index manager. This represents 5.9 percent of total assets.

During Fiscal Year 1984, the initial investments in real estate were made. These investments involved the placement of \$7.5 million in an endowment and foundation closed-end real estate fund and the investment of \$8.0 million in an equity participating real estate mortgage. In addition, commitments were made for the purchase of \$25.0 million in common shares of an equity real estate investment trust whose owners are limited to a select group of major investors, an aggregate amount of \$52.5 million in three different diversified real estate investment pools, and \$10.0 million in an equity participating mortgage in the Cottonwood Mall located in Wasilla, Alaska.



The Year Ahead

The year ahead promises to be even more challenging and exciting than the last. While the staff deals with the exigencies of day-to-day operations, and is concerned with buying, selling, safeguarding and accounting for securities, understanding volatile markets, exploring new investment vehicles, and coping with national and international economic changes in condition and outlook, the Trustees will concentrate on formulating policy necessary to the overall long-term preservation, enhancement, management and institutionalization of the Fund. A few of the major goals for the coming year are set forth below.

Policy Goals

The Trustees will continue to press for public understanding of the Fund to include its long-term potential benefit to Alaskans and how that long-term benefit can be achieved.

They will continue to involve the public through an extensive public information and education program. Without public awareness and concern, there can be no public protection or preservation. As the Fund becomes even more successful, as it grows larger and larger, it becomes an even bigger target for those who would reach out to consume it, either by direct assault on its principal or reserves, or by legislated mandatory investment not in concert with prudent fiduciary objectives.

Operational Goals

The priority operational project for the coming year is the computerization of management and accounting data within the Fund. With assets in excess of \$5.5 billion, the Comptroller and his staff of two accountants must depart from the totally manual system now utilized. Working in close cooperation with the State of Alaska, Department of Administration, the staff is in the final stages of acquiring specialized software and micro-computers. A major goal for the coming year is the satisfactory installation and use of an automated system.

A second operational project involves performance analysis — a portrayal in easy-to-understand terms of just how well the Fund is doing its job in comparison to national indices of investment performance. Performance analysis places policies, strategies and execution under the microscope. It calls for the clear statement of assumptions, consistency of measurement, and comparisons over varying lengths of time. The above-mentioned computerization project will provide a much needed internal data base of underlying information which will be supplemented by reputable, third-party sources providing national indices against which performance is compared.

Economic Outlook

The economic outlook for the second half of 1984 will be dominated by the Presidential election and the prospect of continuing massive federal budget deficits. Calendar year 1985 raises a number of significant questions for which we have no answers at this time. Undoubtedly, the most important question is whether the President and the new Congress will demonstrate the political will to substantially reduce future federal budget deficits. Significant movement to reduce these deficits would carry with it the prospect, over time, of substantially lower interest rates. If, however, the measures adopted were to threaten a recession, the Federal Reserve Bank might feel compelled to bring rates down quickly. A rapid decline could well produce a whole new spate of problems.

A rapid move to lower interest rates would likely result in reduced willingness on the part of foreign investors to hold assets denominated in U.S. dollars. A precipitous decline of the dollar might well reignite inflation as imported goods rose in cost, and businesses in this country raised prices free from foreign competition. Eventually the Federal Reserve Bank would have no choice but to raise interest rates substantially again in order to protect the international value of the dollar.

Substantial progress has been made against inflation. If the new Congress and the President can move harmoniously to put a rational plan in place to eliminate, or at least substantially reduce, this country's budget deficits, the prospects are excellent for a period of unparalleled economic growth, substantially lower interest rates, and minimal inflation. If, however, Congress and the President are perceived as resorting to ineffective half-measures and engaging in partisan acrimony, it is all too likely that foreign investors will eventually lose confidence in the U.S. dollar, and this country will experience yet another round of economic turmoil.



Alaska Permanent Fund Corporation

Financial Statements
June 30, 1984 and 1983





101 WEST BENSON BOULEVARD
ANCHORAGE, ALASKA 99503
907 563-4444

August 22, 1984

To the Board of Trustees
Alaska Permanent Fund Corporation

In our opinion, the accompanying statements of assets, liabilities and fund equity and the related statements of revenue and expenses and of changes in fund equity and financial position present fairly the financial position of the Alaska Permanent Fund Corporation at June 30, 1984 and 1983, and the results of its operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Price Waterhouse

Alaska Permanent Fund Corporation

Statement of Assets, Liabilities and Fund Equity

	<u>June 30,</u>	
	<u>1984</u>	<u>1983</u>
ASSETS		
Cash	\$ 259,000	\$ 183,000
Receivables and prepaid expenses	171,250,000	152,265,000
Investments:		
Marketable debt securities -		
Repurchase agreements	124,600,000	18,800,000
Short-term issues	329,605,000	612,557,000
Intermediate and long-term issues	<u>4,564,080,000</u>	<u>3,727,503,000</u>
Total marketable debt securities	5,018,285,000	4,358,860,000
Common stock, net of valuation allowance	290,835,000	
Real estate equity pools	7,500,000	
Participating real estate mortgage	8,000,000	
Conventional mortgages	34,549,000	31,521,000
Alaska certificates of deposit		<u>50,000,000</u>
Total investments	5,359,169,000	4,440,381,000
Property and equipment, net of accumulated depreciation	<u>121,000</u>	<u>165,000</u>
Total assets	<u>\$5,530,799,000</u>	<u>\$4,592,994,000</u>
LIABILITIES		
Accounts payable	\$ 849,000	\$ 548,000
Income distributable to the State of Alaska	<u>155,130,000</u>	<u>217,410,000</u>
Total liabilities	<u>155,979,000</u>	<u>217,958,000</u>
EQUITY		
Contributed equity	4,838,344,000	4,021,226,000
Reserve for inflation and dividends	557,347,000	
Undistributed income		353,810,000
Unrealized loss on common stock	<u>(20,871,000)</u>	
Total equity	<u>5,374,820,000</u>	<u>4,375,036,000</u>
Total liabilities and equity	<u>\$5,530,799,000</u>	<u>\$4,592,994,000</u>

See accompanying notes to financial statements

Alaska Permanent Fund Corporation

Statement of Revenues and Expenses

	<u>Year Ended June 30,</u>	
	<u>1984</u>	<u>1983</u>
Revenues:		
Interest -		
Investments	\$522,508,000	\$472,178,000
Loaned securities	<u>394,000</u>	<u>22,000</u>
Total interest	<u>522,902,000</u>	<u>472,200,000</u>
Dividends	<u>7,164,000</u>	
Realized gains on the sale of -		
Marketable debt securities	476,000	64,000
Common stock	<u>1,650,000</u>	<u> </u>
Total gains	<u>2,126,000</u>	<u>64,000</u>
Gross revenues	<u>532,192,000</u>	<u>472,264,000</u>
Expenses:		
Salaries and benefits	699,000	462,000
Travel	83,000	67,000
Trustee honoraria	32,000	23,000
Communications	156,000	33,000
Consulting and studies	127,000	47,000
Office rent	89,000	34,000
Custody and safekeeping fees	606,000	310,000
Common stock and real estate management fees	768,000	
Legal and audit	48,000	84,000
Depreciation	51,000	12,000
Other	<u>76,000</u>	<u>67,000</u>
Total operating expenses	<u>2,735,000</u>	<u>1,139,000</u>
Net income	<u>\$529,457,000</u>	<u>\$471,125,000</u>

See accompanying notes to financial statements

Alaska Permanent Fund Corporation

Statement of Changes in Fund Equity For The Years Ended June 30, 1984 and 1983

	<u>Total</u>	<u>Contributed Equity</u>	<u>Reserve for Inflation and Dividends</u>	<u>Unrealized Loss On Common Stock</u>	<u>Undistributed Income</u>
Balance, June 30, 1982	\$3,212,836,000	\$2,969,077,000			\$243,759,000
Appropriations from the State	400,000,000	400,000,000			
Dedicated state revenues	420,957,000	420,957,000			
Net income from operations	471,125,000				471,125,000
Provision for 1983 dividends	(64,111,000)				(64,111,000)
Provision for distributions to the state general fund	(65,771,000)				(65,771,000)
Provision for 1983 inflation	(231,192,000)	231,192,000			(231,192,000)
Balance, June 30, 1983	4,375,036,000	4,021,226,000			353,810,000
Appropriations from the State	300,000,000	300,000,000			
Dedicated state revenues	366,183,000	366,183,000			
Net income from operations	529,457,000				529,457,000
Provision for 1983 dividend supplement	(11,869,000)				(11,869,000)
Provision for 1984 dividends	(163,116,000)				(163,116,000)
Provision for 1984 inflation	150,935,000	150,935,000			(150,935,000)
Allowance for unrealized loss on common stock	(20,871,000)			\$(20,871,000)	
Provision for future inflation and dividends			\$557,347,000		(557,347,000)
Balance, June 30, 1984	<u>\$5,374,820,000</u>	<u>\$4,838,344,000</u>	<u>\$557,347,000</u>	<u>\$(20,871,000)</u>	<u>\$</u>

See accompanying notes to financial statements

Alaska Permanent Fund Corporation

Statement of Changes in Financial Position

	<u>Year Ended June 30,</u>	
FUNDS WERE PROVIDED BY:	<u>1984</u>	<u>1983</u>
Investment operations -		
Net income	\$ 529,457,000	\$ 471,125,000
Items not affecting funds -		
Amortization	(416,000)	(825,000)
Depreciation	51,000	12,000
Increase in receivables & prepaid expenses	(18,985,000)	(27,370,000)
Increase in accounts payable	<u>301,000</u>	<u>548,000</u>
Funds provided by operations	<u>510,408,000</u>	<u>443,490,000</u>
Sales -		
Marketable debt securities	1,648,273,000	2,255,919,000
Common stock	<u>53,758,000</u>	
Total sales	1,702,031,000	2,255,919,000
Maturities of debt obligations	1,252,920,000	1,647,650,000
Conventional mortgage repayments	7,653,000	3,840,000
Redemption of Alaska certificates of deposit	50,000,000	3,000,000
Decrease in value of common stock	20,871,000	
Contributions from the State of Alaska	<u>666,183,000</u>	<u>820,957,000</u>
Total funds provided	<u>4,210,066,000</u>	<u>5,174,856,000</u>
FUNDS WERE USED FOR:		
Purchases -		
Marketable debt securities	3,454,402,000	5,140,755,000
Common stock	365,464,000	
Real estate equity pools	7,500,000	
Participating real estate mortgage	8,000,000	
Conventional mortgages	10,681,000	10,918,000
Alaska certificates of deposit		3,000,000
Equipment	<u>7,000</u>	<u>177,000</u>
Total purchases	3,846,054,000	5,154,850,000
Allowance for unrealized loss on common stock	20,871,000	
Payments to the State of Alaska	<u>237,265,000</u>	<u>1,291,000</u>
Total funds used	<u>4,104,190,000</u>	<u>5,156,141,000</u>
Net change in funds	<u>\$ 105,876,000</u>	<u>\$ 18,715,000</u>
SUMMARY OF CHANGES:		
Increase in cash	\$ 76,000	\$ 115,000
Increase in repurchase agreements	<u>105,800,000</u>	<u>18,600,000</u>
Net change in funds	<u>\$ 105,876,000</u>	<u>\$ 18,715,000</u>

See accompanying notes to financial statements

Alaska Permanent Fund Corporation

Notes to the Financial Statements June 30, 1984 and 1983

Note 1 - Entity:

The Constitution of the State of Alaska was amended by public referendum in 1976 to provide for the automatic segregation of a portion of certain natural resource revenues which are dedicated to the Permanent Fund. The principal of the Permanent Fund is to be invested in perpetuity. In 1980, the State Legislature created the Alaska Permanent Fund Corporation (the "Corporation"), a public corporation separate from the agencies of state government and governed by a Board of Trustees (the "Trustees"), to manage the investments of the Permanent Fund. In 1982, the Legislature amended the law to provide that a portion of the annual earnings would be made available to the State for the payment of dividends and that a portion would be contributed to the principal of the Permanent Fund sufficient to offset the impact of inflation. The balance was to be retained by the Corporation in an undistributed income account.

Note 2 - Significant Accounting Policies:

Contributions

Contributions by operation of statute are recorded when they become due from the State, *i.e.*, when certain revenues are received by the State Department of Natural Resources.

Contributions by appropriation are recorded when they are received.

Depreciation

Furniture and equipment are depreciated on a straight-line basis over a three-year useful life. Other property is depreciated on a straight-line basis over a five-year useful life.

Dividend Appropriations

Current law directs that one-half of a five-year moving average of the net income of the Corporation be made available for payment to the Dividend Fund each year.

Funds

For purposes of the Statement of Changes in Financial Position, the term "Funds" has been defined as cash and repurchase agreements.

Inflation Impact

The impact of inflation is measured by the 1983 United States Consumer Price Index calendar year average for all urban consumers applied against the balance of contributed equity at the end of the fiscal year.

Interest Income

Interest income on all securities is accrued monthly as earned.

Interest income is shown net of amortization of premiums and accretion of discounts.

Investments

In accordance with the American Institute of Certified Public Accountants' Statement of Position of the Accounting Standards Division No. 78-10, investments in the aggregate are valued as follows:

<u>Type</u>	<u>Basis</u>
Marketable debt securities	Cost adjusted for amortization of premiums and accretion of discounts
Common stock	Lower of cost or market value
Real estate equity pools	Market value
Participating real estate mortgages	Market value
Conventional mortgages	Cost
Alaska certificates of deposit	Cost

Realized gains or losses on the sale of investments are determined by specific identification.

Restatement of Prior Year

Prior year balances have been restated to conform with a change in reporting format. This restatement has had no effect on previously reported earnings.

Undistributed Income

Net earnings are credited to the undistributed income account at the end of the fiscal year. Earnings attributed to the investment of undistributed income are based upon the balance at the beginning of the fiscal year.

Note 3 - Marketable Debt Securities:

The estimated market values of investment securities at June 30, 1984 and 1983 are as follows:

	<u>June 30,</u>	
	<u>1984</u>	<u>1983</u>
Repurchase agreements	\$ 124,600,000	\$ 18,800,000
Short-term issues	332,057,000	639,236,000
Intermediate and long-term issues	<u>4,245,140,000</u>	<u>3,737,790,000</u>
	<u>\$4,701,797,000</u>	<u>\$4,395,826,000</u>

All of the Corporation's investment securities are held by commercial lending institutions pursuant to custodial agreements.

Note 4 - Common Stock:

At June 30, 1984, the aggregate cost of the investment in common stock was \$311,706,000. To reduce the portfolio to its aggregate market value at June 30, 1984, a valuation allowance of \$20,871,000 was established by a charge to equity. At August 17, 1984, the aggregate market value of the June 30, 1984 portfolio was \$310,026,000.

Note 5 - Real Estate Equity Pools:

At June 30, 1984, the investment in real estate equity pools was valued at market, which approximates cost. Future adjustments to market value will be based upon independent appraisals of the properties which constitute the pools.

Note 6 - Participating Real Estate Mortgage:

The investment in participating real estate mortgages conveys an undivided interest in real property acquired in connection with a loan made on and collateralized by certain real estate. At June 30, 1984, the investment was valued at market value which approximates cost. Future adjustments to market value will be determined by the combined total of (i) an annual appraisal of the real property, and (ii) the difference between the present value of the mortgage and the outstanding principal balance of the note at year end. Terms of the mortgage note provide for interest at 10.5 percent per annum. In addition, the Corporation will participate to the extent of its percentage of ownership in future net cash flow derived from leasing the property. The total amount of interest and net cash flow each year is limited to the maximum rate for interest allowed under applicable state (Texas) or federal law.

Note 7 - Income Distributable to the State of Alaska:

Income distributable to the State of Alaska is that portion of net income for the year ended June 30, 1984 which has been appropriated by the Legislature for the payment of dividends. Income distributable to the State for the year ended June 30, 1983 is that portion which has been appropriated for the payment of dividends for that year, and an amount payable to the state general fund due under a special one-time transition rule which accompanied the 1982 amendments. The activity for the years ended June 30, 1984 and 1983 is summarized as follows:

	<u>Total</u>	<u>Dividend Fund</u>	<u>General Fund</u>
Balance due, June 30, 1982	\$ 88,819,000	\$ 44,410,000	\$ 44,409,000
Add: 1983 appropriation and transition rule liability	<u>217,410,000</u>	<u>107,875,000</u>	<u>109,535,000</u>
	<u>306,229,000</u>	<u>152,285,000</u>	<u>153,944,000</u>
Less: Cash transfers— Applicable to 1982	(1,291,000)	(646,000)	(645,000)
Transition rule adjustment	<u>(87,528,000)</u>	<u>(43,764,000)</u>	<u>(43,764,000)</u>
	<u>(88,819,000)</u>	<u>(44,410,000)</u>	<u>(44,409,000)</u>
Balance due, June 30, 1983	<u>217,410,000</u>	<u>107,875,000</u>	<u>109,535,000</u>
Add: 1983 supplemental appropriation	11,869,000	11,869,000	
1984 appropriations	<u>163,116,000</u>	<u>163,116,000</u>	
	<u>174,985,000</u>	<u>174,985,000</u>	
Less: Cash transfers— Applicable to 1983	(229,279,000)	(119,744,000)	(109,535,000)
Applicable to 1984	<u>(7,986,000)</u>	<u>(7,986,000)</u>	
	<u>(237,265,000)</u>	<u>(127,730,000)</u>	<u>(109,535,000)</u>
Balance due, June 30, 1984	<u>\$155,130,000</u>	<u>\$155,130,000</u>	<u>\$ _____</u>

Note 8 - Contributed Equity:

The principal balances of the Alaska Permanent Fund at June 30, 1984 and 1983 are as follows:

	<u>June 30,</u>	
	<u>1984</u>	<u>1983</u>
Dedicated state revenues	\$2,056,217,000	\$1,690,034,000
Appropriations from the State	2,400,000,000	2,100,000,000
Cumulative provision for inflation	<u>382,127,000</u>	<u>231,192,000</u>
	<u>\$4,838,344,000</u>	<u>\$4,021,226,000</u>

In 1980, the State Legislature appropriated \$900,000,000 from general fund revenues to the Permanent Fund. This appropriation has been paid in full. In 1981, the Legislature appropriated an additional \$1,800,000,000 from general fund revenues to the Permanent Fund. This appropriation bill directs the Commissioner of Revenue to make monthly deposits of general fund operating surplus until the balance is reached. As of June 30, 1984, \$1,500,000,000 (June 30, 1983, \$1,200,000,000) of this appropriation had been deposited in the Permanent Fund.

Note 9 - Reserve for Inflation and Dividends:

The Trustees of the Permanent Fund have designated the balance of the undistributed income account at June 30, 1984, as reserved for future inflation impact and dividend payments. Although the State Legislature could legally appropriate this amount for other purposes, in the opinion of the Trustees, this designation is in accordance with the stated purpose of undistributed income, *i.e.*, to provide a reserve for the current statutory uses of Corporation income against the possibility of future declines in that income. Such a reserve is intended to enable the Corporation to fully offset the impact of inflation and still maintain a constant level of dividends in years when Permanent Fund earnings are not enough to do both.

Note 10 - Income By Source:

Interest income was provided by the following investments during the fiscal years ended June 30, 1984 and 1983:

	<u>1984</u>	<u>1983</u>
Securities purchased under agreements to resell	\$ 14,766,000	\$ 5,310,000
Commercial paper	2,280,000	
Bankers acceptances	819,000	20,270,000
Certificates of deposit	14,418,000	59,621,000
U.S. Treasury bills	19,353,000	109,382,000
U.S. Treasury notes and bonds	461,595,000	270,270,000
Federal agency securities		979,000
Corporate bonds	2,532,000	1,740,000
Money Market accounts	1,755,000	12,000
Conventional mortgages	4,831,000	4,371,000
Participating real estate mortgage	138,000	
Leases	<u>21,000</u>	<u>223,000</u>
	<u>\$522,508,000</u>	<u>\$472,178,000</u>

Dividend income was provided by the following investments during the fiscal year ended June 30, 1984:

Common stock	\$ 6,779,000
Real estate equity pools	<u>385,000</u>
	<u>\$ 7,164,000</u>



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