





**A Public Trust**  
**Investing For Alaska's Future**





## 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 ended June 30, 1985.

It has been a distinct pleasure to serve as chairman of the board of trustees this past year. Investment policy was carefully constructed, extensively deliberated, and conservatively applied. The trustees worked together as a team and, along with a very able staff, were able to produce excellent operating results.

As of June 30, 1985, total assets exceeded \$6.7 billion, an increase of \$1,192,053,000 in a single year.

Net income from interest, dividends, gains on the sale of securities, and fees from the securities lending program totaled \$657.8 million, a 24% increase over last year's net income of \$529.5 million. In addition, unrealized gains that have not been recognized as income of the current period amounted to \$373.7 million.

For the fourth consecutive year, your Fund exceeded the long-term goal of a 3% realized real rate of return. The return this year, after inflation, was an impressive 7.35%.

New ground was broken this year with the inception of new programs. The Alaska Bank Certificates of Deposit Program invests funds in certificates issued by Alaskan banks. Up to \$200 million is made available, at competitive market rates, for use by banks in making loans to Alaskans. A second program, in which the Fund makes geographically-diversified investments in shopping centers, office buildings and other improved real estate, commenced following detailed planning and the establishment of policy guidelines.

Also this year, the trustees placed increased emphasis on public information and accountability. A variety of informative vehicles have been designed to keep Alaskans aware of Fund activities. We believe in holding ourselves publicly accountable for policy and performance, and welcome your comments or questions.



As I conclude my term as chairman, I wish to extend my thanks for the concern, the support, and the understanding of Alaskans throughout our state. Together we have achieved the goal of establishing and operating the Fund for the benefit of all Alaskans — of today and of the future.

A handwritten signature in cursive script that reads "A. G. Espe".

Arnold G. Espe  
Chairman  
Board of Trustees  
1984-85

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## ORGANIZATION

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### BOARD OF TRUSTEES

Arnold G. Espe  
Byron I. Mallott  
Hugh Malone  
Mary A. Nordale  
Emil Notti  
Clyde M. Sherwood

### OFFICERS

#### Fiscal 1985

Arnold G. Espe, Chairman  
Byron I. Mallott, Vice-Chairman  
David A. Rose, Secretary/Treasurer

#### Fiscal 1986

Byron I. Mallott, Chairman  
Clyde M. Sherwood, Vice-Chairman  
David A. Rose, Secretary/Treasurer

### 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

Ellen Phipps

#### Research & Liaison Officer

Jim Kelly

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## FUND PERFORMANCE

### Statutory Goals Are Being Met: Portion of the Oil Wealth Is Saved, Produces Income

AS 37.13.020 sets out three goals for the Alaska Permanent Fund Corporation: (1) save a portion of the wealth created by development of the state's non-renewable natural resources to benefit all generations of Alaskans; (2) protect those savings from loss of value; and (3) invest those savings to produce income for uses provided by law.

The goals are being met. Certainly in terms of petroleum revenues, it is clear that a significant portion of the state's one-time-only resource wealth is being conserved, protected and invested — with impressive results.

#### Conservation of Mineral Resource Revenue

Since inception, the Permanent Fund has received 23% of total state petroleum revenues, and 20% of what otherwise would have been total General Fund Unrestricted Revenues. This relatively high rate of savings has been accomplished by a combination of constitutional dedication (25% of oil royalties and bonuses) and special legislative appropriations.

amendment to the state Constitution and the Permanent Fund Act of 1980;

- \$300 million as the final payment of a special legislative appropriation outstanding since 1981;

- \$234.6 million transferred from earnings to principal for the purpose of inflation-proofing;

- \$205.9 million from earnings to the undistributed income account as required by AS 37.13.145; and

- \$20.9 million by the recovery of an unrealized loss in common stock.

#### Protection of Principal

Since inception, all contributions to principal have been retained in the Permanent Fund. There has been no loss of principal. In addition, inflation-proofing has provided the principal with protection from loss of value since 1982.

In fiscal 1985, in accordance with law, the trustees have retained, and placed in the principal of the Fund, an amount equal to the rate of inflation, multiplied

#### WHAT PART OF REVENUES GOES TO THE PERMANENT FUND?

FISCAL YEARS 1977-1985

(in millions)

General Fund Unrestricted Revenues	Petroleum Revenues (Net of Permanent Fund)	Permanent Fund Special Appropriations	Permanent Fund Dedicated Revenues
<b>\$23,358.7</b>	<b>\$19,468.3</b>	<b>\$2,700.0</b>	<b>\$2,409.6</b>

During fiscal 1985, the equity of the Permanent Fund grew 21% from \$5,374.8 million on June 30, 1984 to a total of \$6,504.2 million on June 30, 1985. This substantial increase of \$1,129.4 million was generated from contributions as follows:

- \$368 million directly from the dedication of revenues as required by the 1976

by the balance of contributed equity as of June 30, 1985.

#### Production of Income

In addition to saving money and keeping it safe, the Corporation has a third mandate: produce income for uses provided by law. Here, the trustees attempt to maximize total return on the Fund's investment, but their primary concern is maintaining safety of principal.

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## HISTORY AND MANAGEMENT

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# The Permanent Fund: Alaska's Savings Account

The Alaska Permanent Fund is a savings account, restricted as to usage, which belongs to all the people of Alaska. It was created by public referendum in 1976 when the voters, by a margin of 75,588 to 38,518, approved the following amendment to Article IX of the Constitution of the State of Alaska:

*Section 15. ALASKA PERMANENT FUND. At least twenty-five percent of all mineral lease rentals, royalties, royalty share proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments. All income from the permanent fund shall be deposited in the general fund unless otherwise provided by law [Effective February 21, 1977].*

The Fund is established as an inviolate trust. This means the principal of the Fund is to be invested in perpetuity. The beneficiaries of the trust are all present and future generations of Alaskans.

To manage the investments of the Permanent Fund, the legislature, in 1980, created the Alaska Permanent Fund Corporation as a public corporation, separate from state government. It was the intent of the legislature to establish a management system for the Fund which would be protected from political influences but, at the same time, responsive to changes in state policy and accountable to the people through their elected officials.

Consequently, within the statutory framework, corporate policy is formulated independently by a board of six trustees. Four are members of the public with recognized competence and wide experience in finance, investments, or other business management-related fields. They are appointed by the governor for four-year terms. The other members are the com-

missioner of the Department of Revenue and one cabinet officer of the governor's choice.

The trustees, except for the two cabinet members, are citizen volunteers. They are not paid salaries, though they do receive an honorarium of \$400 for each day spent at a meeting of the board or at a public meeting as a representative of the board.

During the fiscal year, there were two changes to the membership of the board of trustees. Steve Cowper, a Fairbanks lawyer and former state legislator who served as last year's chairman, resigned in January. He was succeeded by Hugh Malone, a Kenai land surveyor and also a former state legislator. Robert Heath, the commissioner of the Department of Revenue who resigned in June 1984, was succeeded by Mary Nordale in September.

In July 1985, upon the resignation of Norman Gorsuch, attorney general, Emil Notti, commissioner of the Department of Community & Regional Affairs, was appointed to the board.

Arnold Espe, an Anchorage banker who was appointed to the board in September 1982 and re-appointed in June 1985, served as chairman this year. Byron I. Mallott, chief executive officer for a Juneau-based Native corporation, was the vice-chairman. The chairman and the vice-chairman are elected annually by the trustees.

Officers elected to serve in fiscal 1986 are Byron Mallott, chairman, and Clyde Sherwood, a senior partner in an Anchorage accounting firm, vice-chairman.

David Rose, executive director of the Alaska Permanent Fund Corporation, has served as secretary/treasurer continuously since December 1982.

Day-to-day operations are carried out by the executive director and a staff of ten professional and clerical personnel. Equity and real estate advisors and bank custodians augment staff on a contractual basis.

## Undistributed Income Is Part of the Permanent Fund

The Permanent Fund is made up of two parts: principal and undistributed income. As of June 30, 1985:

The Principal of the Fund is:	\$5.7 billion
Undistributed Income is:	\$763.3 million

The principal of the Fund includes (1) the oil royalties deposited by constitutional dedication; (2) extra money deposited by legislative appropriation; and (3) income of the Fund which has been transferred to principal to inflation-proof the Fund. Expenditure of the principal is constitutionally prohibited.

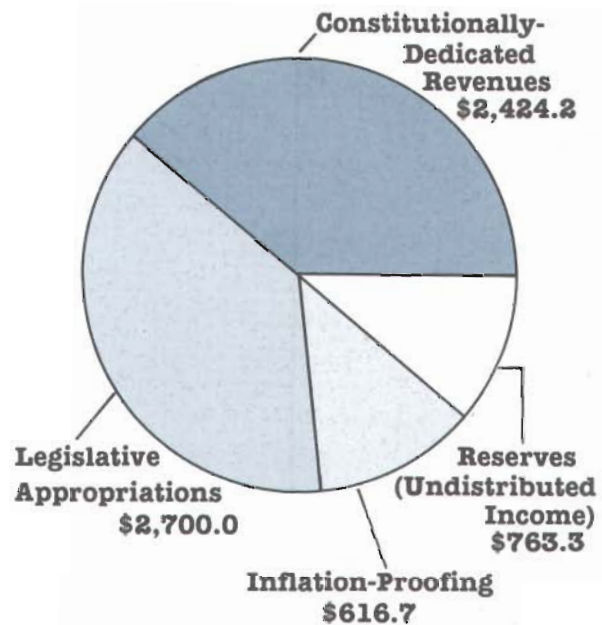
Undistributed income is all other net income — current and prior years' — which has not been paid out as dividends or transferred to principal for inflation-proofing. These accumulated earnings now represent over 11% of the total assets of the Permanent Fund. No constitutional prohibition is placed on their expenditure.

The trustees have designated the undistributed income as "reserves" to be used in future years when either poor earnings or high inflation leave insufficient funds to pay the full portion of dividends and inflation-proofing (the two currently authorized uses for Fund earnings). In this way, the reserves cushion the Fund against sharp fluctuations in income or monetary conditions.

There are two main reasons why the reserves have burgeoned in the recent past — and also two reasons why it is unlikely that this growth will continue into the future.

First, an unusually large percentage of earnings have been held back from distribution by a provision in the enabling act which calls for income to be paid out on the basis of a five-year average. In the early years of the Fund, as assets and income have increased dramatically each

**TOTAL EQUITY: \$6,504.2**  
(in millions)



This chart shows where the money in the Permanent Fund has come from.

year, this provision has had the arithmetic effect of limiting the distribution of income. As the Fund matures, however, the percentage of net income available for distribution will increase.

Second, earnings have been extraordinarily high in the past four years. In each of these years, the Fund's real rate of return — *i.e.*, return after inflation — has been substantially above the target of 3%. A sense of history indicates that such high returns are not sustainable. In fact, the real rate of return for the Fund since inception in 1977 has been 3.8%.

As large as the reserves are, however, they may not be large enough. Current projections, which assume a long-term rate of return for the Fund of 9% and average inflation of 6%, indicate that all of the existing reserves will be needed over the next 15 years to meet future dividend and inflation-proofing needs.

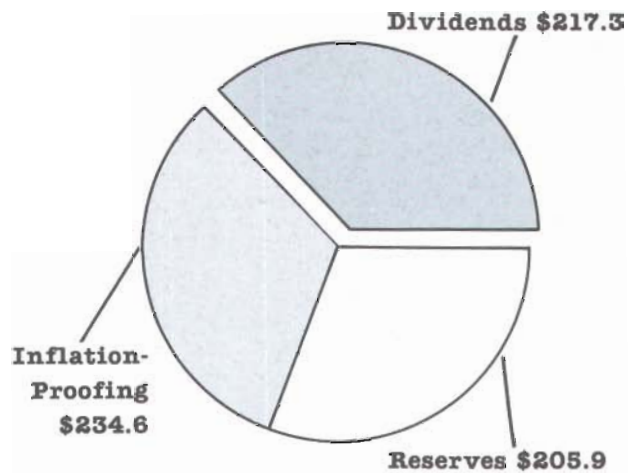
In fiscal 1985, net income totaled \$657.8 million. This represents a 24% increase over fiscal 1984's net income of \$529.5 million. Net income was distributed this year as follows:

- \$217.3 million for dividends;
- \$234.6 million for inflation-proofing;
- \$205.9 million for reserves for future dividends and inflation.

Since inception, the Permanent Fund has produced \$2,218.9 million in net income. As provided by law, this income has been distributed as follows:

- \$228.3 million to the state's General Fund;
- \$610.6 million to the Dividend Fund;
- \$616.7 million to the principal of the Permanent Fund for inflation-proofing;
- \$763.3 million to the reserve account for future inflation and dividends.

**NET INCOME: \$657.8**  
(in millions)



This chart shows the distribution of net income earned from Permanent Fund investments during fiscal 1985.

## Permanent Fund Is Protected Against Inflation

The Permanent Fund is protected against inflation by a provision of state law which requires the automatic reinvestment of income each year in an amount sufficient to offset the effect of inflation on the corpus of the Fund during that year. The income may come from current year earnings or, if earnings are insufficient, from a reserve account established for this purpose.

This protection is provided in Alaska Statute 37.13.145, and is popularly known as inflation-proofing. Inherent in any well-managed trust, this provision was enacted in 1982 to assist the trustees in their efforts to maintain the real value of the Permanent Fund over long periods of time.

Here's how inflation-proofing works.

In each of the last three years, the trustees have taken the principal balance of the Permanent Fund at the end of the fiscal year and multiplied it by the average increase in the previous calendar year's Consumer Price Index (CPI). The product of these calculations has then been transferred from income to principal.

This year, for example, the calculation looks like this:

$$\begin{array}{rclcl} \text{End-of-fiscal-year} & & \text{CPI} & & \text{Inflation-proofing} \\ \text{principal balance} & \times & \text{increase} & = & \text{amount} \\ \$5,506.4 \text{ million} & \times & 4.26\% & = & \$234.6 \text{ million} \end{array}$$

To date, inflation-proofing has added \$616.7 million of earnings to principal to protect the real value of the Fund.

### INFLATION-PROOFING AMOUNTS

Fiscal Year	Inflation Rate Used	Income Reinvested	Percent of Annual Net Income
1985	4.26%	\$234,570,000	36%
1984	3.22%	180,935,000	29%
1983	6.10%	231,192,000	49%





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## YEAR IN REVIEW

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### Fund Investment Policy Is Risk Averse

In the first quarter of each calendar year, the trustees hold a special meeting with their informal advisors to review overall investment plans and determine the optimum mix of investment assets for the Permanent Fund for the upcoming 12 months. This year, the meeting was held in Juneau on February 25.

In determining the proper mix of assets, several elements are considered:

- \* the long-term average rate of return being sought;
- \* the amount of risk the portfolio should be exposed to;
- \* the probability of preserving principal;
- \* the probability of earning enough to offset inflation; and
- \* the probability of earning, in the upcoming year, the target rate of return.

This asset allocation process continues on a less formal basis throughout the year.

Once a rate-of-return goal is established — and there was unanimity that a 3% real rate of return, over time, is a realistic target for a conservative fund such as this — then the job is to design an asset allocation scheme which maximizes the above probabilities and minimizes risk.

The trustees considered a number of different asset allocation scenarios including the present, actual portfolio mix, the mix for typical governmental pension funds, and the mix for typical corporate pension funds. Among the findings:

\* The Fund portfolio of assets appears considerably more risk averse than the typical government or corporate pension fund. This is primarily the result of a greater dedication of assets to common stocks in government pension funds (33%) and corporate pension funds (52%) than in the Permanent Fund (11% actual).

\* The optimum mix of assets for the Fund is one which preserves principal assets as its highest priority, but is not so risk averse as to preclude: (1) a high probability of earning a positive real rate of return, and (2) an acceptable probability of earning the target rate, over time, of 3%.

As a result of the review and analysis of the various asset allocation alternatives, the trustees adopted an investment policy for the Permanent Fund as follows:

Bonds	80%
Stock	15%
Real Estate	5%

### Ad Hoc Advisors to the Trustees

During fiscal 1985, the trustees invited four esteemed persons to meet with them as peers, to assist them in analyzing current conditions and changes in the investment industry. The advisors do not offer specific investment advice as it pertains to individual transactions, but offer general technical comments and share experiences as professionals who have faced comparable questions and challenges.

The advisors are:

- \* Elmer Rasmuson, an Alaskan banker and first chairman of the Alaska Permanent Fund Corporation board;
- \* George Rogers, an Alaskan economist and second chairman of the Alaska Permanent Fund Corporation board;
- \* Robert Greeley, manager of corporate investments, Hewlett-Packard Company;
- \* George Bennett, former treasurer of Harvard University and president, State Street Research & Management Company.

Topics discussed this year by the trustees and their advisors included:

- real rate of return to be sought;
- acceptable degrees of risk;
- extent of diversification required;
- types of different investments;
- shifts in composition of portfolios;
- managing investment managers;
- accounting and internal controls;
- evaluation of industry trends.

# Annual Earnings Continue to Increase

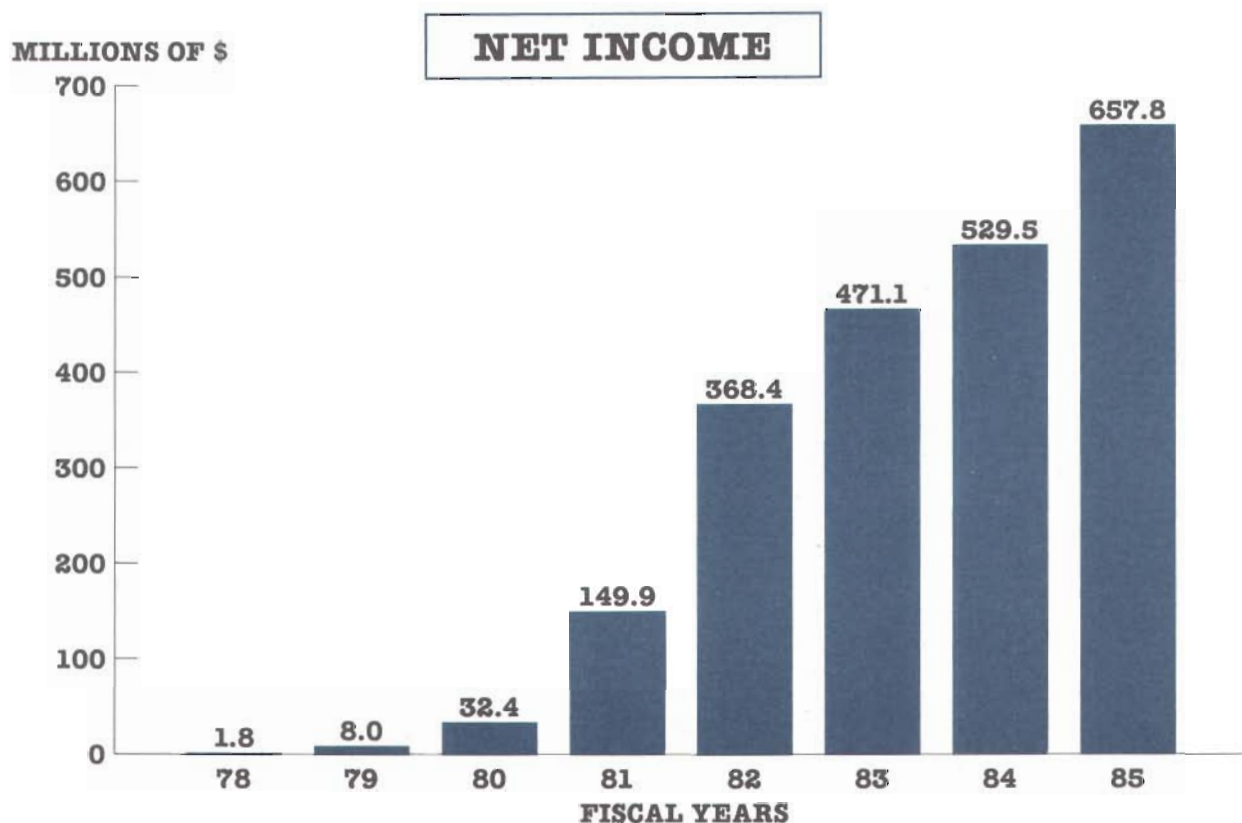
Despite a drop in market yields during the year, the Permanent Fund posted the largest net income in its history. This marks the eighth consecutive year of growth in earnings.

The predominant source of income remained interest earned on bonds, but increased ownership of common stock also meant more dividends received than ever before.

Fee income from loaned securities more than quadrupled, the Fund recorded some appreciation in the value of its real estate holdings for the first time, and there were some very healthy realized gains on the sale of marketable debt securities and common stock.

In addition, there were tremendous unrealized gains in both these portfolios (see chart).

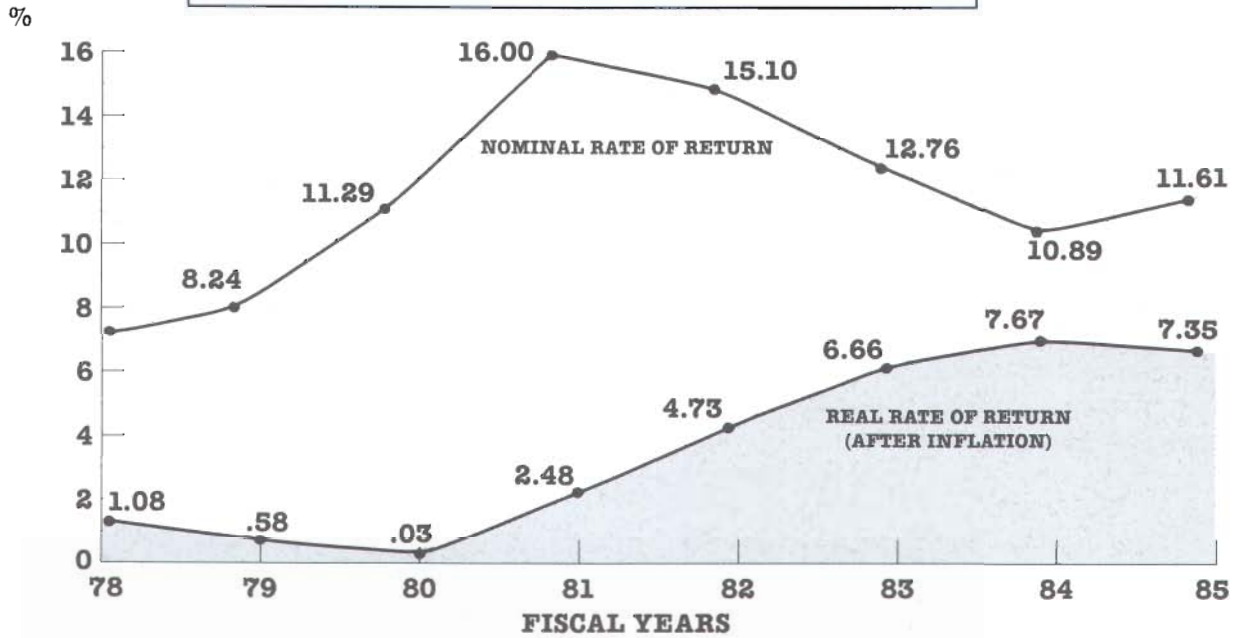
	<b>Realized</b>	<b>Unrealized</b>
Bonds	\$ 4.9	\$282.2
Stocks	9.1	91.5
Subtotal:	14.0	373.7
Real Estate (Recognized)		3.9
<b>Total:</b>	<b>\$14.0</b>	<b>\$377.6</b>



The Permanent Fund is invested to earn income. This graph shows how much income has been earned each year, net of operating expenses, since the Fund began on February 21, 1977.

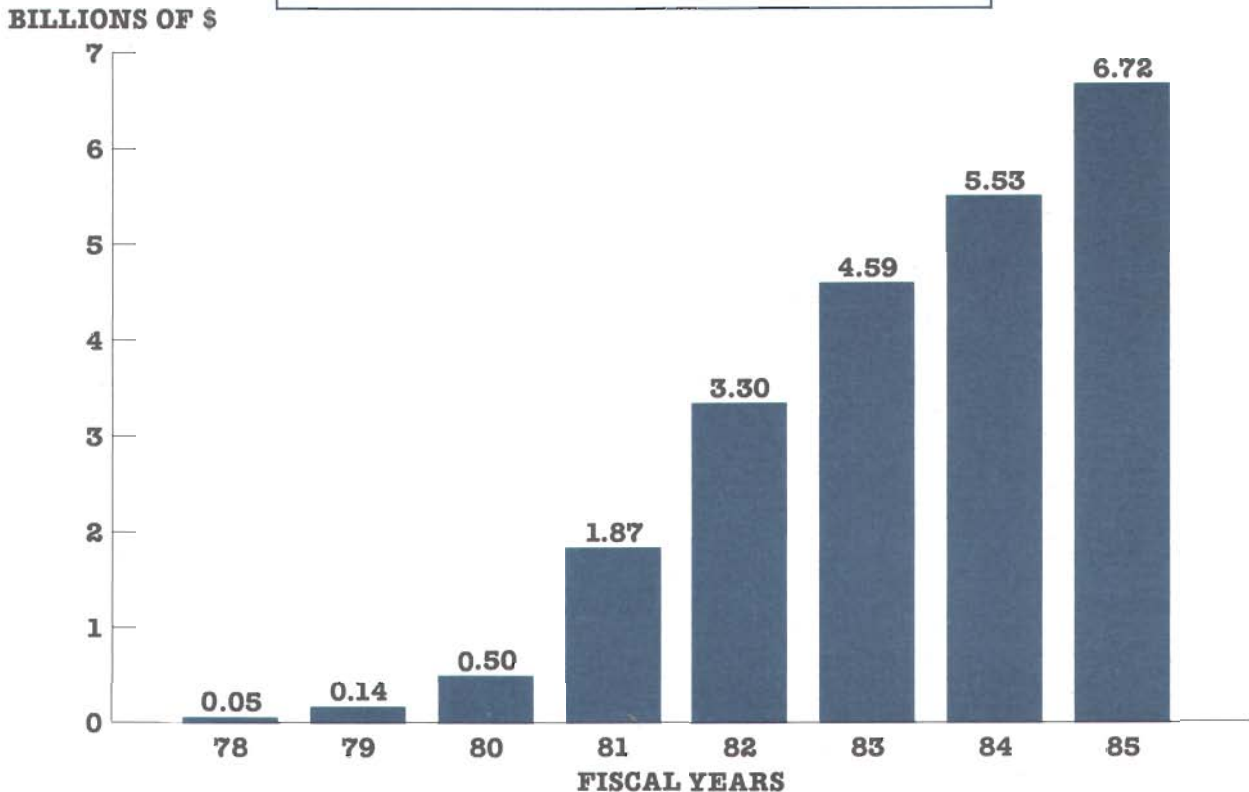
Total income earned in these first eight years is \$2,218,900,000. Current projections show the Permanent Fund, by the year 2005, earning this amount of net income each year.

## REALIZED RATES OF RETURN



In 1985, for the fourth consecutive year, the Fund exceeded its goal of a 3% real rate of return. The nominal yield was 11.61%. Inflation was 4.26%. The real rate of return was 7.35%. This chart shows the returns recognized by the Fund since its inception.

## GROWTH OF TOTAL ASSETS



In 1985, the assets of the Permanent Fund grew by nearly \$1.2 billion. This represents a 21.5% increase in assets in just one year, and makes the Fund one of the largest and fastest growing public savings accounts in the world.

## Stocks Were An Excellent Investment in 1985

In fiscal 1985, \$420 million was disbursed to the Corporation's five equity managers for investment in the stock market. The performance of these managers, and the status of the Permanent Fund's equity investments as of June 30, 1985, are presented in tables below.

\* *Note:* To understand the Permanent Fund's stock portfolio, it is necessary to clearly differentiate among the various terms used to describe the value of these equity investments. (Stocks are also known as equities to denote their ownership characteristics.)

\* *Cost:* At June 30, 1985, the Corporation has invested \$747.3 million in stock — primarily in common stock, but also in preferred stock, of domestic U.S. corporations.

\* *Market:* At June 30, 1985, the market value of the investment in stock amounted to \$838.8 million. This amount is what would be realized if all of the investment were liquidated on that date.

\* *Unrealized Gain:* At June 30, 1985, the arithmetic difference between cost and market value of the investment in stock

amounted to \$91.5 million. The market value exceeded the cost by this amount.

The Permanent Fund made its first stock investment on July 6, 1983. On that date, the Standard & Poor's 500 Stock Index stood at 168.48. On July 30, 1985, the S&P 500 closed at 191.85.

The long-term investment policy adopted by the trustees in March of this year calls for incremental investments in stock up to 15% of the total assets of the Fund by June 30, 1986, market conditions permitting.

The strategy for the stock portfolio divides equity investments between two types of management: two-thirds passive and one-third active. The idea is to attempt to do as well as the market — no better, no worse — with most of the Fund's stock investments (passive), and to attain superior performance with some of the investments (active). This is a conservative approach.

The passive investment is done by Bankers Trust Company, a national leader in stock index funds. During fiscal 1985, this equity manager received \$280 million from the Permanent Fund and invested it through use of a technique

### STATUS OF EQUITY INVESTMENTS

As Of June 30, 1985

(in millions)

Equity Managers	Cost	Market	Unrealized Gain
Bankers Trust	\$ 521.4	\$ 591.8	\$ 70.4
Batterymarch	64.5	66.4	1.9
Eaton/Vance	58.7	63.8	5.1
Lehman Management	52.5	58.1	5.6
Rosenberg Capital	50.2	58.7	8.5
<b>TOTAL</b>	<b>\$ 747.3</b>	<b>\$ 838.8</b>	<b>\$ 91.5</b>

known as "stratified sampling" to statistically replicate the performance of the S&P 500.

The active management is divided among four managers, selected by the trustees in July of 1983, to provide diversification by different generalized investment styles. The styles and the managers are as follows:

\* *Rotational/Contrarian*: Batterymarch Financial Management of Boston, Massachusetts emphasizes, in their portfolio construction, out-of-favor equities with potential for increased value.

\* *Value*: Lehman Management Company Inc. of New York, New York emphasizes inherent or unrecognized value in their purchases.

\* *Growth 1*: Rosenberg Capital Management of San Francisco, California emphasizes stocks with proven long-term growth.

\* *Growth 2*: Eaton/Vance, Inc. of Boston, Massachusetts emphasizes stocks with unestablished but anticipated growth potential.

Each of these managers received \$35 million in fiscal 1985, and \$62.5 million since the inception of the program.

The basic rules for Permanent Fund stock investments are that: (1) no more than 5% of the voting stock of any corporation may be acquired or held; (2) all stocks, except for bank stocks and insurance stocks, must be listed on the New

York or American Stock Exchanges; and (3) only the stock of corporations incorporated in the U.S. may be acquired or held. The purchase of options, or any security on margin, or purchases in the commodities futures market, or futures contracts for any purpose other than hedging are prohibited.

## Loaned Securities Make Profits

The Alaska Permanent Fund Corporation loans both marketable debt securities and common stock to major financial institutions, including broker dealers, for a fee. Securities loaned by the Corporation are collateralized in excess of 100% of market value, and collateral is physically delivered to our custodian banks, the Alaska National Bank of the North and the Bank of America.

### Loaned Securities History

Fiscal Year	Income
1985	\$ 1,860,000
1984	394,000
1983	22,000
1982	—0—

During fiscal 1985, a total of \$1.9 million was received in loaned securities fees. This program alone completely offset all bank custodial fees charged to the Corporation during the year, and at virtually no risk.

### PERFORMANCE OF EQUITY MANAGERS

Equity Managers	Fiscal 1985	Since Inception
Standard & Poor's 500 Stock Index	31.0%	28.8% & 27.6%*
Bankers Trust	31.0%	33.0%
Eaton/Vance	22.6%	9.1%
Batterymarch	19.8%	14.8%
Lehman Management	32.7%	30.9%
Rosenberg Capital	29.1%	28.1%
Managers Average:	<b>27.0%</b>	<b>23.2%</b>

\*Inception for Bankers Trust was July 1983. Since then, the S&P 500 has risen 28.8%. Inception for the four active managers was September 1983. Since then, the S&P 500 has risen 27.6%. In all cases, returns include dividends, capital gains and losses, both realized and unrealized.

## Equity Real Estate: A New Portfolio for the Permanent Fund

In fiscal 1985, the trustees approved equity real estate investments totaling \$109.3 million. Discounting commitments for future funding, and including disbursements for the first three investments of this type approved in fiscal 1984, the market value of the Corporation's equity real estate portfolio, as of June 30, 1985, was \$129.7 million.

The investment strategy for the equity real estate portfolio is structured to (1) maintain safety of principal, and (2) maximize total return. Funds are invested only in income-producing properties — *i.e.*, real estate improved by completed and substantially-rented buildings — located in the United States. The objective is to seek a 6% rate of return, after inflation, for equity real estate as an asset class over a long-term holding period.

Individual investments may be pure equity, or a combination of equity and debt, but at least 60% of the beneficial ownership interests must be held by other institutional investors. Though the law allows up to 15% of the assets of the Permanent Fund to be invested in equity real estate, the trustees have adopted a more conservative 5% limit at this time.

The following policies apply to the selection of equity real estate assets:

- a. Equity real estate investments must consist of those with a high probability of providing continuous cash flow.
- b. Equity real estate investments must offer minimal income volatility.
- c. Equity real estate investment proposals must be subject to development of reliable projections of future earnings.

To minimize risks attributable to regional economic imbalances, property performance volatility, and management style, the equity real estate portfolio exhibits diversification by location, prop-

erty type, investment type, and investment manager.

There are three classifications of assets in the equity real estate portfolio:

### Class I

These assets are like shares in mutual funds. They are investments in commingled real estate funds sponsored by professional real estate investment managers with demonstrated experience in the acquisition and management of real estate assets on behalf of institutional investors. The sponsors of the funds maintain investment discretion of these assets.

The Permanent Fund has three investments in Class I assets:

**A \$15 million investment in Endowment and Foundation Realty, Ltd. — JMB II.** This is a 12.5% interest in a closed-end real estate fund sponsored by JMB Institutional Realty Corporation of Chicago, Illinois. Some of our co-investors in JMB II include the Ford Foundation, University of Pennsylvania, Stanford University, University of Notre Dame, the Carnegie Corporation of New York, and Yale University. (A \$20 million commitment has also been issued to participate in JMB's latest closed-end fund, JMB III.)

**A \$28.9 million investment in CPI,** a \$1.3 billion real estate investment trust sponsored by Corporate Property Investors, located in New York, New York. CPI is a vehicle for investment in real property with a special emphasis on regional shopping centers. Major shareholders include the Government of Kuwait, the pension fund of AT&T, and Prudential Insurance Company.

**A \$25.6 million investment in CIGNA Fund S,** a \$130 million closed-end real estate fund sponsored by CIGNA Capital Advisors, Inc. This particular fund, or real estate pool, emphasizes office buildings. The management firm is located in Hartford, Connecticut. Some of our co-in-

vestors in this pool include the Rockefeller Foundation, University of Pittsburgh, United Methodist Church, Board of Pensions of the United Presbyterian Church, and the State of Connecticut Trust Funds.

## **Class II**

These assets include direct real estate investments originated by selected real estate advisors who structure joint ventures with other institutional investors. At the annual meeting last September, the trustees, with the help of the Corporation's real estate consultant, Pension Realty Advisors, Inc. of San Francisco, California, selected three firms to be Class II real estate advisors to the Corporation: (1) Heitman Advisory Corporation, located in Chicago, Illinois; (2) The Boston Company Real Estate Counsel, Inc., located in Boston, Massachusetts; and (3) Kennedy Associates Real Estate Counsel, Inc., located in Seattle, Washington.

The trustees have made three investments in Class II assets, and issued two commitments for future funding:

**A \$6.6 million investment in an industrial park in Cincinnati, Ohio,** known as Tri-County Corporate Center. This all-equity investment consists of 10 office/warehouse buildings. The Corporation is a one-third owner.

**A \$9.4 million investment in the Oakwood Mall Shopping Center,** located in Enid, Oklahoma. This is a new regional shopping center with a total gross leasable area of 444,247 square feet. The investment is a one-third joint venture participation in a participating mortgage. (A participating mortgage provides a fixed rate of return, a share in the lease profits, and a share in the appreciated value of the property involved.)

**A \$14.4 million all-equity investment in the Villa Marina Shopping Center,** located in Marina del Rey, California. This is a multi-use community shopping center containing 245,853 leaseable square feet. The Corporation is a 40% owner.

**A \$25 million commitment to participate, upon completion, in the Owings Mills Town Center,** located in Owings Mills, Maryland. The investment will be a 25% participation in a participating mortgage. Phase I of the project will consist of an 815,000 square foot regional shopping mall. Estimated funding date: the fourth quarter of 1986.

**An \$11.4 million commitment to participate, upon completion, in the Epic Center, a 22-story office building,** located in Wichita, Kansas. The investment will be a 40% participation in a participating mortgage. Estimated funding date: the first quarter of 1987.

## **Class III**

These assets include real estate investments which are made by the Corporation to take advantage of real estate market opportunities which exist beyond the outreach of the Class II advisors.

Two investments have been made under this class as follows:

**A \$21.8 million all-equity investment in the Tyson's Corner Regional Shopping Center,** located in McLean, Virginia. The center contains approximately 1.5 million net rentable square feet. The Corporation has a 14% ownership interest. The originator and manager of this investment is Lehndorff and Babson Real Estate Counsel, Inc., located in Dallas, Texas.

**An \$8 million investment in the Paragon Building, a 14-story office building,** located in Dallas, Texas. The Corporation has a one-quarter participation in a participating mortgage. The partner in this investment is the Equitable Life Assurance Society of the United States. The Paragon Building was the Corporation's first equity real estate investment, which was made in September 1983.

# REAL ESTATE HOLDINGS

Investment Entity	Investment Manager	Permanent Fund Investment as % of Total Property	Dollars Invested (in millions)	Investment Property Name	Property Type
Equity Pools	Corporate Property Investors	2.0%	\$ 28.9	60 properties	Office/Retail
	JMB Institutional Realty Corporation	12.5%	15.0	8 properties	Office/Retail
	<b>Total Equity Pools</b>		<u>43.9</u>		
Participating Mortgage	The Equitable Life Assurance Society of the United States	25.0%	8.0	Paragon Building Dallas, Texas	Office
Limited Partnership	CIGNA Capital Advisors	19.6%	25.6	11 properties	Office/Retail Residential/Industrial
General Partnerships	Heitman Advisory Corporation	33.0%	9.4	Oakwood Mall Enid, Oklahoma	Retail
	Heitman Advisory Corporation	33.0%	6.6	Tri County Corporate Center, Cincinnati, Ohio	Industrial
	Heitman Advisory Corporation	39.8%	14.4	Villa Marina Marina del Rey, California	Retail
	Lehndorff & Babson Real Estate Counsel	14.0%	21.8	Tyson's Corner Shopping Center, McLean, Virginia	Retail
	<b>Total General Partnerships</b>		<u>52.1</u>		
	<b>TOTAL PERMANENT FUND DOLLARS INVESTED</b>		<b>\$129.7</b>		

# REAL ESTATE DIVERSIFICATION

<b>By Investment Manager</b>			<b>By Investment Type</b>		
	<b>Permanent Fund Dollars</b> <small>(in millions)</small>	<b>% Weight</b>	<b>Equity</b>	<b>Hybrid</b>	
JMB	\$ 15.0	11.6%	73%	27%	JMB
CIGNA	25.6	19.7%	57%	43%	CIGNA
CPI	28.9	22.3%	80%	20%	CPI
Heitman	30.4	23.4%	0%	100%	Oakwood
Equitable	8.0	6.2%	100%	0%	Tri-County
Lehndorff	21.8	16.8%	100%	0%	Villa Marina
<b>Total</b>	<b>\$129.7</b>	<b>100.0%</b>	<b>70%</b>	<b>30%</b>	Paragon
					Tyson's
					<b>Total</b>

### By Property Type

	<b>% Weight</b>	<b>Office</b>	<b>Retail</b>	<b>Industrial</b>	<b>Residential</b>
JMB	12%	42%	58%	0%	0%
CIGNA	20%	67%	10%	13%	10%
CPI	21%	16%	83%	1%	0%
Oakwood	8%	0%	100%	0%	0%
Tri-County	5%	0%	0%	100%	0%
Villa Marina	11%	0%	100%	0%	0%
Paragon	6%	100%	0%	0%	0%
Tyson's	17%	0%	100%	0%	0%
<b>Total</b>	<b>100%</b>	<b>28%</b>	<b>62%</b>	<b>8%</b>	<b>2%</b>

### By Property Location

	<b>% Weight</b>	<b>East</b>	<b>South</b>	<b>Midwest</b>	<b>West</b>
JMB	12%	11%	43%	7%	39%
CIGNA	20%	0%	54%	16%	30%
CPI	21%	49%	26%	9%	15%
Oakwood	8%	0%	100%	0%	0%
Tri-County	5%	0%	0%	100%	0%
Villa Marina	11%	0%	100%	0%	0%
Paragon	6%	0%	100%	0%	0%
Tyson's	17%	100%	0%	0%	0%
<b>Total</b>	<b>100%</b>	<b>29%</b>	<b>35%</b>	<b>11%</b>	<b>25%</b>

## Trustees Extend Maturity of Bond Portfolio

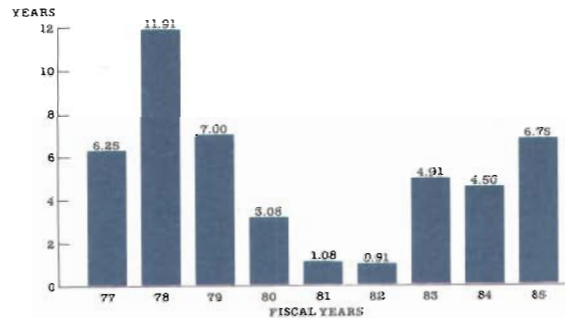
During fiscal 1985, the trustees recognized that progress had been made against inflation, and that there existed the possibility of significant new deficit reduction programs being proposed after the 1984 elections. In light of these factors, they adopted an investment strategy which provided for gradual portfolio maturity extension (see graph below).

Accordingly, the trustees directed the staff of the Alaska Permanent Fund on March 18, 1985 to place marketable fixed-income emphasis on:

“... securities with maturities of not less than two years or more than ten years. If, in the opinion of staff, the inflation outlook continues favorable, and there is reason to believe that substantive measures will be taken to reduce future Federal budget deficits, increased emphasis may be placed on the four to ten year maturity range. Investments in this maturity range, however, shall not exceed

50% of the marketable fixed-income portfolio. Investments in securities with maturities in excess of ten years shall not exceed 15% of the portfolio.”

### AVERAGE MATURITY OF BONDS



This chart shows the weighted average length of maturity for all the marketable fixed-income investments of the Permanent Fund as of the end of each fiscal year. As of June 30, 1985, for example, this was six years and nine months.

## Trustees: Accountability Is a Priority

Because the Alaska Permanent Fund is a public trust — that is, wealth which belongs, collectively, to all the people of the state, for the benefit of present and future generations — the people have a clear right to know what is happening with their money.

Recognizing this, the trustees, at a special meeting in April, gave final approval to a comprehensive public information and accountability program. The program is designed to ensure that the Alaskan public understands the history of the Fund, its formation, how it works, how it's doing, and its role in the future.

There is, however, more to the program than simply attempting to satisfy the people's right to know. There is also the responsibility to build an informed constituency to protect the Fund. When there are billions of dollars of public money at stake, there are significant dangers that the

wealth may somehow be dissipated — by poor investments, improper management, or premature withdrawals to spend the public's savings on special interests.

Elements of the Corporation's public information and accountability program include:

\* **Monthly Financial Statements:** These reports are the cornerstone of the Corporation's print communications. They convey all the important current financial information in a timely manner. In addition, each month's report includes a narrative highlighting various specific aspects of the Fund. There is an extensive mailing list for these monthly financials. Persons interested in being added to the mailing list should contact the Corporation's Juneau office.

\* **Speakers Bureau:** In fiscal 1985, trustees and staff spoke to over 30 different civic groups and organizations around

the state as part of an organized and active effort to reach some of Alaska's most important opinion makers. The trustees appreciate the opportunity these public appearances provide to communicate directly with the Fund's beneficiaries.

\* **Instructional Television Program:** Perhaps the most ambitious public information effort this year has been to produce a short video and teacher's guide for the 43,633 high school students in Alaska. This group of people will be deciding the future of the Permanent Fund as they grow to become Alaska's voting and tax-paying citizens and leaders. They are an important part of the Corporation's long-term communications program. Intended to provide basic information about the Permanent Fund, this instructional program should be completed and distributed to Alaska's 55 school districts by January 1986.

\* **Permanent Fund Dividend Brochure:** The mailing of the 1985 Alaska Permanent Fund dividend checks will include an informational brochure produced by the Corporation in cooperation with the Department of Revenue. This method of direct mail provides an excellent opportunity to communicate a limited but important amount of information about the Fund to over 520,000 individual Alaskans.

\* **Public Service Announcements (PSAs):** The Corporation is in the process

of developing a series of 30- and 60-second radio spots to be used to clear up certain misconceptions about the Permanent Fund. Relatively inexpensive to produce, and broadcast at no expense, radio PSAs are a simple way to communicate basic information to large numbers of people. One PSA, which was broadcast this year on television, related to the dividend program and the deadline for submitting applications. Again, this was produced in conjunction with the Department of Revenue.

In addition, as required by law, the Corporation published its fiscal 1984 annual financial statements in newspapers in each judicial district, and included descriptive material in the biennial election pamphlet mailed to each registered voter in the last election.

The Corporation also distributes and has available to the public: (1) annual reports; (2) brochures describing the Fund's home mortgage program; (3) projections of Fund revenues, earnings and balances; and (4) research papers on various topics of concern to the Corporation, *e.g.*, analyses of legislation.

The Corporation was assisted in the development of portions of this public information and accountability program by a media consultant hired for this purpose, Pacific Communications and Marketing. This Alaska-based firm was chosen by the trustees at the February meeting following a competitive proposal process.

## Corporation Meetings Open to the Public

It is the policy of the trustees to conduct all meetings of the Alaska Permanent Fund Corporation as open meetings. The general public is encouraged to participate at each meeting, and a portion of each agenda is reserved for this purpose. Alaskans must always be given the opportunity to be involved in — not simply told about — the decisions that affect their lives and futures.

During fiscal 1985, the trustees held four regular meetings — one in each quarter — and four special meetings.

The dates and locations were as follows:

### Regular Meetings

September 20-21, 1984 — Anchorage

December 10, 1984 — Juneau

March 18, 1985 — Juneau

June 28, 1985 — Juneau

### Special Meetings

August 8, 1984 — Anchorage

January 28, 1985 — Juneau/Anchorage

February 25, 1985 — Juneau

April 29, 1985 — Anchorage

Summary minutes for all meetings are on file in the Corporation's Juneau office.

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## COMMITMENT TO ALASKA

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### Fund Makes In-State Investments

As of June 30, 1985, \$303.5 million, or 4.5%, of the Permanent Fund was committed to Alaskan investments, and 2.6% was actually disbursed. Authorized Alaskan investments include the following:

\* **Home Mortgages:** The trustees have allocated \$80 million for investment in Alaska residential mortgages (owner-occupied, one-to-four units). These are offered at market rates, adjusted once each year, for a term not to exceed 30 years. A change in the regulations for this program this year imposed a 6% cap on the adjustable rate over the life of the loan. During fiscal 1985, at rates ranging from 12 to 13%, 102 loans were closed, amounting to \$18.5 million. As of June 30, 1985 the total home mortgage portfolio consisted of 326 loans totaling \$48 million.

\* **AHFC Taxable Bonds:** The Fund presently holds \$23.5 million in taxable corporate bonds issued by the Alaska Housing Finance Corporation (AHFC). Backed by Alaskan home mortgages owned by AHFC, these bonds offer an excellent investment opportunity in terms of yield, quality, liquidity and diversification.

\* **Alaska Certificates of Deposit:** The trustees have allocated \$200 million

for investment in the local economy through the purchase of certificates of deposit issued by Alaska banks. This program, which was initiated last year, has met with substantial interest. At year end, \$107.5 million had been disbursed to six Alaska financial institutions. These CDs have three-year terms and are priced at a floating rate of interest equal to the 90-day U.S. Treasury bill rate, plus 50 basis points, adjusted quarterly. All CDs are collateralized in excess of 100% of value.

\* **Commercial Real Estate:** Though no investments have been made to date in Alaska commercial properties, the authorization exists. The Permanent Fund can and will invest in Alaska real estate improved by completed and substantially-rented buildings whenever the risk level and expected yield are comparable to alternate investments.

In addition to in-state investment, the Permanent Fund plays a significant role in the Alaska economy by virtue of the Permanent Fund Dividend Program which will distribute in excess of \$200 million this year to all qualified residents of the state. Economists say no other use of an equal amount of state dollars has a more positive macroeconomic effect than this direct cash distribution.

#### 1984-85 INTEREST RATE TRENDS

Quarter	Permanent Fund CD Rate	Permanent Fund Home Mortgage Rate	Prime Rate
6/84	10.91%	12.125%	13.00%
9/84	11.15%	12.75%	12.75%
12/84	8.55%	12.875%	10.75%
3/85	8.97%	12.375%	10.50%
6/85	7.72%	12.125%	9.50%

# The Alaska Permanent Fund Dividend Program: Economic Effects and Public Attitudes

When the legislature approved the Alaska Permanent Fund Dividend Program in 1982, it also authorized the expenditure of \$125,000 to study public attitudes about the program and its effects on the economy of the state and on the lives of individual Alaskans. The study was conducted by the Institute of Social and Economic Research (ISER) and was presented to the trustees in September 1984.

*Though this report is now nearly a year old, the economic effects of the dividend program, as described below, are still valid. As to public attitudes, though the answers to the questions may have changed, the questions themselves will remain near the center of public policy debate for years to come.*

As described by the lead investigator for the project, the study did not take a stance or offer recommendations with respect to the dividend program, but rather assembled information. The study consists simply of "fact findings".

Key findings include the following:

## 1. Economic Effects.

\* Dividends accounted for 17% of the increase in disposable income for 1981-1983.

\* The dividend program has resulted in the contribution to the economy of over 7,000 jobs.

\* Compared to the expenditure of an equivalent amount of public funds for other purposes, including government operations, capital projects, subsidies, local transfers, or nonpetroleum tax reductions, the dividends produce the largest increase in before- and after-tax income, employment and population.

\* How Alaskans used their dividends varied with income. Lower income Alaskans used more of the money to reduce their debt and for day-to-day expenses,

while higher-income Alaskans used more of the money for taxes and savings.

\* Inflation and the desire to work were little affected by the dividends, and few people moved to Alaska solely to receive a dividend. However, because the dividend program stimulates employment more than other uses of public funds, it does have the effect of bringing more people to Alaska.

## 2. Public Attitudes.

\* About 60% of Alaskans think the dividend program is a good idea. Twenty-nine percent have mixed feelings. Ten percent think it is a bad idea.

\* A majority of Alaskans prefer the dividend program over more state and local construction projects, reduced property taxes, subsidized loan programs, or putting the money for dividends back into the Permanent Fund.

\* Eighty-seven percent of Alaskans would not halt the inflation-proofing of the Fund so that the state could use the earnings for other purposes.

\* Seventy-one percent of Alaskans would choose to end the dividends now rather than reimpose the personal income tax.

\* A substantial majority of Alaskans think that they are entitled to a share in the earnings of the Permanent Fund and have no problem with receiving money directly from the state. In addition to viewing dividends as an entitlement, most Alaskans see the dividend program as a means of protecting the principal of the Permanent Fund and as a more effective vehicle for using public funds to benefit Alaska residents than legislative appropriations. They also think that the dividend program has made them pay closer attention to how the state spends the money it receives.

## Report on 1985 Legislation

The 1985 Alaska State Legislature did not pass any major Permanent Fund legislation. Of the 17 bills and 3 resolutions introduced this session which would affect the Permanent Fund or the Permanent Fund Dividend Program, only two — CSSB 283(Finance) and CCSSB 56 — were signed into law by the governor.

The first, Chapter 45, SLA 1985, provides that the Department of Revenue shall prepare future Permanent Fund dividend applications to allow applicants to designate that \$5 of the dividend be subtracted from their checks and contributed to the Alaska Winter Olympics account in the General Fund “to be used to develop facilities for Winter Olympic training and competition and to attract the Winter Olympics to Alaska.” The effective date of the bill is July 1, 1986.

The second, Chapter 99, SLA 1985, provides for continuation of the existing longevity bonus program for all one-year Alaska residents over the age of 65, and requires an advisory vote at the next general election on the question of whether the legislature should adopt an annuity program — funded in part by Permanent Fund dividends — in its place. Under the complex provisions of the bill, the existing program will continue until and unless a future legislature either (1) repeals the sections of this bill which would create the annuity program, in which case the longevity bonus program is then closed to all persons who have not reached age 65 by January 1, 1988; or (2) repeals the section of this bill which would close the

longevity bonus program to all persons who have not reached age 65 by January 1, 1988, in which case the annuity program then becomes effective.

The more controversial Permanent Fund bills, such as those measures which would increase deposits to the Fund, or those which would spend portions of the undistributed income account, did not see final action.

The House did pass CSHB 28(Finance) which transfers \$400 million from the undistributed income account to the principal of the Permanent Fund. It also passed CSHB 71 (State Affairs) which authorizes a special open-ended appropriation of \$500 million to the Fund. Neither bill, however, was given a hearing in the Senate.

The Senate passed CSSB 233 which would have allowed Alaska financial institutions to use obligations of the state or instrumentalities of the state as collateral against funds borrowed from the Permanent Fund under the Alaska Bank Certificates of Deposit Program, but this bill stalled in the House Finance Committee.

One development related to past legislative action was the final deposit by Governor Sheffield of \$300 million due to the Permanent Fund as part of a previous \$1.8 billion appropriation.

All bills introduced in the First Session of the 14th Legislature remain on the table for consideration in the Second Session. In addition, it is possible — and likely — that other bills will be introduced next year which relate to the Permanent Fund.

## U.S. Economic Rebound Expected in 1986

During the second half of calendar year 1985, the economy will likely stumble along, continuing to show further weakness. The recent weakness in homebuilding and auto sales, combined with a slump in high technology industries, does not augur well for the second half. Consumer spending may be limited in coming months by an increasingly heavy debt burden. American consumer loans have increased 20% from the levels of a year ago. In addition, many personal, corporate, and banking balance sheets have deteriorated seriously as the dollar value of agricultural land, oil, and much real estate has fallen. It would not be surprising should the Federal Reserve Bank ease monetary policy further in the second half in order to support economic activity.

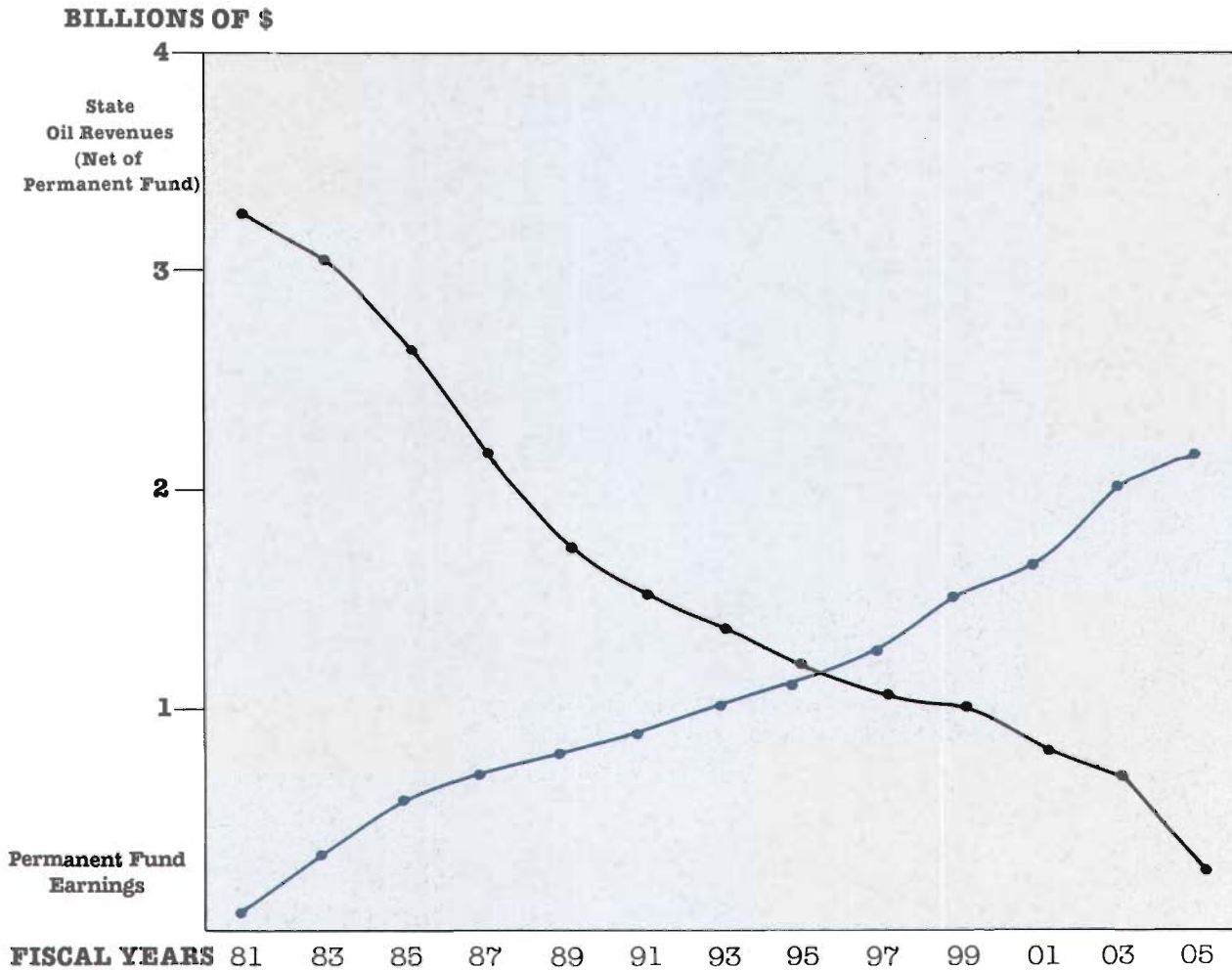
Indications, however, suggest that the prospects for a substantial economic rebound in 1986 have improved considerably. Real interest rates have fallen sharply during 1985, and the level of real short rates has not been lower in over five years. The magnitude of the decline in short rates over the past year and the rapid rise in M1, the most widely followed measure of money growth, underscore the magnitude of the easing of monetary policy and the degree of liquidity infusion undertaken by the Federal Reserve Bank. These factors, combined with the fact that the U.S. dollar has been trending lower and inflation has remained subdued in the United States and other industrial countries, would indicate that the economic stage has been set for a rebound of the U.S. economy in 1986, a rebound of perhaps significant proportions. Although the secular disinflation process appears to remain the dominant long-term economic force, a cyclical interruption of perhaps moderate proportions appears increasingly likely during 1986.

The failure of Congress to meet its own deficit reduction goals through reductions in spending and increases in revenue poses difficult economic problems for the future. Using conservative Congressional Budget Office estimates for Treasury revenues and growth in public debt, and assuming no further fiscal measures, interest on the United States public debt could approach \$290 billion or 27% of all Treasury revenues within five years' time. The impact of burgeoning budget deficits has already been felt in the form of high real interest rates, an overvalued U.S. dollar, and record high trade deficits. Manufacturing, farming, and mining have all suffered as a consequence. In addition to declining profitability, the damage is reflected in lost jobs, failure to modernize industry, and lost international competitiveness.

While there is little likelihood that inflation will come to life over the next six to nine months, it could well become a problem in 1986 should the Federal Reserve Bank continue to ease monetary policy and permit continued rapid growth in the money supply. Should Congress and the President be perceived as resorting to ineffective half-measures to deal with the chronic deficit problem, it is all too likely that both foreign and domestic investors will eventually lose confidence in the U.S. dollar, and this country will experience yet another round of inflation and economic turmoil. Of concern to all investors is the possibility that without a satisfactory resolution of the deficit problem, governmental officials will at some point pursue economic policies that deal with the problem by promoting inflation in order to pay interest on the debt with grossly inflated dollars and thus reduce the deficit's impact on the economy.

**PROJECTED STATE OIL REVENUES VS.  
PERMANENT FUND EARNINGS  
1980-2005**

(actual and projected)



This graph depicts the relationship between total expected state oil revenues, as forecast by the state Department of Revenue, net of constitutionally-dedicated contributions to the Permanent Fund, and the projected earnings of the Permanent Fund, as projected by the corporation. According to these projections, fund earnings will overtake oil revenues and become the number one producer of state income about ten years from now.





# **ALASKA PERMANENT FUND CORPORATION**

**Financial Statements**  
**June 30, 1985 and 1984**

**REPORT OF INDEPENDENT ACCOUNTANTS**



101 West Benson Boulevard  
Suite 500  
Anchorage, Alaska 99503

August 13, 1985

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, 1985 and 1984, 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*

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**STATEMENT OF ASSETS, LIABILITIES AND FUND EQUITY**


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ASSETS	June 30,	
	1985	1984
Cash	\$ 878,000	\$ 259,000
Receivables and prepaid expenses	188,592,000	171,250,000
Investments:		
Marketable debt securities —		
Repurchase agreements	7,300,000	124,600,000
Short-term issues	54,493,000	329,605,000
Intermediate and long-term issues	5,438,792,000	4,564,080,000
Total marketable debt securities	<u>5,500,585,000</u>	<u>5,018,285,000</u>
Real estate —		
Equity pools	43,898,000	7,500,000
Participating mortgage	8,000,000	8,000,000
Limited partnership	25,648,000	
General partnerships	52,104,000	
Total real estate	<u>129,650,000</u>	<u>15,500,000</u>
Preferred and common stock, net of valuation allowance (1984)	747,303,000	290,835,000
Conventional mortgages	47,985,000	34,549,000
Alaska certificates of deposit	107,500,000	
Total investments	<u>6,533,023,000</u>	<u>5,359,169,000</u>
Property and equipment, net of accumulated depreciation	359,000	121,000
<b>Total assets</b>	<u><u>\$ 6,722,852,000</u></u>	<u><u>\$ 5,530,799,000</u></u>
<b>LIABILITIES</b>		
Accounts payable	\$ 1,372,000	\$ 849,000
Income distributable to the State of Alaska	217,274,000	155,130,000
<b>Total liabilities</b>	<u>218,646,000</u>	<u>155,979,000</u>
<b>EQUITY</b>		
Contributed equity	5,740,942,000	4,838,344,000
Reserve for inflation and dividends	763,264,000	557,347,000
Unrealized loss on common stock		(20,871,000)
<b>Total equity</b>	<u>6,504,206,000</u>	<u>5,374,820,000</u>
Total liabilities and equity	<u><u>\$ 6,722,852,000</u></u>	<u><u>\$ 5,530,799,000</u></u>

See accompanying notes to financial statements

## ALASKA PERMANENT FUND CORPORATION

## STATEMENT OF REVENUES AND EXPENDITURES

	<u>Year Ended June 30,</u>	
	<u>1985</u>	<u>1984</u>
<b>Revenues:</b>		
Interest	<b>\$ 614,021,000</b>	\$ 522,508,000
Dividends	<b>25,325,000</b>	7,124,000
Fees on loaned securities	<b>1,860,000</b>	394,000
Earnings on real estate partnerships	<b>2,622,000</b>	
Realized gains on the sale of —		
Marketable debt securities	<b>4,889,000</b>	476,000
Preferred and common stock	<b>9,125,000</b>	1,650,000
Total gains	<b>14,014,000</b>	2,126,000
Unrealized gain on real estate	<b>3,898,000</b>	
<b>Gross revenues</b>	<b>661,740,000</b>	532,152,000
<b>Expenses:</b>		
Salaries and benefits	<b>751,000</b>	699,000
Travel	<b>70,000</b>	83,000
Trustee honoraria	<b>34,000</b>	32,000
Communications	<b>146,000</b>	156,000
Real estate consulting fees	<b>236,000</b>	43,000
Printing and advertising	<b>39,000</b>	23,000
Office rent	<b>90,000</b>	89,000
Custody and safekeeping fees	<b>786,000</b>	606,000
Real estate management fees	<b>64,000</b>	
Preferred and common stock management fees	<b>1,117,000</b>	515,000
Conventional mortgage service fees	<b>164,000</b>	113,000
Participating mortgage service fees	<b>80,000</b>	100,000
Legal and audit	<b>153,000</b>	48,000
Public information program	<b>140,000</b>	
Depreciation	<b>71,000</b>	51,000
Other	<b>38,000</b>	137,000
Total operating expenses	<b>3,979,000</b>	2,695,000
<b>Net income</b>	<b>\$ 657,761,000</b>	\$ 529,457,000

See accompanying notes to financial statements

**STATEMENT OF CHANGES IN FUND EQUITY  
FOR THE YEARS ENDED JUNE 30, 1985 AND 1984**

	Total	Contributed Equity	Reserve For Inflation and Dividends	Unrealized Loss On Common Stock	Undistributed Income
<b>Balance, June 30, 1983</b>	<b>\$ 4,375,036,000</b>	<b>\$ 4,021,226,000</b>			<b>\$ 353,810,000</b>
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 dividends 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)
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)
<b>Balance, June 30, 1984</b>	<b>5,374,820,000</b>	<b>4,838,344,000</b>		<b>(20,871,000)</b>	
Appropriations from the state	300,000,000	300,000,000			
Dedicated state revenues	368,027,000	368,027,000			
Net income from operations	657,761,000				657,761,000
Citizen contributions	1,000	1,000			
Provision for 1985 dividends	(217,274,000)				(217,274,000)
Provision for 1985 inflation		234,570,000			(234,570,000)
Recovery of unrealized loss on common stock	20,871,000			20,871,000	
Provision for future inflation and dividends			205,917,000		(205,917,000)
<b>Balance, June 30, 1985</b>	<b>\$ 6,504,206,000</b>	<b>\$ 5,740,942,000</b>	<b>\$ 763,264,000</b>	<b>\$</b>	<b>\$</b>

See accompanying notes to financial statements

## ALASKA PERMANENT FUND CORPORATION

## STATEMENT OF CHANGES IN FINANCIAL POSITION

	<u>Year Ended June 30,</u>	
	<u>1985</u>	<u>1984</u>
<b>FUNDS WERE PROVIDED BY:</b>		
Investment operations —		
Net income	\$ 657,761,000	\$ 529,457,000
Items not affecting funds —		
Amortization	(1,391,000)	(416,000)
Depreciation	71,000	51,000
Increase in receivables and prepaid expenses	(17,342,000)	(18,985,000)
Increase in accounts payable	523,000	301,000
Unrealized gain on real estate	(3,898,000)	
Undistributed partnership earnings	(958,000)	
Funds provided by operations	<u>634,766,000</u>	<u>510,408,000</u>
Sales —		
Marketable debt securities	2,754,418,000	1,648,273,000
Preferred and common stock	103,920,000	53,758,000
Total sales	<u>2,858,338,000</u>	<u>1,702,031,000</u>
Maturities of debt obligations	676,188,000	1,252,920,000
Conventional mortgage repayments	5,035,000	7,653,000
Redemption of Alaska certificates of deposit		50,000,000
Decrease in value of common stock		20,871,000
Recovery of value of common stock	20,871,000	
Citizen contributions	1,000	
Contributions from the State of Alaska	668,027,000	666,183,000
<b>Total funds provided</b>	<u>4,863,226,000</u>	<u>4,210,066,000</u>
<b>FUNDS WERE USED FOR:</b>		
Purchases —		
Marketable debt securities	4,028,815,000	3,454,402,000
Conventional mortgages	18,471,000	10,681,000
Preferred and common stock	539,517,000	365,464,000
Real estate equity pools	32,500,000	7,500,000
Participating real estate mortgage		8,000,000
Limited real estate partnership	25,000,000	
General real estate partnerships	51,794,000	
Property and equipment	309,000	7,000
Alaska certificates of deposit	107,500,000	
Total purchases	<u>4,803,906,000</u>	<u>3,846,054,000</u>
Provision for decrease in value of common stock		20,871,000
Provision for increase in value of common stock	20,871,000	
Payments to the State of Alaska	155,130,000	237,265,000
<b>Total funds used</b>	<u>4,979,907,000</u>	<u>4,104,190,000</u>
Net change in funds	<u>\$ (116,681,000)</u>	<u>\$ 105,876,000</u>
<b>SUMMARY OF CHANGES:</b>		
Increase in cash	\$ 619,000	\$ 76,000
(Decrease) increase in repurchase agreements	(117,300,000)	105,800,000
<b>Net change in funds</b>	<u>\$ (116,681,000)</u>	<u>\$ 105,876,000</u>

See accompanying notes to financial statements

## NOTES TO THE FINANCIAL STATEMENTS

### JUNE 30, 1985 AND 1984

#### 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. 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, to manage the investments of the Permanent Fund. By law, a portion of the annual earnings is made available to the state for the payment of dividends, and a portion of the annual earnings is contributed to the principal of the Permanent Fund sufficient to offset the impact of inflation. The balance is retained by the Corporation in a reserve for future inflation and dividends account.

#### 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, excluding unrealized gains and losses, be made available for the payment of dividends 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 1984 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:

Type	Basis
Marketable debt securities	Cost adjusted for amortization of premiums and accretion of discounts
Preferred and common stock	Lower of cost or market
Real estate	Market
Conventional mortgages	Cost
Alaska certificates of deposit	Cost

Real estate investments are carried at cost until independent appraisals are made. The carrying value is then adjusted to reflect market value as determined by the independent appraisals.

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 for-

mat. This restatement has no effect on previously reported earnings.

### 3. MARKETABLE DEBT SECURITIES:

The estimated market value of investment securities at June 30, 1985 and 1984 are as follows:

	June 30,	
	1985	1984
Repurchase agreements	\$ 7,300,000	\$ 124,600,000
Short-term issues	55,483,000	332,057,000
Intermediate and long-term issues	5,720,038,000	4,245,140,000
	<u>\$5,782,821,000</u>	<u>\$4,701,797,000</u>

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

### 4. PREFERRED AND COMMON STOCK:

At June 30, 1985, the investment in preferred and common stock was valued at cost which was lower than market. The aggregate market value of the investment on that date amounted to \$838,765,000, which represents a total unrealized gain of \$91,462,000.

At June 30, 1984, the investment in common stock was valued at market which was lower than cost. The aggregate cost of the investment on that date amounted to \$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.

### 5. REAL ESTATE:

The Corporation has purchased certain real estate investments. The underlying properties constituting these investments include but are not limited to, office buildings and shopping malls. Certain terms unique to these various investments are as follows:

#### Equity Pools —

An independent appraisal of the properties of one real estate pool (CPI) was completed on December 31, 1984. The appraisal

indicated a 15.6% increase in net asset value or \$11.69 per common share — a total unrealized gain for the Corporation of \$3,898,000. At June 30, 1985, the investment was valued at market as determined at December 31, 1984.

#### Participating Real Estate Mortgage —

The investment in a participating real estate mortgage conveys an undivided interest in real property acquired in connection with a loan made on and collateralized by certain real estate. Future adjustments to market value will be determined by the combined total of (i) an independent 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% per annum and a service fee of 1% 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 or federal law.

#### Limited Partnership —

The Corporation will participate to the extent of its percentage of ownership in future net cash flow derived from leasing the properties. The general partner may call for an additional one-time capital contribution from the Corporation of up to \$1,250,000.

#### General Partnerships —

The Corporation will participate to the extent of its percentage of ownership in future net cash flow derived from leasing the properties. Additional contributions to capital shall only be made by agreement of all the partners and in proportion to their respective partnership interests. Responsibility for property and investment management of the partnerships is vested in real estate advisors under contract to the Corporation. Investment management fees are shown as period expenses of the Corporation.

## 6. INCOME DISTRIBUTABLE TO THE STATE OF ALASKA:

Income distributable to the State of Alaska is that portion of net income for the years ended June 30, 1985 and 1984 which has been appropriated by the legislature for the payment of dividends. The activity for the years ended June 30, 1985 and 1984 is summarized as follows:

	<u>Total</u>	<u>Dividend Fund</u>	<u>General Fund</u>
<b>Balance due, June 30, 1983</b>	<b>\$ 217,410,000</b>	<b>\$ 107,875,000</b>	<b>\$ 109,535,000</b>
Add: 1983 supplemental appropriation	11,869,000	11,869,000	
1984 appropriation	<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>
<b>Balance due, June 30, 1984</b>	<b>155,130,000</b>	<b>155,130,000</b>	
Add: 1985 appropriation	217,274,000	217,274,000	
Less: Cash transfers —			
Applicable to 1984	<u>(155,130,000)</u>	<u>(155,130,000)</u>	
<b>Balance due, June 30, 1985</b>	<b><u>\$ 217,274,000</u></b>	<b><u>\$ 217,274,000</u></b>	<b><u>\$</u></b>

## 7. CONTRIBUTED EQUITY:

The principal balances of the Alaska Permanent Fund at June 30, 1985 and 1984 are as follows:

	<u>June 30,</u>	
	1985	1984
Dedicated state revenues	<b>\$ 2,424,244,000</b>	\$ 2,056,217,000
Appropriations from the state	<b>2,700,000,000</b>	2,400,000,000
Provision for inflation	<b>616,697,000</b>	382,127,000
Citizen contributions	<b>1,000</b>	
	<u><b>\$ 5,740,942,000</b></u>	<u><b>\$ 4,838,344,000</b></u>

## 8. RESERVE FOR INFLATION AND DIVIDENDS:

The trustees of the Permanent Fund have designated the balance of the undistributed income account 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.

## 9. INCOME BY SOURCE:

### Interest —

Interest income was provided by the following investments during the fiscal years ended June 30, 1985 and 1984:

	<u>1985</u>	<u>1984</u>
Securities purchased under agreements to resell	\$ 6,073,000	\$ 14,766,000
Commercial paper	1,165,000	2,280,000
Bankers acceptances	1,274,000	819,000
Certificates of deposit		
Alaskan banks	9,643,000	
Other	2,537,000	14,418,000
U.S. Treasury bills	4,269,000	19,353,000
U.S. Treasury notes and bonds	576,757,000	461,595,000
Corporate bonds	3,290,000	2,532,000
Money market accounts	2,325,000	1,755,000
Conventional mortgages	5,709,000	4,831,000
Participating real estate mortgage	910,000	138,000
Leases	69,000	21,000
	<u>\$ 614,021,000</u>	<u>\$ 522,508,000</u>

### Dividends —

Dividends income was provided by the following investments during the fiscal years ended June 30, 1985 and 1984:

	<u>1985</u>	<u>1984</u>
Preferred and common stock	\$ 23,367,000	\$ 6,779,000
Real estate equity pools	1,958,000	345,000
	<u>\$ 25,325,000</u>	<u>\$ 7,124,000</u>

### Fees on Loaned Securities —

The Corporation earned the following fees from loaning portfolio securities during the fiscal years ended June 30, 1985 and 1984:

	<u>1985</u>	<u>1984</u>
U.S. Treasury notes and bonds	\$ 1,849,000	\$ 394,000
Preferred and common stock	11,000	
	<u>\$ 1,860,000</u>	<u>\$ 394,000</u>

### Earnings on Real Estate Partnerships —

The Corporation participated in the following net cash flows derived from equity real estate partnerships during the fiscal year ended June 30, 1985:

Limited partnership	\$ 1,211,000
General partnerships	1,411,000
	<u>\$ 2,622,000</u>



