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Growth | Change | Prosperity

The Alaska Permanent Fund (Fund) is an investment savings account that belongs to the State of Alaska. It was created in 1976 by a voter-approved amendment to the Alaska Constitution. The beneficiaries of the Fund are the State of Alaska and all present and future generations of Alaskans.

The Permanent Fund is made up of two parts: reserved (principal) and unreserved (realized income). The reserved portion of the Fund is invested permanently and cannot be spent without amending the state constitution through a majority vote of the people. Decisions about uses of the unreserved portion are made each year by the people's elected representatives – the Alaska State Legislature and the Governor. The Alaska Permanent Fund Corporation (AFPC) manages the Fund.



Letter from the Chair



Board of Trustees from front left to right:

- Chair Carl Brady
- William A. Corbus
- Vice Chair Steve Frank
- Bill Hudson
- Eric E. Wohlforth
- David Márquez

- Growth
- Change
- Prosperity

On behalf of the Board of Trustees, I am pleased to bring you the fiscal year 2005 annual report of the Alaska Permanent Fund Corporation.

This has been a year of growth, change and prosperity for the Permanent Fund. We've seen changes in how we manage our assets, creating the small-cap manager program in our equities portfolio and granting limited discretion to our real estate managers to purchase properties on our behalf. We have also added a secondary consultant pool to ensure that the Trustees have all of the information needed to make sound investment decisions for the Fund.

We welcomed David Márquez, Alaska's Attorney General, to the Board of Trustees this year. Having the state's Attorney General on the Board of Trustees is a great advantage to the Permanent Fund. In addition to our regular counsel, the Attorney General adds depth in legal guidance and opinion.

The greatest change was created by the passage of House Bill 215. This bill allows the Trustees to use the prudent investor rule as the guideline for investments of the Fund. As the most significant change in the Fund's operations since the corporation was created in 1980, it will allow the Trustees to implement new investment strategies in a timelier manner.

The Fund has grown and prospered this year. It was exciting to reach \$30 billion for the first time in the Fund's history. Earlier this decade, during the bear markets, our decision to hold the course in our investment allocation has paid off with our stock portfolios continuing to significantly contribute to this year's strong annual return.

Looking to the future, there are changes that still need to be made, most importantly the transition to a payout based on a percent of the Fund's market value. The Board of Trustees continues to support this as the only way to ensure that the Fund is adequately protected for the future. This change will also allow the alignment of the Fund's investment strategies with the Fund's payout method. To this end we have

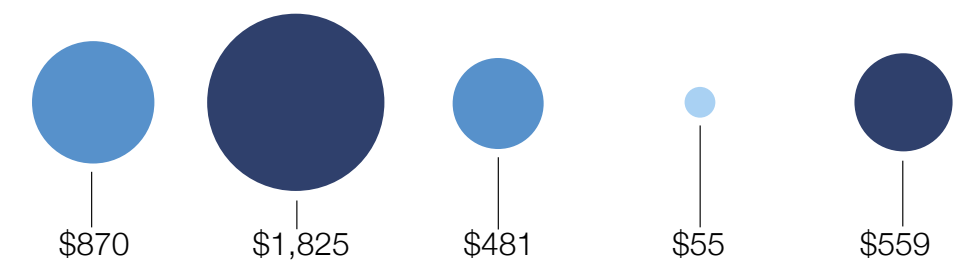
introduced resolutions in both bodies of the Legislature to place the necessary proposition on the next general election ballot.

Next year is the Permanent Fund's 30th anniversary. As we look forward to that milestone, we should take time to reflect on the decisions that have been made along the way to create the prosperous fund that we have today. We stand on the shoulders of those who have helped create the framework and managed the Fund: governors, legislators, trustees and staff. We have many and much to be thankful for.

Sincerely,

Carl Brady, Chairman
Board of Trustees

Sources and uses in fiscal 2005 in millions



Sources

Stock dividends, bond interest and real estate cash flow	\$870
Net increase in fair value of investments	\$1,825
Dedicated mineral revenue	\$481

Uses

Operating costs and other legislative appropriations	\$55
Transfers out (dividend distribution and Capital Income Account)	\$559



Letter from the Executive Director



Fiscal year 2005 was a second consecutive year of strong growth for the Permanent Fund after the bear markets of a few years ago. The Fund had a total return of 10.4 percent, and a real rate of return of 7.7 percent, after accounting for inflation. This is in line with our benchmark return of 10.5 percent for the same period. The Fund ended fiscal 2005 with a balance of \$29.96 billion on June 30.

All of the Fund's asset classes showed positive returns for the year. The real estate portfolio led with a greater than 27 percent return, while overseas investments in bonds and stocks returned 10 percent and 15 percent respectively. US bond and stock investments also performed well, each returning about 7 percent. Additional information on the performance of each asset class and changes in the portfolios is available in this report.

While the Fund had a strong return overall, the entire fiscal year was not characterized by growth. First quarter returns were low in most markets, and the Fund's US stock portfolio lost almost 3 percent. Following the November elections, the US and overseas stock markets rallied, carrying the Fund to \$29 billion for the first time in four years. The Fund ended the calendar year even higher, at just under \$30 billion.

In the third quarter, Fund performance took a downward turn. All of the portfolios provided negative returns with the exception of essentially flat performance in the overseas stock portfolio and strong returns for the Fund's real estate holdings. A modest upturn in all markets in the 4th quarter improved the Fund's final return and brought the total value back to just under \$30 billion after dividends were paid.

The Permanent Fund continues its focus on the long term, while attempting to minimize the short-term impact of market swings.

Closer to home, the Permanent Fund is pleased to introduce three new staff members who joined us this year. Our newest additions are Eric Richter, Fixed Income Investment Officer, Jiangning (Jennifer) Ma, Equity Investment Analyst and Kaitlin Kreuzenstein, Receptionist. I am pleased to have them on board and wish them success in their careers at APFC.

It was just a year ago that I, myself joined the APFC. I am privileged to have been here to witness a significant change for the Fund – the removal of the statutory investment list by the Legislature this spring. This change will bring significant challenges for the staff as we draft new investment regulations and contemplate how to

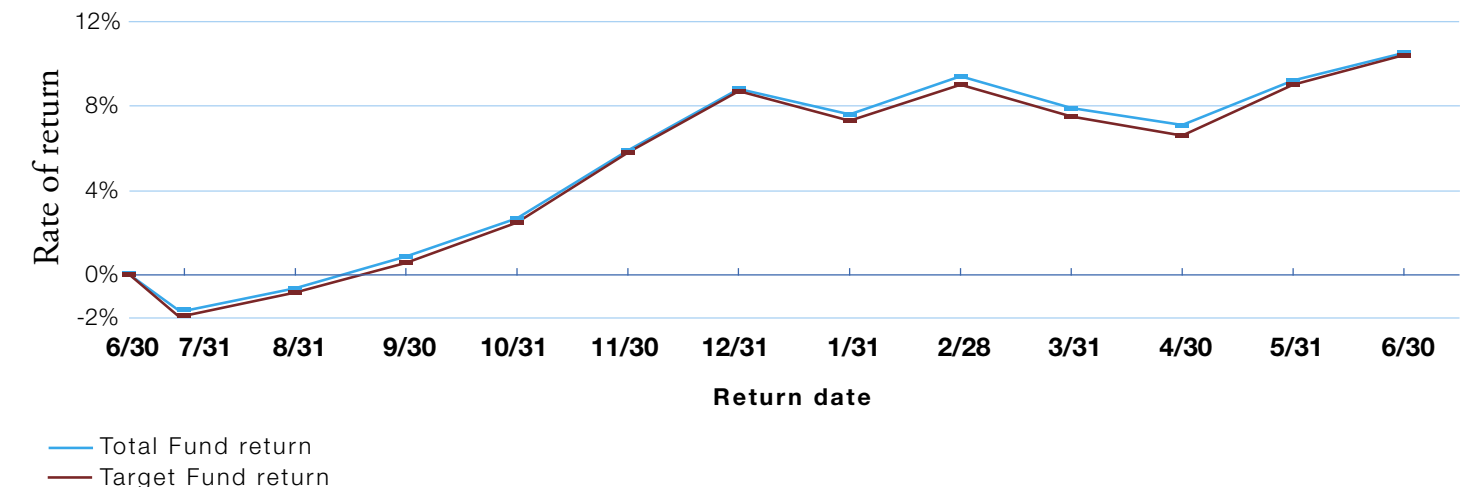
best implement the new responsibility that we have been granted. We have undertaken additional research into investment options – some new, some old – and are determining new ways of limiting investment risk in a portfolio bound by the traditional guidelines of the prudent investor rule.

As I have had a chance to get to know the APFC staff over the last year, I have seen dedicated professionals who work hard and understand their responsibility to the Fund and to the people of Alaska. I am privileged to have joined their ranks. We will continue to take our charge of managing Alaska's Permanent Fund seriously as we look ahead to the coming year.

Sincerely,

Michael J. Burns
Executive Director

Cumulative month-to-month returns FY05





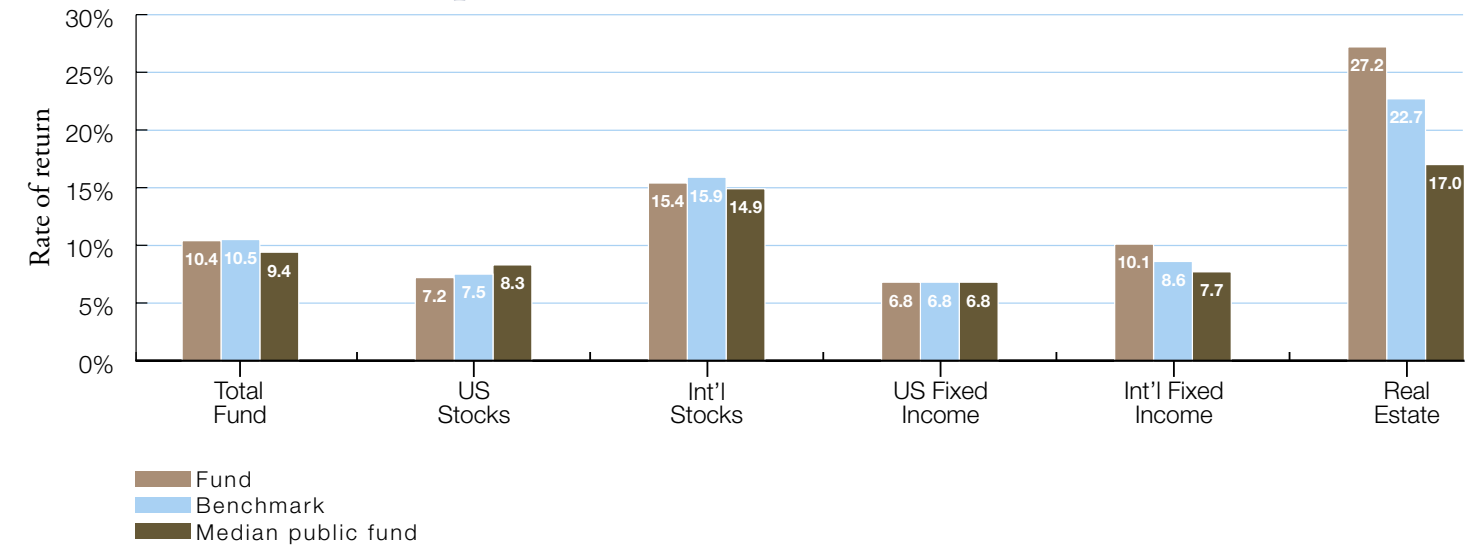
Investing for the long run

To achieve a target total rate of return, the Board of Trustees of the Alaska Permanent Fund Corporation manages risk by strategically allocating the Fund among stocks, bonds, real estate and recently, alternative investments. Different types of assets are influenced differently by factors such as the economic cycle, interest rates, inflation and fiscal policy. A mix of asset types whose returns move out of sync with one another moderates the total Fund's volatility.

Each year the Board fine-tunes its asset allocation to adjust to changes in the market environment. Its current goal is to earn about 5 percent over the rate of inflation in the long run. That means, in any 10-year period, the average real return (the return after inflation) of the Fund should be around 5 percent. The charts below illustrate how the Fund has been doing.

Fiscal 2005 performance

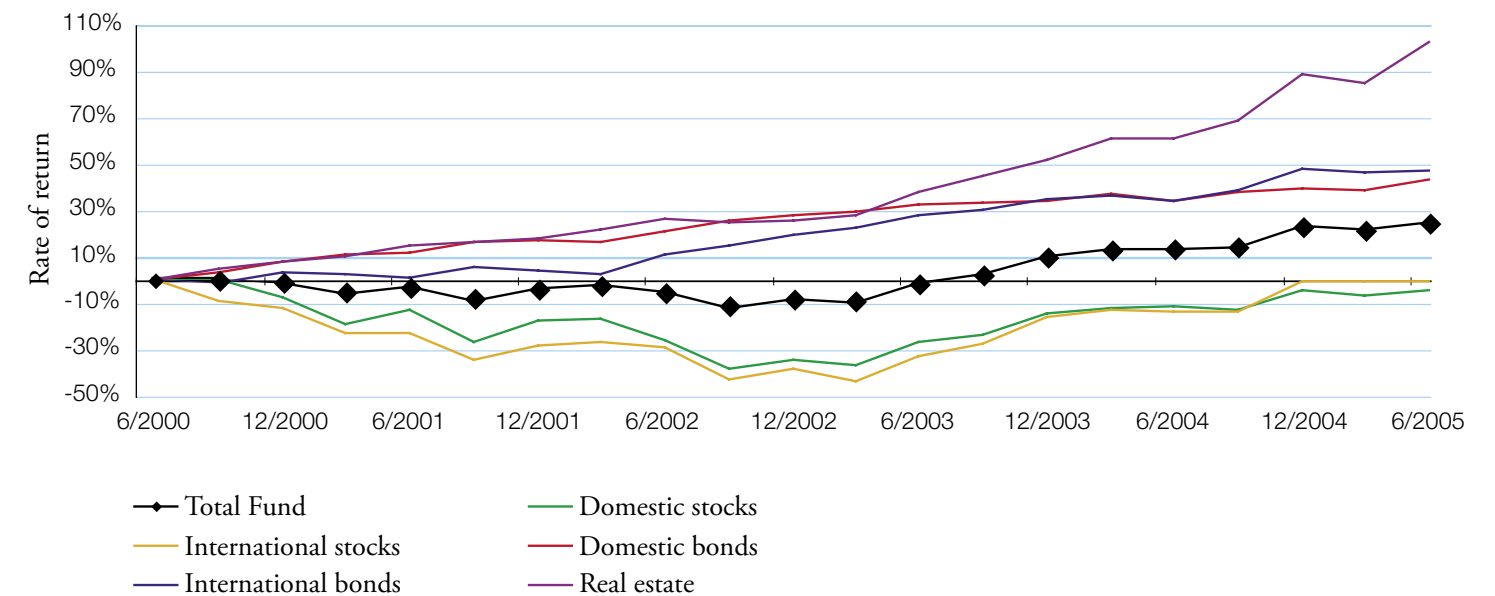
Fund fiscal '05 performance



Diversification

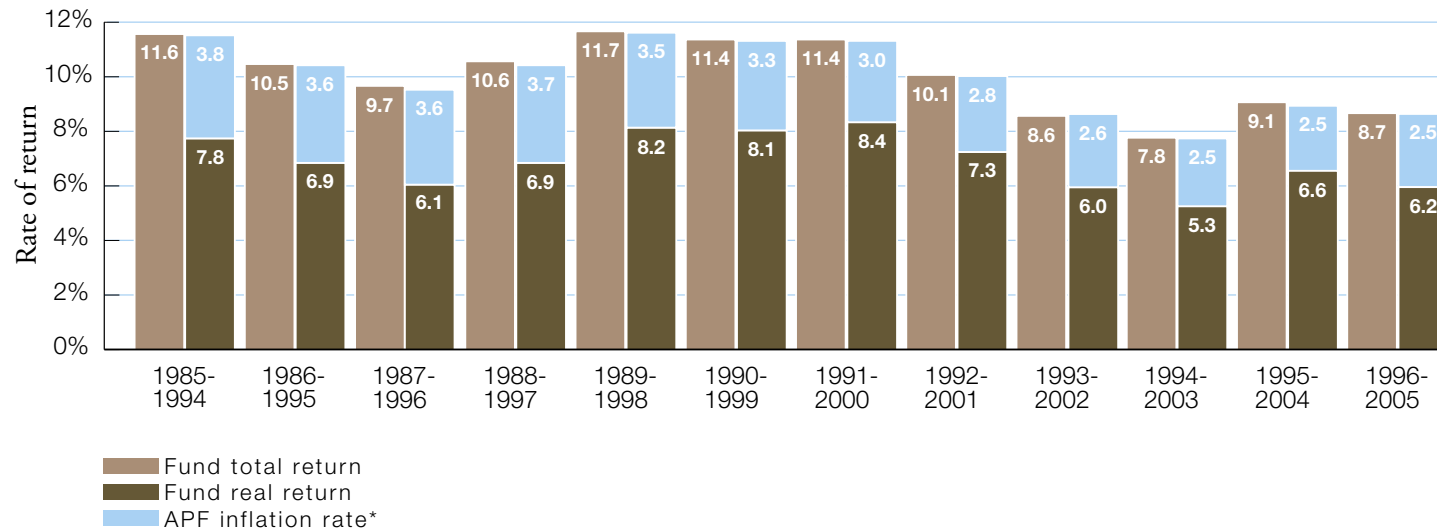
The effect of diversification

Five-year cumulative return



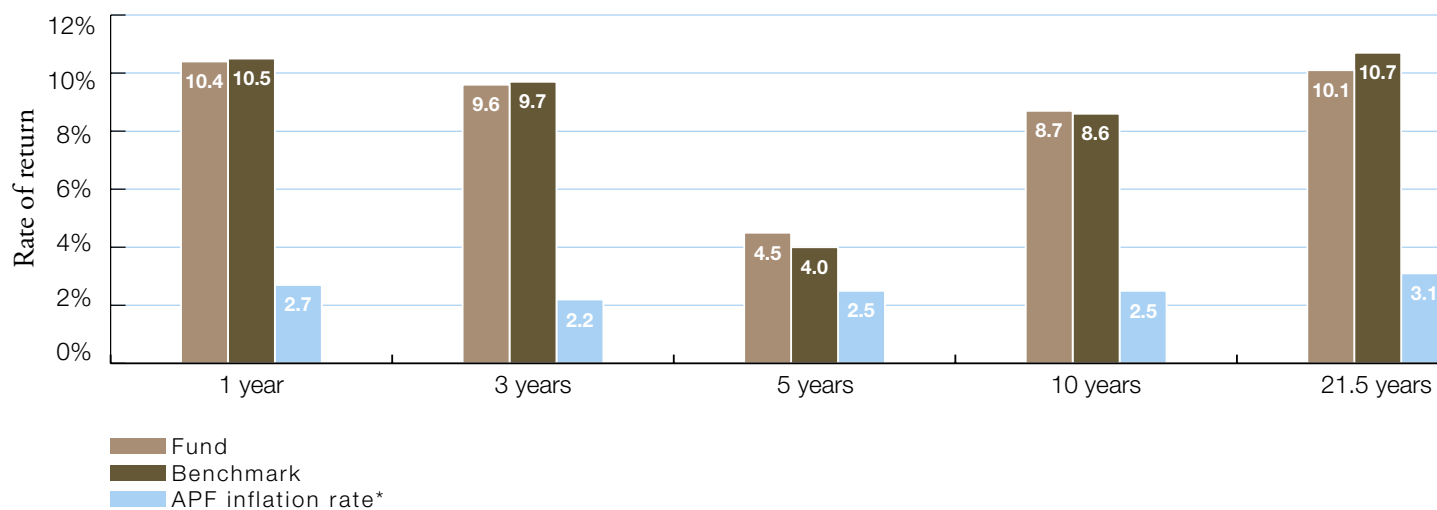
Rolling 10-year returns

Annualized returns for periods ending June 30, 2005



Fund's long-term investment performance

Annualized returns for periods ending June 30, 2005



* See page 30 for detailed information regarding the APF inflation rate



Remembering a father of the Fund Jay Hammond

1922-2005 Jay Hammond was Governor of Alaska from 1974 to 1982. His support was instrumental in encouraging the Legislature and the people of Alaska to pass a constitutional amendment creating the Permanent Fund in 1976. While in office, he also signed into law the bill creating the Alaska Permanent Fund Corporation, to ensure the Fund was managed independently of political pressures.

Governor Hammond is considered by many to be the father of the Permanent Fund Dividend. Not only has this program allowed all Alaskans to share equally in a portion of our state's oil wealth, but it has achieved his goal of making us all keenly interested in the health and protection of the Permanent Fund.

The Alaska of today, and certainly the Alaska of tomorrow, would be vastly different if Governor Hammond had not had the wisdom to tirelessly advocate for the creation of the Permanent Fund. The Permanent Fund lost a friend when Governor Hammond passed away on August 2, 2005.



Governor Jay Hammond signs legislation creating the Alaska Permanent Fund Corporation in 1980.

Stocks

With domestic and international stocks (equities) posting their second consecutive year of positive returns since 1999, the Permanent Fund benefited from its large exposure to the stock markets in fiscal year 2005. At fiscal year end, the Fund had 58 percent of its assets in stocks, on the high side of the allowable range set by the Board of Trustees. The higher exposure reflects both the favorable performance of stocks relative to other asset classes, and a temporary under weighting in private equity investments.

For the year, US stocks measured by the Russell 3000 Index gained 8 percent. Stocks of smaller companies beat those of larger companies again this year, with the Russell 2000 Index of US small-cap stocks returning 9.4 percent. Non-US stocks outpaced domestic stocks, with the MSCI Index for Europe, Asia and the Far East (EAFE) returning 13.6 percent and the MSCI Index for

emerging/developing countries gaining nearly 35 percent. Several factors appeared as key drivers of equity returns this past year. The price of crude rose sharply during the fiscal year, from \$37 to \$57 per barrel. Not surprisingly, oil company stocks benefited from the rise in oil prices and the energy sector was the best performing sector of the S&P 500, returning 39 percent for the year. Utilities were a close second, returning 38 percent.

While short-term interest rates increased, long-term rates fell slightly over the year. This caused investors seeking yield to flock to dividend paying stocks, causing them to outperform.

In the international markets, the UK and continental Europe economies expanded, while China continued to grow, along with its appetite for oil and commodities.

Domestic equity managers

- Alliance Capital Management
- Cordillera Asset Management
- Dodge & Cox Investment Managers
- DuPont Capital Management
- Forstmann-Leff Associates
- GE Asset Management
- Jennison Associates
- Kalmar Investments
- Lazard Asset Management
- Luther King Capital Management
- Martingale Asset Management
- McKinley Capital Management
- Mellon Capital Management
- Penn Capital Management
- Peregrine Capital Management
- RCM Capital Management

- T. Rowe Price Associates
- Tukman Capital Management
- Turner Investment Management
- UBS Global Asset Management
- Voyageur Asset Management
- Washington Capital Management

Non-domestic equity managers

- Capital Guardian Trust Company
- Capital Guardian Trust Company –
Emerging Markets Growth Fund
- Clay Finlay
- Lazard Asset Management
- Mellon Capital Management
- Mondrian Investment Partners
- Schroders Capital Management
- UBS Global Asset Management



Domestic stock portfolio

The Fund's domestic stock portfolio returned 7.2 percent in fiscal year 2005, slightly lagging its benchmark return of 7.5 percent. The small-cap stock portfolio returned 11.6 percent, outpacing the large-cap portfolio, which returned 6.1 percent. Value-style managers, with more exposure to energy and utilities, beat tech-heavy growth-style managers again this year.

Looking toward the future

During this past year, the Board of Trustees made several changes designed to add value to the Fund's domestic stock portfolio.

For the last five years, since the technology bubble burst, the Russell Value Index has returned 6.6 percent, while the Growth Index has returned -10.4 percent on an annualized basis. Given the duration of the performance

gap, and the belief that markets are cyclical in nature, many investors are starting to rebalance their portfolios between value and growth. APFC shifted \$250 million to Alliance Capital, one of the Fund's existing growth managers, from other asset classes. This shift has already started to deliver benefits, as Alliance's portfolio returned 7.0 percent for the 4th quarter and the Fund's overall stock returns improved in the second half of the year compared to the benchmark.

The Board hired GE Asset Management for an existing \$580 million large-cap growth portfolio, with a substantially greater growth orientation than the prior manager. The Trustees also granted additional flexibility to RCM Capital Management to invest a portion of their \$1.3 billion mandate in a concentrated "best ideas" growth portfolio. The Alliance, GE and RCM steps have all been taken in the context of an appropriate balance between value and growth styles.

Recognizing the capacity issues faced by many small-cap managers, and the value-added opportunities among small-cap stocks, the Board created a small-cap manager pool (SCMP) to increase APFC's access to this segment of the equities market. Rather than giving a large mandate to one manager, a pool of 12 managers oversees portfolios ranging from \$60 million to \$152 million, totaling \$940 million. While the Board will monitor the performance of the SCMP as a whole, staff will monitor individual managers in the pool and rebalance among managers as needed.

portfolio returned 16.2 percent, while Schroder's Pacific-Rim portfolio returned 6.4 percent. The Fund's global managers, UBS and Lazard, returned 12.5 percent and 10.5 percent, respectively, outperforming the MSCI World Index return of 10 percent.

The Board hired London-based Mondrian Investment Partners for a \$200 million emerging markets mandate. Together with its investment in the Capital International's Emerging Market Growth Fund, the Fund had \$682 million invested in emerging market stocks as of the fiscal year end, and is slightly above its target allocation of 2 percent.

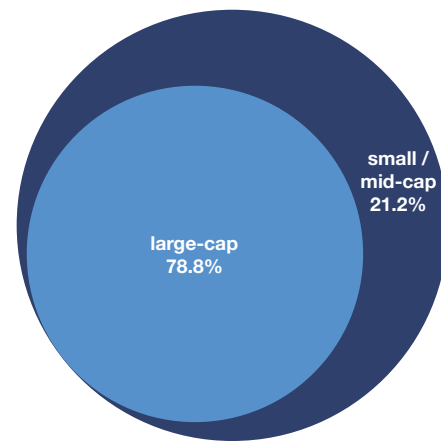
International stocks

The Fund's international stock portfolio returned 15.4 percent, with the developed countries portfolio returning 13.7 percent and the emerging countries portfolio returning 33 percent. Reflecting sharp differences in regional performance, Clay Finlay's European growth

Domestic stock diversification

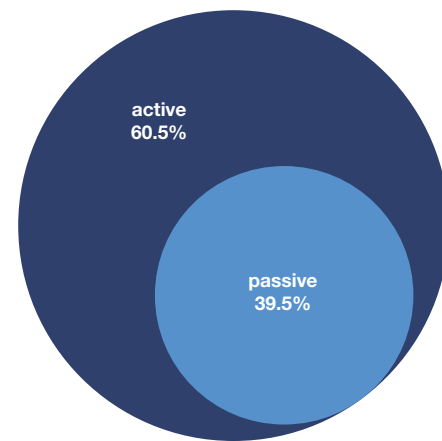
Two views of the \$11.9 billion portfolio, as of June 30, 2005

by large- v. small-cap



large-cap	small/mid-cap	total value
\$9.4 billion	\$2.5 billion	\$11.9 billion

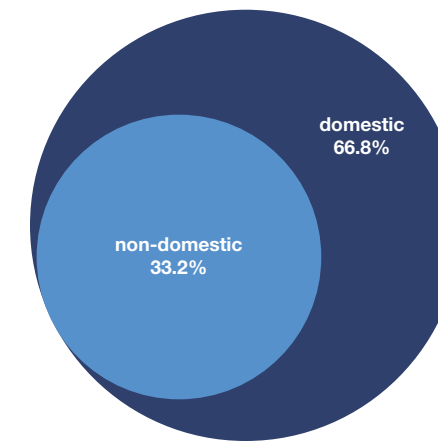
by active v. passive management styles



active	passive	total value
\$7.2 billion	\$4.7 billion	\$11.9 billion

Stock diversification

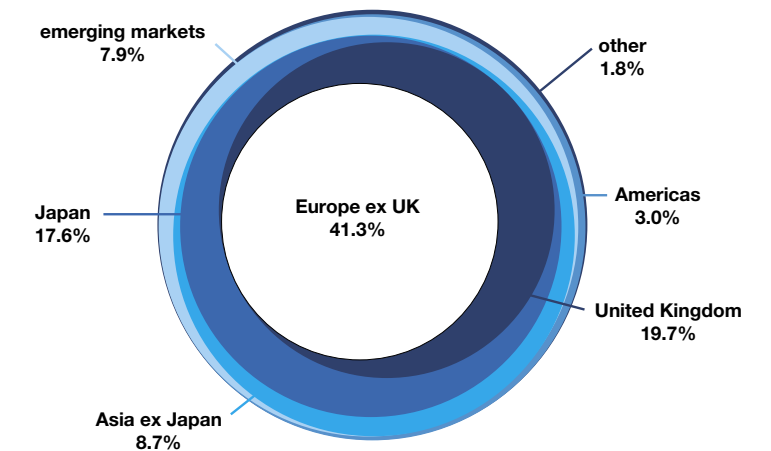
by region as of June 30, 2005



total value
\$17.8 billion

Non-domestic stock diversification

by region as of June 30, 2005



total value
\$5.9 billion



Bonds

Fiscal year 2005 was the tenth consecutive year of positive bond (fixed income) returns, with both the domestic and international portfolios showing strong performance. The 6.8 percent return for the Lehman Brothers Aggregate Index was a particularly pleasant surprise given the low starting yields at the beginning of the fiscal year.

The Fund's bond portfolio ended June 30, 2005 with a value of \$9.6 billion. APFC fixed income staff internally managed \$7.4 billion of the \$8.3 billion domestic portion of the portfolio. The internal portfolio returned 6.8 percent, matching the index. UBS Global Asset Management (UBS) and Alaska Permanent Capital Management (APCM), returned 6.4 percent and 6.6

percent respectively. In anticipation of higher rates, all of our managers maintained portfolio durations shorter than that of their benchmark for much of the year.

In February, Federal Reserve Board Chairman Alan Greenspan characterized the unanticipated behavior of the bond markets as "a conundrum." Because of steady growth in the economy, the Fed increased the federal funds rate by a quarter of a percent eight times during the fiscal year, ending the year at 3.25 percent. Despite the increase in short-term rates, long-term rates actually declined for the year. At the beginning of the fiscal year, the difference in yield between the six-month Treasury bill and the 30-year Treasury bond was 3.66 percentage points versus .86 percentage points at the close of the

year. This flattening of the yield curve was the largest single determinant of positive performance for core fixed income managers.

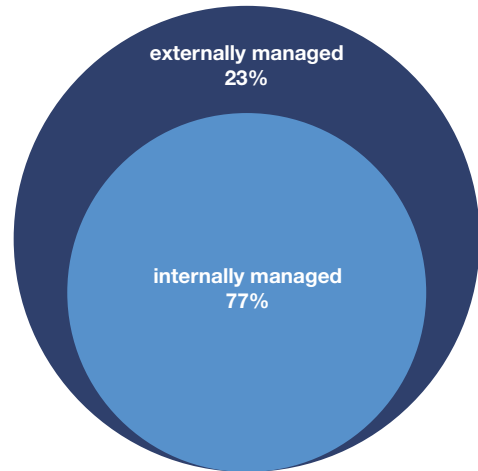
One possible cause of this unexpected result for bond performance was a substantial increase in demand from foreign sources for US fixed income assets, driven by the burgeoning current account deficit. The opposing market forces of the Fed raising rates and foreign central banks appetite for longer dated bonds caused the yield curve to flatten dramatically.

Corporate bonds continued to perform well due to strong earnings and supply/demand dynamics. Mortgage-backed securities also outperformed similar duration treasury notes.

The APFC's two international bond managers each outperformed their index in fiscal year 2005. The benchmark, Salomon Brothers World Government Bond Index, which is adjusted for a 50 percent hedge on foreign currencies, returned 8.64 percent versus the Fund's managers, Julius Baer and Rogge Asset Management's returns of 10.4 percent and 9.8 percent respectively. Both managers benefited from the dollar weakening versus other currencies through the fiscal year, and the portfolio ended the fiscal year with a value of \$1.3 billion.

Bond diversification

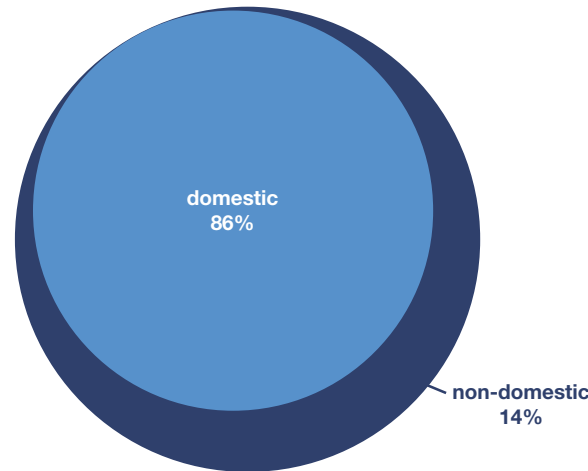
by internal v. external management as of June 30, 2005



externally managed	internally managed	total value
\$2.2 billion	\$7.4 billion	\$9.6 billion

Bond diversification

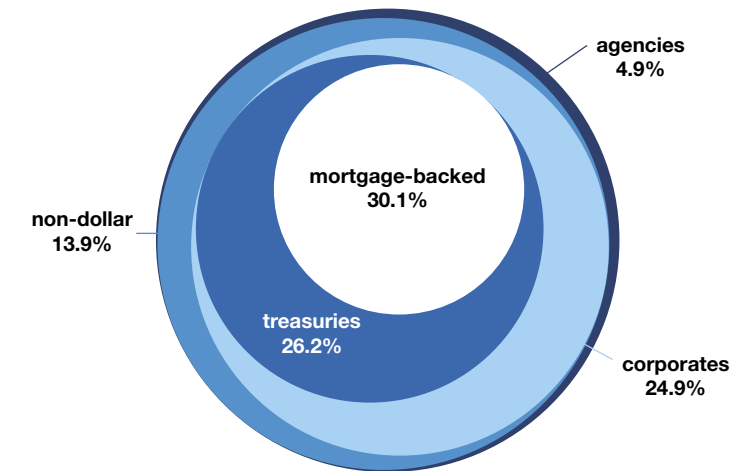
by region as of June 30, 2005



domestic	non-domestic	total value
\$8.3 billion	\$1.3 billion	\$9.6 billion

Bond diversification

by type as of June 30, 2005



corporates	treasuries	non-dollar
\$2.2 billion	\$2.4 billion	\$1.3 billion
mortgage-backed		agencies
\$2.7 billion		\$440 million

Domestic bond managers

Alaska Permanent Capital Management
APFC Internal Fixed Income Account
UBS Global Asset Management

Non-domestic bond managers

Julius Baer Investments Limited
Rogge Global Partners



Real estate

As of June 30, 2005, the APFC's real estate portfolio had a total value of \$3.0 billion and a total return of 27.2 percent. The public equity portion of the portfolio returned a remarkable 37.2 percent, well above the Morgan Stanley REIT Index benchmark return of 32.9 percent, ending the fiscal year with a value of \$1.2 billion.

The direct equity portfolio provided a 20.7 percent return, beating the NCREIF NPI benchmark return of 18.0 percent and ending the year with a value of \$1.8 billion. It is important to note that a meaningful portion of this strong return came from the revaluation of one existing property: the shopping center Tyson's Corner, near Washington, D.C.

The task for fiscal 2005 was to bring the real estate portfolio, which started the year at 7.8 percent, closer to its target allocation of 10 percent of the Fund. Two things helped the real estate investments staff meet this goal: a larger than anticipated increase in the market value of existing holdings and a program designed to enhance the purchase of new properties.

In July 2004, the Board of Trustees granted discretion to specific external real estate managers to purchase property on the Fund's behalf. Because of the highly competitive real estate markets, requiring the managers to obtain approval at every step of the real estate transaction was limiting the APFC's effectiveness in acquisitions, without enhancing the quality of decision-making. Under the new discretionary program, all purchases must meet the specifications of

the corporation's annual tactical plan, which imposes limits on manager discretion including factors such as property type, geography, and acquisition price. In return for discretionary flexibility, the program raises the accountability of managers for the properties they commit to and manage on behalf of the APFC.

The Board-designated Strategic Investment Managers – L&B Realty, LaSalle Investment Management, Sentinel Realty Advisors, CB Richard Ellis Investors and Kennedy Associated Real Estate Counsel – have been actively identifying possible acquisitions for the APFC. Every manager has presented potential transactions to the APFC since the discretionary program was created. The APFC has acquired 9 new assets under this program for a total of \$336.5 million.

The discretionary program has proven very successful in increasing the APFC's real estate exposure, and staff believes the program has made the relationship between the Fund and its managers more effective overall.

Real estate markets remain highly competitive with an unprecedented level of capital flowing into the asset class. Due to this, and the fact the APFC has reached its real estate target of 10 percent, next year's plan for real estate involves managing and repositioning the portfolio. This will include a focus on selective dispositions, as well as adding new properties to enhance the diversification of the overall portfolio.

Real Estate Investment Trust (REIT) advisors

- AEW Capital Management (Focus Group)
- AEW Capital Management (REITs)
- Wellington Management Company

Private equity real estate advisors

- CB Richard Ellis
- Kennedy Associates
- L&B Realty Advisors, Inc.
- LaSalle Investment Management
- Sentinel Realty Advisors, Inc.

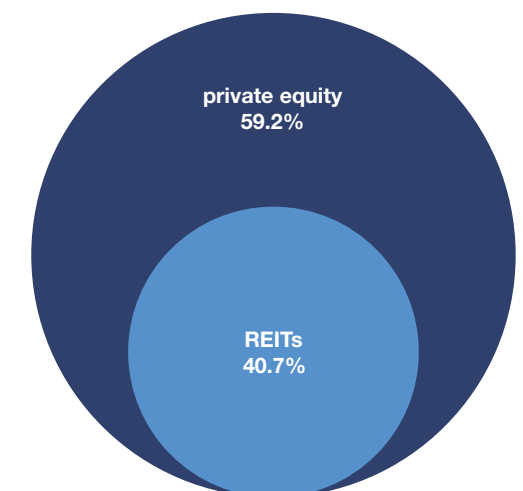


The Maui Marketplace in Kahului, Hawaii is part of the APFC's \$3 billion real estate portfolio.



Alaska Permanent Fund Corporation headquarters in Juneau, one of APFC's Alaska real estate investments.

Real estate diversification as of June 30, 2005



private equity	REITs	other
59.2%	40.7%	.1%

total value
\$3.0 billion



Alternative investments

The definition of alternative investments is not yet standardized within the industry. For some, the term applies to anything that is not stocks or bonds; others view it as encompassing anything that is not a traditional asset class found in most public plans. Depending on the definition of alternatives, the APFC is either new to the asset class this past fiscal year, or it is a very experienced alternatives investor given its long-standing 10 percent allocation to real estate.

The Fund defines alternatives as investments other than traditional stocks, bonds and real estate. However, the definitions of many assets and strategies seem to be in a prolific state of evolution at the moment. Regardless of definition, we are focusing on evaluations of the opportunity provided by an asset or a strategy to enhance the overall Fund.

With this in mind, the APFC Trustees made initial allocations last year to both private equity (2 percent of Fund assets) and absolute return (1 percent). In each case, policies were developed, manager searches conducted by the Board's consultant, managers selected and, where appropriate, tactical plans were drafted and adopted. Managers were funded, and we have the early results of these diversification efforts.

Private equity. The Fund selected Pathway Capital Management of Irvine, CA as its private equity "gatekeeper." Pathway's mission is to select private equity limited partnership investments for the Fund in compliance with Board adopted guidelines and annual tactical plan. These investments will be diversified among many partnerships investing in such strategies as large, mid-sized and small company buyouts, as well as all stages of venture capital, distressed debt and other

Alternative investments managers

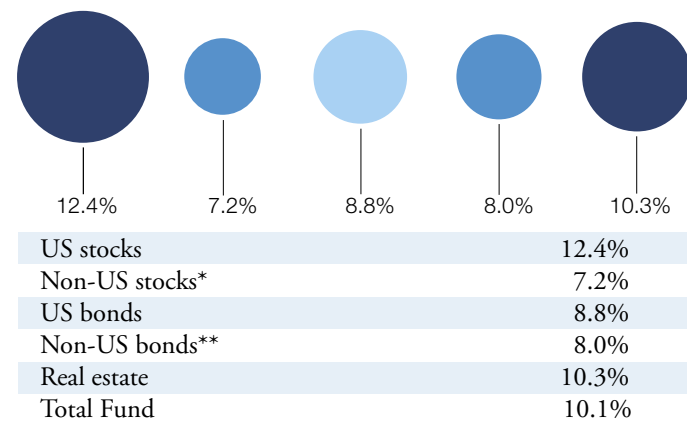
Crestline Investors, Inc.
Pathway Capital Management

strategies. While approximately \$300 million has been committed to limited partnerships since inception, the amounts actually funded are small and the performance is not yet a meaningful statistic.

Absolute return. The Fund also hired Crestline Investors, Inc. to create a separate limited partnership consisting of investments in a diversified portfolio of hedge fund strategies. This type of arrangement is sometimes referred to as a "fund-of-funds." The term is not precise since, at this time, the APFC is the sole limited partner in this partnership. The partnership has approximately 14 separate strategies, diversified across more than 30 managers, targeting a bond-like return with bond-like expected volatility. While individual strategies may be more volatile than traditional asset classes, the combined effect of the strategies is intended to result in muted outcomes that are not highly correlated to more traditional asset classes. Crestline's performance for the three calendar quarters since funding was 5.3 percent versus a benchmark target of 4.9 percent.

Fund cumulative return for major asset classes

last 21.5 years, annualized, as of June 30, 2005



The Fund has not been invested in all asset classes for the full 21.5 year period
* 10-year returns
** 5-year returns

Legislation

In the spring of 2005, the Alaska State Legislature authorized the Board of Trustees to move the list of the Permanent Fund's allowed investments from statute to regulation, the most significant change to the Fund since the creation of the corporation in 1980. The new regulations will take effect on January 1, 2006.

The constitution specifies that the Fund may only be invested in assets "specifically designated by law." The Legislature interpreted this to mean that a list of allowed investments should be maintained in statute. At the time the list was created in 1980, it was accepted practice to limit investment risk for a fund based on the individual risk profile of each asset type. In addition to listing allowed investments, the statutes also placed limits on the Fund's allocations to some assets, including stocks.

Over the years the Trustees approached the Legislature for greater investment authority, requesting the ability to make new investments or to make greater allocations to existing assets. A legislative change can be a lengthy process, often requiring two to four years to complete.

Modern investment theory focuses on the combined risk of a total portfolio, rather than the risk of each asset type. The majority of large institutional funds now invest under the guidelines of the prudent investor rule, diversifying their investments among assets that respond differently to similar market conditions. Over time, this will better ensure a positive return for the Fund and lower overall risk.

In December, 2004, the Board asked two consulting firms, Callan Associates and RV Kuhns, to review the impact of the statutory list's restrictions on the Fund's investment risk and returns. What both firms found is that the Fund might have been taking on greater risk

without the promise of commensurate returns due to the investment restrictions in state statutes. It became clear that the Trustees needed the ability to manage the Fund's asset allocations under the guidelines of the prudent investor rule, without the limitations of a statutory list.

Representative Norman Rokeberg of Anchorage had been a long-time champion for allowing the Board of Trustees greater investment authority. He sponsored the necessary legislation, along with co-sponsors Representative Ethan Berkowitz and Representative Mike Hawker.

House Bill 215 changed Alaska statutes to require the Board to maintain a list of allowed investments in regulation, while keeping the statutory requirement that all investments conform to the prudent investor rule. The bill passed the House on April 19 with a vote of 30-8, and passed the Senate on May 8 with a vote of 17-2. Governor Frank Murkowski signed HB 215 into law on June 25, 2005.

Giving the Board this flexibility allows it to better balance the Fund's investment risk and return. This also allows the Trustees to gain the full benefit of the investment professionals, managers and advisors who work for the Alaska Permanent Fund Corporation.



Seth Holden of UAA interned with McKinley Capital Management in Anchorage, summer 2005.



UAA graduate Esa Wiegert interned at Alaska Permanent Capital Management in Anchorage, summer 2005.

Commitment to Alaskans

With the oil pipeline “boom” some 30 years behind us, Alaskans are working hard to find ways to grow our economy. In keeping with this spirit, the APFC Trustees take a value-added approach to Fund management in their role as fiduciaries of one of the largest savings accounts of its kind in the world.

Alaska investment law and policy

State law provides that the Permanent Fund will prioritize in-state investments that are comparable in expected risk and return to their alternatives, and are within the allowable types of assets set out in state law. In support of that goal, the Board has set a policy to ensure that it is aware of all potential Alaska real estate and other Alaska investment opportunities. Additionally, the policy formally endorses that the APFC’s management firms hire qualified Alaska students as summer interns. Another Board policy supports the APFC fostering interaction and relationships between the international business and investment community and Alaska government and business. These policies have resulted in several formal programs at the APFC:

- **Alaska real estate investments**

The APFC’s Alaska investment policy provides that one of its real estate managers be designated the “Alaska Manager.” The Alaska Manager focuses on finding opportunities for the Fund to invest in Alaska properties that fit within the parameters of the APFC’s investment strategy. Kennedy Associates Real Estate Counsel of Seattle is the Fund’s Alaska Manager. Kennedy has helped the APFC to identify Plaza Port West in Ketchikan and Goldbelt Place in Juneau for the Permanent Fund’s real estate portfolio. In addition to keeping up with the Alaska real estate market, Kennedy has been the foremost participant among the Fund’s managers in hiring Alaska student interns. Since the program began in 1988, Kennedy has hired a total of 20 APFC program interns in its Seattle and Bethesda offices. Kennedy has also hired several interns on a permanent basis, including Mark Reinikka, the first intern in this program.

- **APFC summer intern program**

The APFC and its participating management firms offer internships exclusively for qualified students attending school in Alaska and Alaskans attending school out

of state. Each February, the APFC posts recruitment bulletins on apfc.org for its summer internships. In 2005, four students from UAA, seven from UAF and four Alaskans attending school out of state were hired to work for the APFC or our partner firms.

- **Energizing the economy: lending money to Alaska banks**

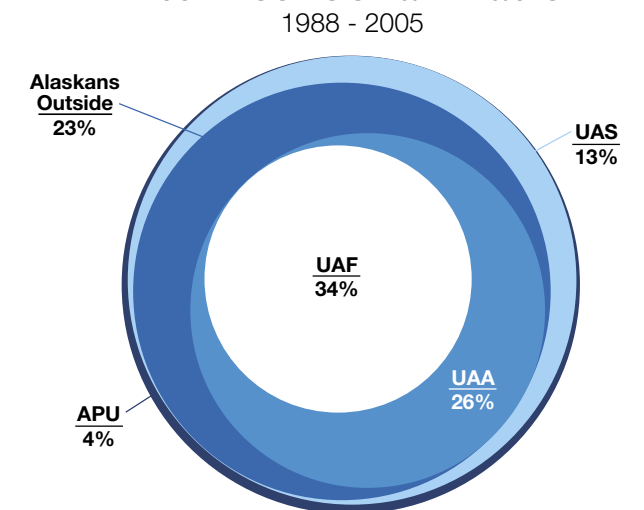
Alaska banks that wish to increase the amount of money they have available for loan programs may purchase certificates of deposit from the APFC at competitive interest rates. As part of a diversified investment strategy, APFC Trustees make up to \$300 million available for this CD program annually. This fixed income investment provides a low risk revenue stream for the Permanent Fund and contributes to the amount of business loan capital available to Alaskans – a win-win arrangement. Wells Fargo Bank and Northrim Bank both invested in the APFC CD program in fiscal year 2005.

Adding more value: managing Fund money in Alaska

Managing a fund worth over \$30 billion involves a lot of players, and the Trustees ensure that Alaskans have a role. The APFC employs 32 people – all in Alaska – including 10 investment officers and analysts. The

Corporation has also issued portfolios to McKinley Capital Management and Alaska Permanent Capital Management – both based in Anchorage. Incidentally, both of these companies hired Alaska student interns in 2005, contributing yet more value to our state.

Intern school affiliation



Number of interns	APU	UAS	UAA	UAF	Alaskans attending school Outside
	8	28	58	78	52



Management's Discussion and Analysis

This annual report has three integral parts: the narrative with charts and graphs preceding the financial statements, this Management's Discussion and Analysis, and the financial statements with accompanying notes. Together, they present the Alaska Permanent Fund's (Fund's) financial performance during the fiscal years ending June 30, 2005 and 2004. Fiscal year 2003 information also is shown here in the Management's Discussion and Analysis for comparative purposes.

Required financial statements

Governmental Accounting Standards Board statement number 34 requires two financial statements: the Balance Sheet and the Statement of Revenues, Expenditures, and Changes in Fund Balances. These statements report financial information about the Fund's net asset balances and fiscal year activities using accounting principles generally accepted in the United States of America.

Balance sheets

Balance Sheets report assets, liabilities, and fund balances of the Fund as of the specific dates shown.

Assets. Assets represent the value of the Fund's investments on the financial statement dates. Assets are the investments that generate revenue for the Fund, like stocks, bonds and real estate holdings, and also include cash, receivables and prepaid expenses. Cash amounts represent not just cash but also short-term, liquid investments. All assets are valued at their fair market, or recoverable, value as of the dates shown, except private equity real estate holdings which are valued under the equity method of accounting, according to generally accepted accounting principles. The equity method of accounting is defined as historical cost of the asset plus the Fund's portion of the property's undistributed earnings.

Liabilities. Liabilities represent known claims against the Fund's assets, which are paid subsequent to June 30, 2005 and June 30, 2004 respectively.

Fund balances. Reserved fund balances are unavailable for appropriation and include all mineral revenues received by the Fund, inflation-proofing transfers from the realized earnings account and special legislative appropriations. Also included in the reserved fund balances are the accumulated unrealized gains and losses of invested assets, which are not available for appropriation. See 2003 Attorney General Opinion (June 18; 663-03-0153).

The unreserved fund balances (realized earnings) is where all income available for appropriation is recorded, retained and reinvested until distributed in accordance with State of Alaska law. The values shown on this report for the realized earnings are after recording the Fund's fiscal year end financial obligations, primarily the annual dividend transfers and the transfers from realized earnings to the reserved section for safeguarding the accumulated contributions from inflation.

Balance sheets

<i>As of June 30</i>	2005	2004	\$ increase (decrease)	% change	2003
Assets					
Cash	\$ 1,298,571,000	1,496,994,000	(198,423,000)	(13.3)%	637,752,000
Receivables, prepaid expenses and other	648,000,000	243,562,000	404,438,000	166.1	381,587,000
Marketable debt securities	9,006,628,000	9,285,020,000	(278,392,000)	(3.0)	9,082,157,000
Preferred and common stock	17,630,359,000	15,836,268,000	1,794,091,000	11.3	12,750,289,000
Real estate	2,694,595,000	2,086,928,000	607,667,000	29.1	2,057,104,000
Alternative investments	266,000,000	0	266,000,000	100.0	0
Alaska certificates of deposit	157,953,000	172,759,000	(14,806,000)	(8.6)	196,802,000
Securities lending collateral invested	4,569,049,000	1,431,224,000	3,137,825,000	219.2	3,378,416,000
Total assets	\$ 36,271,155,000	30,552,755,000	5,718,400,000	18.7	28,484,107,000
Liabilities					
Accounts payable	1,181,556,000	1,140,445,000	41,111,000	3.6	220,275,000
Income distributable to State of Alaska	558,882,000	581,246,000	(22,364,000)	(3.8)	691,082,000
Securities lending collateral	4,569,049,000	1,431,224,000	3,137,825,000	219.2	3,378,416,000
Total liabilities	\$ 6,309,487,000	3,152,915,000	3,156,572,000	100.1	4,289,773,000
Fund balances					
Reserved - principal					
Contributions and appropriations	24,647,217,000	23,525,752,000	1,121,465,000	4.8	22,988,019,000
Unrealized appreciation on invested assets	3,874,602,000	3,015,548,000	859,054,000	28.5	1,106,315,000
Unreserved					
Realized earnings	1,439,849,000	858,540,000	581,309,000	67.7	100,000,000
Total fund balances	\$ 29,961,668,000	27,399,840,000	2,561,828,000	9.3	24,194,334,000

Values rounded in thousands

The above table shows the value of Fund assets by type as of June 30, 2005, 2004, and 2003, as well as liabilities and fund balances. The mix of Fund assets reflects the asset allocation decisions made by the Board of Trustees of the Alaska Permanent Fund Corporation (Corporation) as implemented by staff. The dollar and percentage changes in the value of the assets between 2005 and 2004 are due to many factors: an increase in total asset value due to the overall increase in the financial markets in fiscal year 2005, an increase in securities lending collateral, the additional mineral revenues to the Fund in fiscal year 2005 and the lower dividend distribution in fiscal year 2005 caused by income averaging over the last five years. The market gains for marketable debt securities were positive in FY05, however the lower value shown in FY05 is a direct result of funding the FY04 dividend and new asset managers in early FY05 with money allocated from marketable debt. Changes in value from 2003 to 2004 reflect many of the same factors; mineral revenue contributions, the annual dividend distribution and a significant increase in the financial markets in fiscal year 2004. However, securities lending collateral was lower.

In fiscal year 2005 the Fund produced a 10.4 percent return, following a 14.2 percent return in fiscal year 2004 and a 4.5 percent return for fiscal year 2003. Fiscal year 2005 showed a significant gain in international markets and real estate and modest gains in all other assets. Conversely, fiscal year 2004 showed a substantial gain in value of common stocks and only a slight increase in value of bonds.

The Alaska certificates of deposit balance reflects the year-end participation in the program. Participation in this program is voluntary by Alaska banks and subject to a maximum Alaska certificate of deposit program level of \$300 million. Invested securities lending collateral represents cash collateral received for loaning Fund securities to borrowers approved for the program. This is offset by a corresponding liability representing the Fund's obligation to return the cash collateral upon termination of the loan and subsequent return of the loaned securities. Changes in the invested collateral recorded for securities lending from day to day is a function of the type of collateral and level of borrowing activity.

Liabilities represent known claims against the Fund's assets. Accounts payable typically represent pending trades at month end that have not yet been paid. Cash held to pay for pending trades is reflected in the assets section. The level in cash and accounts payable at June 30, 2005 is dependent on month end trading decisions by asset managers. Lower income distributable to the state at June 30, 2005 and June 30, 2004 results from the lower dividend liability owed to the Department of Revenue for the Permanent Fund dividend program. Dividend distributions are determined by specific income and formula, both defined in Alaska statute. The formula averages certain income results over five years. This averaging resulted in reduced dividend distributions in each of 2005 and 2004 versus 2003. Fiscal year 2005 also includes, for the first time, an additional liability of \$26.8 million from realized income to be paid out of the segregated Amerada Hess settlement assets. Income from these assets, by law, cannot be used in the dividend calculation and were previously deposited into the reserved assets of the Fund. Beginning in FY05, this income will be paid out to the newly created Alaska capital income fund.

Contributions and appropriations to the Fund increased in fiscal year 2005 and 2004 by the dedicated mineral revenues deposited into the reserved fund balance and the annual inflation proofing transfer from realized earnings. The increase in the value of the unrealized appreciation on invested assets reflects the net unrealized gains in the financial markets for each fiscal year.

The increase in the realized earnings balance from fiscal year 2004 to fiscal year 2005 reflects modest realized earnings in fiscal year 2005 and a lower annual dividend distribution. The increase in the realized earnings balance from fiscal year 2003 to fiscal year 2004 is reflective of realized earnings for the fiscal year, the deduction for the annual dividend transfer to the Department of Revenue and the lower annual inflation proofing transfer to the reserved fund balance section due to pre-funding a portion of 2004 inflation proofing in fiscal year 2003.

Statements of revenues, expenditures, and changes in fund balances

The Statements of Revenues, Expenditures, and Changes in Fund Balances account for all of the current and prior years' net investment revenues. These statements show the activity that occurred during each of the last two fiscal years. Fiscal year 2003 is shown for comparison purposes.

Revenues. Revenues include dividends from stocks, interest from bonds and the Alaska CD program, and net rental income from real estate investments. Also included in revenues is the change in the fair market value (realized and unrealized gains and losses) of the investments held by the Fund.

Expenditures. The Fund's operating costs include all expenditures required by the Corporation to manage the Permanent Fund. This includes internal operating expenses as well as external manager and custodial fees. Also included in the Fund's expenditures are additional appropriations related to Fund matters, approved by the

Statements of revenues, expenditures and changes in fund balances

<i>Years ended June 30</i>	2005	2004	\$ increase (decrease)	% change	2003
Revenues					
Dividends, interest, real estate and other income	\$ 869,635,000	813,093,000	56,542,000	7.0%	859,850,000
Total net increase in the fair value of investments	1,825,133,000	2,668,343,000	(843,210,000)	(31.6)	139,344,000
Total revenues	\$ 2,694,768,000	3,481,436,000	(786,668,000)	(22.6)	999,194,000
Less operating expenditures	(47,735,000)	(42,171,000)	(5,564,000)	13.2	(36,633,000)
Less other legislative appropriations	(6,821,000)	(5,585,000)	(1,236,000)	22.1	0
Excess of revenues over expenditures	\$ 2,640,212,000	3,433,680,000	(793,468,000)	(23.1)	962,561,000
Other financing sources/uses					
Transfers in – mineral revenue	480,498,000	353,072,000	127,426,000	36.1	397,642,000
Transfers out – annual dividend distribution/other	(558,882,000)	(581,246,000)	22,364,000	(3.8)	(691,082,000)
Net changes in fund balances	2,561,828,000	3,205,506,000	(643,678,000)	(20.1)	669,121,000
Fund balances end of prior period (beginning of period)	27,399,840,000	24,194,334,000	3,205,506,000	13.2	23,525,213,000
Fund balances end of period	\$ 29,961,668,000	27,399,840,000	2,561,828,000	9.3	24,194,334,000
Statutory income calculation					
Excess of revenues over expenditures	2,640,212,000	3,433,680,000	(793,468,000)	(23.1)	962,561,000
Less settlement earnings and unrealized gains	(885,804,000)	(1,931,596,000)	1,045,792,000	(54.1)	(607,220,000)
Statutory net income	\$ 1,754,408,000	1,502,084,000	252,324,000	16.8	355,341,000

Values rounded in thousands

Alaska Legislature to the Department of Law, Department of Revenue, and Department of Natural Resources. Expenditures are subtracted from revenues.

Other financing sources/uses. These lines account for the mineral revenues received by the Fund as well as appropriations out of the Fund.

Net changes in fund balances. This section shows the net effect of all the Fund's activities on fund balances during the year. In fiscal year 2005, for example, the Fund net assets were \$27.4 billion at the beginning of the year and \$30.0 billion at the end of the year. This statement accounts for the change in total Fund value.

Statutory income calculation. Statutory net income is accounting net income adjusted for any unrealized gains and losses of the Fund and other monies excluded by law. The statutory net income calculation is necessary to determine the annual dividend distribution.

Fiscal years 2005, 2004 and 2003, shown in the table above, are most notably marked by the large increase in Fund value due to the financial markets. Overall, interest income, dividends and real estate income were slightly higher in fiscal year 2005 than in prior fiscal years.



The operating expenditures of the Fund were higher in fiscal year 2005 than 2004 and 2003 since management fees paid on externally managed assets are based on market value. Management fees also increase when more complex asset types are added to the Fund's portfolio allocation. Other appropriations to State departments from corporate receipts were \$6.8 million in fiscal year 2005 and \$5.6 million in fiscal year 2004.

Transfers into the Fund represent the Fund's share of Alaska mineral revenues. Higher mineral revenues in fiscal year 2005 over 2004 were primarily due to the higher average price of oil. In general, the Fund had a lower overall dedication of mineral revenue in both fiscal year 2005 and 2004, due to the effects of House Bill 11, reducing the Fund's portion of revenue on certain leases from 50 percent to 25 percent; however, the reduction in dedicated mineral revenues was mitigated in both fiscal years by the higher average oil price. The lower dividend distributions from the Fund reflect the impact of the five-year averaging formula of the Fund's statutory net income, outlined in statutes AS 37.13.140 and AS 37.13.145. As the five-year formula replaced years of higher statutory net income (fiscal years 1999 and 2000) with years of lower statutory net income (fiscal years 2003 and 2004), lower dividend distributions occurred. In fiscal year 2005 the transfer out includes \$26.8 million to the Alaska capital income fund.

Investment and economic factors

The Trustees increased the diversification of the Permanent Fund's investments by authorization of investments in two new asset classes; private equity and absolute return strategies. Managers were selected and contracts signed in fiscal year 2004 and the first investments in these assets took place in early fiscal year 2005.

The market value of Fund assets is directly impacted by the volatility and direction of the financial markets. Diversification of investment types is intended to mitigate these factors.

Supplemental information

The table on the following page summarizes the changes to the reserved and unreserved fund balances during the prior two years. Additional information on changes to the fund balances can be found in the notes to the financial statements.

FY04 Reserved fund balance (in millions)

	Contributions and appropriations	Unrealized appreciation	Total
Beginning balance	22,988.0	1,106.3	24,094.3
Mineral revenue	353.1		353.1
Change in unrealized appreciation		1,907.8	1,907.8
Transfer from realized earnings		1.5	1.5
Inflation proofing	169.9		169.9
Settlement earnings transfer	14.7		14.7
Total year-end	23,525.7	3,015.6	26,541.3

FY04 Unreserved fund balance (in millions)

	Realized earnings	Total Fund
Beginning balance	100.0	24,194.3
		353.1
		1,907.8
Income - dividends, interest, real estate, and other income	813.1	813.1
Realized gains	760.5	760.5
Dividend liability	(581.2)	(581.2)
Transfer to unrealized earnings	(1.5)	
Inflation proofing transfer to reserved fund balance	(169.9)	
Settlement earnings transfer, State v. Am Hess et al	(14.7)	
Fund operating expenditures and other	(47.8)	(47.8)
Total year-end	858.5	27,399.8

FY05 Reserved fund balance (in millions)

	Contributions and appropriations	Unrealized appreciation	Total
Beginning balance	23,525.7	3,015.6	26,541.3
Mineral revenue	480.5		480.5
Change in unrealized appreciation		859.0	859.0
Inflation proofing	641.0		641.0
Total year-end	24,647.2	3,874.6	28,521.8

FY05 Unreserved fund balance (in millions)

	Realized earnings	Total Fund
Beginning balance	858.5	27,399.8
		480.5
		859.0
Income - dividends, interest, real estate, and other income	869.6	869.6
Realized gains	966.2	966.2
Dividend liability	(532.1)	(532.1)
Inflation proofing transfer to reserved fund balance	(641.0)	
Capital income fund transfer (settlement earnings)	(26.8)	(26.8)
Fund operating expenditures and other	(54.6)	(54.6)
Total year-end	1,439.8	29,961.6



Independent auditors' report

The Board of Trustees
Alaska Permanent Fund Corporation
(A Component Unit of the State of Alaska):

We have audited the accompanying balance sheets of the Alaska Permanent Fund as of June 30, 2005 and 2004, and the related statements of revenues, expenditures, and changes in fund balances for the years then ended. These financial statements are the responsibility of the Alaska Permanent Fund Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only the Alaska Permanent Fund and do not purport to, and do not, present fairly the financial position of the State of Alaska as of June 30, 2005 and 2004, and changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Alaska Permanent Fund as of June 30, 2005 and 2004, and its changes in financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management discussion and analysis on pages 1 through 6 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

August 12, 2005
Anchorage, Alaska

Balance sheets

June 30	2005	2004
Assets		
Cash and temporary investments	\$ 1,298,571,000	1,496,994,000
Receivables, prepaid expenses and other assets	648,000,000	243,562,000
Investments –		
Marketable debt securities	9,006,628,000	9,285,020,000
Preferred and common stock	17,630,359,000	15,836,268,000
Real estate	2,694,595,000	2,086,928,000
Alternative investments	266,000,000	0
Alaska certificates of deposit	157,953,000	172,759,000
Total investments	29,755,535,000	27,380,975,000
Securities lending collateral invested	4,569,049,000	1,431,224,000
Total assets	\$ 36,271,155,000	30,552,755,000
Liabilities		
Accounts payable	\$ 1,181,556,000	1,140,445,000
Income distributable to the State of Alaska	558,882,000	581,246,000
Securities lending collateral	4,569,049,000	1,431,224,000
Total liabilities	6,309,487,000	3,152,915,000
Fund balances		
Reserved – principal		
Contributions and appropriations	24,647,217,000	23,525,752,000
Unrealized appreciation on invested assets	3,874,602,000	3,015,548,000
Total reserved	28,521,819,000	26,541,300,000
Unreserved		
Realized earnings	1,439,849,000	858,540,000
Total fund balances	29,961,668,000	27,399,840,000
Total liabilities and fund balances	\$ 36,271,155,000	30,552,755,000

The accompanying notes are an integral part of the financial statements.



Notes to financial statements

Statements of revenues, expenditures and changes in fund balances

Years ended June 30	2005	2004
Revenues		
Interest	\$ 389,825,000	387,762,000
Dividends	333,372,000	258,029,000
Real estate and other income	146,438,000	167,302,000
Total interest, dividends, real estate and other income	869,635,000	813,093,000
Net increase (decrease) in the fair value of investments		
Marketable debt securities	258,917,000	(262,987,000)
Preferred and common stock	1,241,205,000	2,777,126,000
Real estate	298,882,000	187,069,000
Alternative investments	14,098,000	0
Foreign exchange contracts	11,950,000	(32,499,000)
Currency	81,000	(366,000)
Total net increase in the fair value of investments	1,825,133,000	2,668,343,000
Total revenues	2,694,768,000	3,481,436,000
Expenditures		
Operating expenditures	(47,735,000)	(42,171,000)
Other legislative appropriations	(6,821,000)	(5,585,000)
Total expenditures	(54,556,000)	(47,756,000)
Excess of revenues over expenditures	\$ 2,640,212,000	3,433,680,000
Other financing sources (uses)		
Transfers in	480,498,000	353,072,000
Transfers out	(558,882,000)	(581,246,000)
Net changes in fund balances	2,561,828,000	3,205,506,000
Fund balances		
Beginning of period	27,399,840,000	24,194,334,000
End of period	\$ 29,961,668,000	27,399,840,000

The accompanying notes are an integral part of the financial statements.

No. 1 Entity

The Constitution of the State of Alaska (the “state”) was amended by public referendum in 1976 to dedicate a portion of certain natural resource revenues to the Alaska Permanent Fund (the “Fund”). These contributions to the Fund are to be invested in perpetuity. The Alaska State Legislature (the “legislature”) created the Alaska Permanent Fund Corporation (the “Corporation”), a component unit of the state that is administered by a board of trustees (the “Trustees”), to manage the investments of the Fund. By statute, and subsequent appropriation, (i) a portion of annual realized earnings is transferred to the state’s dividend fund, (ii) a portion of the realized earnings sufficient to offset the impact of inflation on contributions and appropriations is transferred to the reserved balance of the Fund, and (iii) beginning in fiscal year 2005, the realized earnings on the balance of the North Slope royalty case (State v. Amerada Hess, et al.) settlement money is transferred to the Alaska Capital Income Fund (the “ACIF”). The balance of the Fund’s realized earnings is held in the realized earnings account, and is subject to appropriation by the Legislature. Unrealized gains and losses on Fund assets are considered reserved, and are not available for appropriation, nor do they affect the realized earnings account. All assets are aggregated for investment purposes.

The Fund’s assets are held in a wide variety of investments, in accordance with Alaska statutes and investment policies of the Corporation. The investments include stocks and bonds, both domestic and non-domestic, private equity and public equity real estate, as well as alternative investments in private equity limited partnerships, and absolute return strategies. The Fund’s results of operations rely largely on the success of the financial markets. However, the volatility of markets, especially that of public and private equity markets, can cause substantial period-to-period fluctuations in operating results. Diversification by asset type helps to mitigate the volatility of operating results.

No. 2 Significant accounting policies

The Fund’s financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. In preparing the financial statements, management is required to make estimates and assumptions as of the date of the balance sheet that affect the reported amounts of assets and liabilities and the disclosure of contingent assets, liabilities, revenues, and expenses for the period. Actual results could differ from those estimates.

Dividend appropriations

Statutory net income excludes realized earnings from contributions made in the North Slope royalty case settlements (State v. Amerada Hess, et al.), and recorded unrealized gains and losses on the Fund’s investments. Current statutes require that one-half of twenty-one percent of the Fund’s five year rolling average of statutory net income be made available for the payment of dividend appropriations each year. However, amounts available for the dividend appropriations are further limited to no more than one-half of the realized earnings account balance.

Fund balances

Reserved fund balances consist of historical mineral revenues, special appropriations, and inflation proofing transfers within the Fund, as well as recorded unrealized appreciation or depreciation of invested assets. On June 18, 2003, the Corporation received an Alaska Attorney General’s Opinion (Opinion), clarifying the portion of Fund assets that



is legally reserved. The Opinion indicates that the recorded unrealized appreciation and depreciation on invested assets must be classified as part of the reserved portion of fund balances, making them unavailable for appropriation. Based on the Opinion, the recorded unrealized earnings of the fund balance were reclassified from unreserved fund balances to reserved fund balances. The Opinion had no impact on previous or future inflation proofing calculations or the excess (deficiency) of revenues over expenditures. See 2003 Attorney General Opinion (June 18; 663-03-0153). Unreserved fund balances consist of those realized earnings of the Fund that have not yet been appropriated.

Inflation proofing

State statute requires that the contributions and appropriations of the Fund be adjusted annually for the impact of inflation. The annual inflation proofing transfer within the Fund each year can only be done through legislative appropriation. The impact of inflation is measured by the percent change in each of the two prior calendar years' averages of the United States consumer price index for all urban consumers applied against the total of the reserved fund balance, excluding unrealized gains and losses, at the end of the fiscal year. The inflation rates were 2.67 percent and 2.28 percent, and were applied to the years ended June 30, 2005 and 2004, respectively.

Interest income

Interest income is accrued daily as earned and is recorded monthly in the books of the Fund.

Income taxes

In the opinion of legal counsel, as integral parts of the state, the Fund and the Corporation are not subject to federal or state income taxes. In addition, the Internal Revenue Code provides that gross income for tax purposes does not include income earned by a state or any subdivision thereof, which is derived from the exercise of any essential governmental function. The Fund and the Corporation perform an essential governmental function and are therefore also exempt from federal income taxes under that provision.

Investments and related policies

Carrying value of investments

The Fund's investments, excluding certain real estate investments, are reported at fair market value in the financial statements. Unrealized gains and losses are reported as components of net income. Fair market values are obtained from independent sources for marketable debt and equity securities and real estate investment trusts. Fair market values of alternative investments are determined by independent managers of such investments, who are under contract with the Corporation to provide such services.

Real estate commingled funds, private equity real estate investments, and direct mortgages are carried at the equity value, which is historical cost plus the Fund's share of undistributed earnings. If, upon analysis by management under applicable accounting rules, a permanent impairment of value has occurred, the investment is written down to fair market value by recording a realized loss on invested assets.

Securities transactions are recorded on the trade date that securities are purchased or sold.

Investment policy

The Trustees have established a long-term goal of achieving a 5% real rate of return on the investment portfolio. To achieve this target, the Trustees allocate the Fund investments among various asset classes. In order to allow for market fluctuations and to minimize transaction costs, the Trustees also adopted acceptable ranges around the targets. At June 30, 2005, the Corporation's asset allocation policy (with acceptable ranges) is as follows:

Domestic equities	37% (± 6%)
International equities	18% (± 3%)
Domestic fixed income	28% (± 6%)
Non-dollar fixed income	4% (± 3%)
Real estate	10% (± 3%)
Private equity	2% (± 2%)
Absolute return	1% (± 1%)

Per Alaska Statute 37.13.120, the Corporation must limit certain invested Fund assets in: (i) equity securities to fifty-five percent (55%) of total Fund investments, (ii) real estate investments to fifteen percent (15%), and (iii) up to ten percent (10%) of total Fund investments in additional investments that meet the prudent investor rule, including those currently authorized by law. The statute further specifies limits on and acceptable investments in various other assets, such as certificates of deposit and residential mortgages.

Concentration of credit risk

Concentration of credit risk is the risk of loss attributable to holding investments from a single issuer. Pursuant to Alaska Statute 37.13.120, the Corporation may not invest Fund assets in equity securities that would result in ownership of more than 5% of the voting shares of any corporation. The Fund further manages its concentration of credit risk by following its asset allocation resolution, and by diversifying investments among many managers with varying investment styles and mandates. The Corporation's policy for mitigating this risk of loss for fixed income and equity investments is to ensure compliance with Trustee resolution 02-09, and resolution 05-05, respectively, as well as investment manager contracts. Those resolutions and contracts specify concentration limits for issuers and types of investments.

Credit risk

The Corporation requires that all fixed income corporate bonds and non-domestic bonds have at least one Nationally Recognized Statistical Rating Organization's (NRSRO) rating in a relevant jurisdiction, provided that no NRSRO rating may be below investment grade. Should the rating on an existing fixed income security fall below investment grade, the security must be sold within six months.

The Corporation does not have an allocation to cash. Managers are limited to the amount of cash they may hold, and most cash reflects pending transactions. The Corporation manages the aggregate cash position of all domestic equity and REIT managers and the internal fixed income portfolio in a Unitized Cash Fund (UCF). The UCF is primarily intended to serve as an efficient mechanism for investing daily transactional cash. UCF securities must be rated by at least two NRSROs comparable to Moody's or Standard & Poor's equivalents of P1 or A1 for short-term investments.

Custodial credit risk

The Corporation generally requires that all investment securities be held in the name of the Fund or the Corporation. For non-domestic securities held by sub-custodians, the Corporation is indemnified against custodial credit risk by its primary custodian.



Foreign currency risk

Foreign currency risk arises when a loss may result from changes in foreign currency exchange rates. Foreign currency risk is managed by the international investment managers through their decisions to enter into foreign currency forward contracts. As stated in Trustee resolution, Corporation policy, and manager contracts, managers are allowed to purchase foreign currency futures contracts in order to facilitate securities transactions or for defensive hedging of foreign currencies into the US dollar. Also, policy prohibits managers from selling securities short or holding a net short position in any currency.

Interest rate risk

The Corporation manages the Fund's exposure to fair value losses arising from changing interest rates by establishing effective duration guidelines in its fixed income investment policy. Duration is used to explain a portfolio's sensitivity to changes in interest rates. The duration of a portfolio is the average market value weighted duration of all bonds in the portfolio. In general, the major anticipated factors affecting duration are, in order of importance: maturity, prepayment frequency, size of coupon, level of market interest rates, and frequency of coupon payments. Duration will fall as interest rates rise. Effective duration attempts to account for the price sensitivity of a bond, including the impact of embedded options.

The Corporation's policy specifies an effective duration range for the long term domestic fixed income portfolios of 80% -120% of the respective portfolio benchmark index's duration, and for non-domestic fixed income securities a portfolio duration range of 50% -150% of the respective portfolio benchmark index's duration. The Corporation uses industry-standard analytical software to calculate effective duration. The software takes into account various possible interest rates, historical and estimated prepayment rates, call and put options, and other variable cash flows for the effective duration calculation. As an example, for a bond with a duration of 5.0, a one percentage point parallel decline in interest rates would result in a price increase on that bond of 5.0%.

For short-term debt investments, the Corporation's policy states that the weighted average day count of the short-term UCF cannot exceed 150 days, with a final maximum maturity of 14 months for any single investment.

Forward exchange contracts

The Corporation, on behalf of the Fund, is party to a variety of forward currency contracts in its trading activities, and in the management of its foreign exchange rate exposure. These contracts are intended to guard against foreign currency fluctuations and the contract amounts do not appear on the balance sheet. Realized gains and losses are included in net income at the time the contract is closed or matures, and are determined based on the difference between the contract rate and the market rate at the time of maturity or closing. Unrealized gains and losses are also included in net income and are calculated based on the difference between the contract rate and the forward market rate determined as of the balance sheet date.

Transfers in

Contributions from dedicated state revenues are recorded when certain revenues defined by statute are received or reported by the Alaska Department of Natural Resources. Contributions from appropriations and other sources are recorded when received.

Transfers out

Transfers out to other state agencies are recorded when measurable.

No. 3 Short-term investments

All short-term investments bear interest at competitive rates and are summarized as follows at June 30:

	2005 [†]	2004 [†]
US agencies	\$ 216,772,000	98,384,000
Treasury bills	591,048,000	986,067,000
Domestic certificates of deposit	3,060,000	0
Commercial paper	312,753,000	267,725,000
Total short-term investments	1,123,633,000	1,352,176,000
Cash	174,938,000	144,818,000
Total cash and short-term investments	\$ 1,298,571,000	1,496,994,000

At June 30, 2005, all commercial paper and certificates of deposit were rated A-1 by Standard & Poor's, P-1 by Moody's, or an equivalent rating. US agencies and treasury bills are either explicitly or implicitly guaranteed by the US government and are not rated. Short-term investments held at fiscal year end 2005 in the UCF had a weighted average maturity of 27 days. At June 30, 2005, uninvested, uninsured cash of \$48,303,000 was held at the custodian or subcustodian banks. All remaining cash balances either were insured or were invested in short-term pooled investment funds, which were rated AAA by Standard & Poor's.

No. 4 Receivables, prepaid expenses and other assets

Receivables, prepaid expenses and other assets at June 30 are as follows:

	2005 [†]	2004 [†]
Interest receivable	\$ 89,303,000	92,810,000
Dividends receivable	31,030,000	28,337,000
Sales receivable	479,224,000	87,503,000
Foreign exchange contracts	3,969,000	0
Contributions receivable	44,474,000	34,231,000
Other receivables	0	681,000
Total receivables, prepaid expenses and other assets	\$ 648,000,000	243,562,000

No. 5 Marketable debt securities

Marketable debt securities at June 30 are summarized as follows:

	Cost [†]	Market [†]	Unrealized gains/(losses) [†]
2005			
Treasury notes/bonds	\$ 2,323,651,000	2,364,077,000	40,426,000
Mortgage-backed securities	2,706,094,000	2,715,279,000	9,185,000
Other federal agencies	431,774,000	440,468,000	8,694,000
Corporate bonds	2,176,551,000	2,237,612,000	61,061,000
Non-domestic bonds	1,230,579,000	1,249,192,000	18,613,000
Total marketable debt securities	\$ 8,868,649,000	9,006,628,000	137,979,000
2004			
Treasury notes/bonds	\$ 2,635,951,000	2,621,146,000	(14,805,000)
Mortgage-backed securities	2,860,776,000	2,872,492,000	11,716,000
Other federal agencies	447,406,000	451,533,000	4,127,000
Corporate bonds	2,115,578,000	2,155,807,000	40,229,000
Non-domestic bonds	1,137,454,000	1,184,042,000	46,588,000
Total marketable debt securities	\$ 9,197,165,000	9,285,020,000	87,855,000



No. 6 Marketable debt credit ratings

In order to manage credit risk for marketable debt securities, the Corporation monitors daily market values of all securities and routinely reviews its investment holdings' credit ratings. Issues falling below investment grade are required to be sold within six months of the downgrade date. If credit ratings differ between NRSROs, the rating with the highest degree of risk (the lowest rating) is used. At June 30, 2005, the Fund's credit ratings for its marketable debt securities issued by NRSROs are as follows:

Quality rating	Domestic	Non-domestic	Total market value
AAA	\$ 594,423,000	865,011,000	1,459,434,000
AA	336,360,000	15,904,000	352,264,000
A	716,268,000	281,601,000	997,869,000
BBB	656,766,000	86,676,000	743,442,000
BB	61,871,000	0	61,871,000
Total market value of rated debt securities	2,365,688,000	1,249,192,000	3,614,880,000
US government explicitly backed			
by the US government	2,424,882,000	0	2,424,882,000
US government implicitly backed			
by the US government	2,966,866,000	0	2,966,866,000
Total market value debt securities	\$ 7,757,436,000	1,249,192,000	9,006,628,000

No. 7 Marketable debt duration

In order to manage its interest rate risk on marketable debt securities, the Corporation monitors daily market values and routinely reviews portfolio effective duration in comparison to an established benchmark. At fiscal year end, the aggregate holdings of debt securities were within the required range in relation to such benchmarks. At June 30, 2005, the effective duration by investment type, based on market value, is as follows:

	Percent of bond holdings	Duration
Domestic bonds		
Treasury	28.45%	3.71
Government sponsored	8.61%	5.00
Mortgage (agency and corporate)	37.75%	2.53
Corporate bonds	17.11%	6.31
Canadian/Yankee, Supra/Sovereign	8.08%	5.47
Total domestic bonds	100.00%	3.96
Non-domestic bonds		
Government and agency	90.70%	5.95
Corporate and other non-government	9.30%	5.40
Total non-domestic bonds	100.00%	5.90

No. 8 Concentration of credit risk

At June 30, 2005, more than 5% of the Fund's total investments were held in securities of the issuer listed below:

Issuer of securities	Market value of holdings	Percent of total Fund
Federal National Mortgage Association		
Mortgage-backed securities	\$ 1,876,089,000	6.3%
Senior debt	215,275,000	.7%
Equity	32,271,000	.1%
Total	\$ 2,123,635,000	7.1%

No. 9 Preferred and common stock

All investments in preferred and common stock, except for one, are held by custodian banks in the name of the Fund. The assets of the Emerging Markets Growth Fund (EMGF), managed by Capital International, Inc., are held by the custodian bank of the fund manager on behalf of the commingled fund's investors. The market value of the Fund's shares in the EMGF was \$468,106,000 and \$344,547,000 as of June 30, 2005 and 2004, respectively. The value of the Fund's investment in the commingled fund represented approximately 3.4 percent and 2.2 percent of the total EMGF value at June 30, 2005 and 2004, respectively.

Preferred and common stocks at June 30 are summarized as follows:

	Cost	Market	Unrealized gains
2005			
Domestic	\$ 9,743,814,000	11,929,688,000	2,185,874,000
Non-domestic	4,605,882,000	5,700,671,000	1,094,789,000
Total preferred and common stock	\$ 14,349,696,000	17,630,359,000	3,280,663,000
2004			
Domestic	\$ 8,895,449,000	10,856,996,000	1,961,547,000
Non-domestic	4,257,875,000	4,979,272,000	721,397,000
Total preferred and common stock	\$ 13,153,324,000	15,836,268,000	2,682,944,000



No. 10 Foreign currency exposure

At June 30, 2005, the Fund's non-domestic equity and debt securities had exposure to foreign currency risk as follows (shown in US dollar equivalent):

Foreign currency	Equity market value	Debt market value	Total foreign currency exposure
Australian Dollar	\$ 194,596,000	73,627,000	268,223,000
Brazilian Real	23,049,000	0	23,049,000
British Pound Sterling	1,167,883,000	87,480,000	1,255,363,000
Canadian Dollar	80,312,000	0	80,312,000
Czech Koruna	1,357,000	0	1,357,000
Danish Krone	21,671,000	57,823,000	79,494,000
Egyptian Pound	3,944,000	0	3,944,000
Euro Currency	1,926,629,000	702,210,000	2,628,839,000
Hong Kong Dollar	84,357,000	0	84,357,000
Hungarian Forint	6,661,000	3,318,000	9,979,000
Indian Rupee	6,964,000	0	6,964,000
Indonesian Rupiah	7,519,000	0	7,519,000
Israeli Shekel	4,139,000	0	4,139,000
Japanese Yen	1,042,219,000	254,210,000	1,296,429,000
Malaysian Ringgit	16,929,000	0	16,929,000
Mexican Nuevo Peso	5,420,000	32,134,000	37,554,000
New Taiwan Dollar	30,310,000	0	30,310,000
New Zealand Dollar	4,521,000	13,000	4,534,000
Norwegian Krone	25,745,000	41,376,000	67,121,000
Philippines Peso	821,000	0	821,000
Polish Zloty	4,856,000	19,425,000	24,281,000
Renminbi Yuan	900,000	0	900,000
Singapore Dollar	41,566,000	0	41,566,000
South African Rand	45,816,000	0	45,816,000
South Korean Won	52,852,000	9,302,000	62,154,000
Swedish Krona	85,111,000	3,838,000	88,949,000
Swiss Franc	357,006,000	0	357,006,000
Thai Baht	13,311,000	0	13,311,000
Turkish Lira	8,486,000	0	8,486,000
Total foreign currency exposure	\$ 5,264,950,000	1,284,756,000	6,549,706,000

Amounts in the schedule above include receivable, payable, and cash balances in the related currency of each investment type.

No. 11 Real estate

The Corporation is authorized by statute to invest Fund assets in real estate improved by completed and substantially rented buildings located in the United States. Real estate investments may take the form of private equity real estate interests, real estate title-holding entities, real estate investment trusts, real estate operating companies or other entities whose assets consist primarily of real property, debt obligations secured by real property, or similar entities. The Corporation invests Fund assets in direct real estate through its ownership of interests in corporations, limited liability companies and partnerships that own title to the real estate. External real estate management firms administer the Fund's private equity real estate investments.

The Corporation routinely analyzes private equity real estate holdings for permanent impairment, in accordance with Corporate resolution 04-07 and Governmental Accounting Standards Board Statement No. 42 (Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries). During the fiscal year ending June 30, 2005, no real estate assets were at a market value deemed necessary for permanent impairment analysis. During the fiscal year ending June 30, 2004, losses of \$17,250,000 were realized due to the permanent impairment of real estate assets.

The carrying value of real estate at June 30, 2005 and 2004 was \$2,694,595,000 and \$2,086,928,000, respectively. Private equity real estate investments, commingled funds, property notes receivable, and residential mortgages are recorded in the financial statements using the equity method, which consists of the asset's historical cost plus the Fund's share of undistributed earnings from the asset. Public equity real estate investments (real estate investment trusts) are recorded in the financial statements at their market value.

In the ordinary course of business, the Corporation has made Fund commitments related to real estate investments. In the opinion of management, meeting these commitments will not have a materially adverse effect on the Fund's financial position, results of operations, or liquidity. Real estate investments at June 30 are summarized as follows:

	Cost/equity value	Market value	Unrealized gains/(losses)	Financial statement carrying value
2005				
Real estate investment trusts	\$ 772,613,000	1,210,469,000	437,856,000	1,210,469,000
Alaska residential mortgages	72,000	72,000	0	72,000
Property note receivable	3,340,000	3,340,000	0	3,340,000
Private equity real estate -				
Retail	399,239,000	603,388,000	204,149,000	399,239,000
Office	559,760,000	628,174,000	68,414,000	559,760,000
Industrial	208,038,000	222,852,000	14,814,000	208,038,000
Multifamily	313,677,000	351,073,000	37,396,000	313,677,000
Total real estate	\$ 2,256,739,000	3,019,368,000	762,629,000	2,694,595,000
2004				
Commingled funds	\$ 1,043,000	853,000	(190,000)	1,043,000
Real estate investment trusts	714,941,000	969,220,000	254,279,000	969,220,000
Alaska residential mortgages	84,000	84,000	0	84,000
Property note receivable	3,273,000	3,273,000	0	3,273,000
Private equity real estate -				
Retail	257,320,000	274,861,000	17,541,000	257,320,000
Office	464,845,000	499,128,000	34,283,000	464,845,000
Industrial	135,964,000	148,869,000	12,905,000	135,964,000
Multifamily	255,179,000	291,352,000	36,173,000	255,179,000
Total real estate	\$ 1,832,649,000	2,187,640,000	354,991,000	2,086,928,000

Subsequent to fiscal year end 2005, additional real estate was purchased for the Fund. A portion of an existing office building investment joint venture in New Jersey was purchased for an additional \$7,437,000, which made the Fund the sole owner of the property. An office building in San Francisco, California was also purchased for \$134,120,000. The Fund owns 98% of the office building. Amounts in the schedule above include \$9,872,000 in earnest money deposited on the San Francisco building prior to fiscal year end, as well as \$494,000 deposited on a retail building in Hawaii.



No. 12 Alternative investments

The Trustees increased the diversification of the Fund's investments by authorization of investments in two new asset classes. The first, private equity, is comprised of various investments such as in unlisted, illiquid common and preferred stock, or subordinated and senior debt of privately held companies. The second, absolute return strategies, are investments in non-market correlated strategies through specialized investment funds. Resolutions were drafted, managers were selected and contracts signed in fiscal year 2004, and the first investments in these assets took place in early fiscal year 2005.

The Trustees authorized a three-year pilot program for an absolute return strategy by allocating up to one percent of Fund assets. The Board chose a separately managed portfolio comprised of a single-investor limited partnership ("fund of one") that invests in a diversified portfolio comprised of limited partnership interests, with the general partner providing essential investment management services. Fair value for limited partnership interests are valued by the general partner and reviewed by the investment manager. Some of the absolute return investments do not have readily ascertainable market values and may be subject to withdrawal restrictions and/or additional expenses.

The Trustees authorized investments in private equity up to two percent of the total Fund value. Private equity investments involve the purchase of limited partnership interests which typically invest in unlisted, illiquid common and preferred stock and to a lesser degree, subordinated and senior debt of companies that are in most instances privately held. The Corporation has hired an external manager to select limited partnership interests which are diversified by geography and strategy. This investment type is characteristically funded slowly over time as opportunities are identified by the general partners and external manager. Investments in this category are valued utilizing the most current information provided by the general partner.

Alternative investments at June 30 are summarized as follows:

	Cost	Market	Unrealized gains/(losses)
2005			
Absolute return strategy	\$ 244,133,000	259,531,000	15,398,000
Private equity	7,756,000	6,469,000	(1,287,000)
Total alternative investments	\$ 251,889,000	266,000,000	14,111,000

As of June 30, 2005, the Corporation had various private equity investment commitments of approximately \$300 million.

No. 13 Alaska certificates of deposit

The Corporation is authorized by statute and Trustee resolution 04-03, to invest Fund assets in certificates of deposit or the equivalent instruments of banks, savings and loan associations, mutual savings banks and credit unions doing business in Alaska. Collateral, as required by law, primarily in the form of letters of credit from the Federal Home Loan Bank or US government securities, secures these investments.

No. 14 Securities lending

Under Alaska Statute 37.13.120(f), the Corporation is authorized to enter into securities lending transactions on behalf of the Fund. The Corporation, through an agreement with the Bank of New York (the Bank), lends marketable debt and equity securities. These loans are fully collateralized with cash or US government guaranteed marketable securities at not less than one hundred two percent (102%) of the market value of the loaned securities for domestic securities and one hundred five percent (105%) of the market value for non-domestic loaned securities. The Corporation is able to sell any securities out on loan. Upon borrower default, the Bank may hold cash collateral or sell non-cash collateral. The Corporation is protected from credit risk associated with the lending transactions through indemnification by the Bank against any loss resulting from counterparty failure, loss resulting from the reinvestment of collateral, default on collateral investments, or default on loaned securities.

Cash collateral received for securities on loan, which is required to be reported on the balance sheet of the Fund, is invested by the Bank in the name of the Fund. As of June 30, 2005, such investments were in overnight repurchase agreements secured at one hundred two percent (102%) by US government guaranteed securities, and had a weighted-average maturity of one day. The average term of the loans was also one day. At June 30, the value of securities on loan and related collateral is as follows:

	2005	2004
Market value of securities on loan	\$ 4,508,284,000	3,804,367,000
Collateral		
Cash collateral	4,569,049,000	1,431,224,000
Non-cash collateral	44,477,000	2,501,494,000
Total collateral	\$ 4,613,526,000	3,932,718,000

The Fund receives 80% of earnings derived from securities lending transactions. During the years ended June 30, 2005 and 2004, there were no losses incurred as a result of securities lending transactions. The Fund received \$10,413,000 and \$9,092,000 from securities lending for the years ended June 30, 2005 and 2004, respectively.

No. 15 Accounts payable

Accounts payable at June 30 are summarized as follows:

	2005	2004
Accrued liabilities	\$ 12,961,000	12,039,000
Foreign exchange contracts	0	9,401,000
Securities purchased	1,168,595,000	1,119,005,000
Total accounts payable	\$ 1,181,556,000	1,140,445,000



No. 16 Income distributable to the State of Alaska

The legislature appropriates portions of the Fund's statutory net income for various purposes, including the payment of dividends to qualified residents of the state. In addition, the legislature has appropriated a portion of the dividend distribution to fund various other agency activities. Per statute, for fiscal year 2005 and forward, realized earnings on the principal balance of the dedicated state revenues from the North Slope royalty case (State v. Amerada Hess, et al.) settlements are to be transferred out of the Fund to the ACIF, and managed at the state treasury. Income distributable to the state at June 30 is summarized as follows:

	2005 [†]	2004 [†]
Dividends	\$ 505,203,000	550,099,000
Appropriation to the Departments of -		
Corrections	4,238,000	5,092,000
Health and Social Services	12,885,000	15,950,000
Revenue	6,105,000	5,794,000
Public Safety	2,585,000	3,107,000
Legislature	273,000	329,000
Administration	842,000	875,000
Total to dividend fund	532,131,000	581,246,000
Alaska Capital Income Fund	26,751,000	0
Total income distributable	\$ 558,882,000	581,246,000

No. 17 Reserved and unreserved fund balances

Fund balance activity during the years ended June 30 is summarized as follows:

	2005 [†]	2004 [†]
Reserved		
Balance, beginning of year	\$ 26,541,300,000	24,094,334,000
Dedicated state revenues	480,498,000	353,072,000
Inflation proofing transfer from realized earnings	640,967,000	524,102,000
Liquidation of assets managed for other funds	0	1,484,000
Special appropriation reclassified to inflation proofing	0	(354,155,000)
Settlement earnings, net of inflation	0	14,713,000
Change in market value appreciation on invested assets	859,053,000	1,907,750,000
Balance, end of year	\$ 28,521,818,000	26,541,300,000
Unreserved		
Balance, beginning of year	\$ 858,540,000	100,000,000
Inflation proofing transfer to reserved fund balance	(640,967,000)	(169,947,000)
Liquidation of assets managed for other funds	0	(1,484,000)
Settlement earnings to ACIF	(26,751,000)	0
Settlement earnings to reserved fund balance	0	(14,713,000)
Dividends to Department of Revenue	(532,131,000)	(581,246,000)
Realized earnings, net of operating expenditures	1,781,159,000	1,525,930,000
Balance, end of year	\$ 1,439,850,000	858,540,000
Total		
Balance, beginning of year	\$ 27,399,840,000	24,194,334,000
Dedicated state revenues	480,498,000	353,072,000
Settlement earnings to ACIF	(26,751,000)	0
Dividends to Department of Revenue	(532,131,000)	(581,246,000)
Excess of investment revenues over expenditures	2,640,212,000	3,433,680,000
Balance, end of year	\$ 29,961,668,000	27,399,840,000

In fiscal year 2003, the legislature made a special appropriation (through Senate Bill 100) of \$354,155,000 from the Fund's realized earnings account to its contributions and appropriations reserved fund balance. In fiscal year 2004, the legislature further defined this special appropriation (through Senate Bill 283) as inflation proofing related to the 2004 fiscal year. Therefore, in fiscal year 2004, the \$354,155,000 was moved from the special appropriations section of contributions and appropriations to the inflation proofing section. An additional \$169,947,000 was appropriated through Senate Bill 283, to fully inflation proof the contributions and appropriations of the Fund in fiscal year 2004.



The composition of the contributions and appropriations reserved fund balance at June 30 is shown as follows:

	2005	2004
Dedicated state revenues	\$ 8,559,651,000	8,079,153,000
Special appropriations	6,885,906,000	6,885,906,000
Inflation proofing	9,048,749,000	8,407,782,000
Settlement earnings	152,911,000	152,911,000
Total contributions and appropriations	\$ 24,647,217,000	23,525,752,000

During the fiscal years 1990 through 1999, the Fund received dedicated state revenues from North Slope royalty case (State v. Amerada Hess, et al.) settlements. By statute, realized earnings from these settlement payments are to be treated in the same manner as other Fund income, except that these earnings on settlements are excluded from the dividend calculation, and in 2005 are to be transferred to the ACIF managed by the state treasury. Prior to 2005, statute required such earnings to be transferred to the principal of the reserved fund balance. Total realized earnings on settlement principal were \$26,751,000 in 2005 and \$23,846,000 in 2004. The fiscal year 2005 earnings were accrued and subsequently transferred to the ACIF. Of the 2004 earnings, \$9,133,000 was added to inflation proofing and \$14,713,000 was transferred to principal. Accumulated settlement related activity, which is included in the contributions and appropriations balance of the Fund at June 30, is shown as follows:

	2005	2004
Settlement		
Principal	\$ 194,083,000	194,083,000
Earnings	152,911,000	152,911,000
Inflation proofing	77,405,000	77,405,000
Total settlement principal	\$ 424,399,000	424,399,000

No. 18 Statutory net income

By Alaska law, statutory net income is computed in accordance with accounting principles generally accepted in the United States of America (GAAP), excluding settlement income from the North Slope royalty case (State v. Amerada Hess, et al.) and any unrealized gains or losses. However, net income is required by GAAP to include unrealized gains and losses and all other income, regardless of source. Consequently, GAAP net income and statutory net income differ. It is statutory net income that is used to compute the amount available for the annual Permanent Fund dividend.

Statutory net income for the years ended June 30 is calculated as follows:

	2005	2004
Excess of revenues over expenditures	\$ 2,640,212,000	3,433,680,000
Unrealized gains	(859,053,000)	(1,907,750,000)
Settlement earnings	(26,751,000)	(23,846,000)
Statutory net income	\$ 1,754,408,000	1,502,084,000

No. 19 Investment income by source

Investment income during the years ended June 30 is summarized as follows:

	2005	2004
Interest		
Domestic marketable debt securities	\$ 304,332,000	327,544,000
Non-domestic marketable debt securities	49,935,000	46,298,000
Alaska certificates of deposit	3,692,000	2,635,000
Short-term domestic and other	31,866,000	11,285,000
Total interest	\$ 389,825,000	387,762,000
Dividends		
Domestic preferred and common stock	190,443,000	144,743,000
Non-domestic preferred and common stock	142,929,000	113,286,000
Total dividends	\$ 333,372,000	258,029,000
Real estate and other income		
Private equity real estate interest	\$ 268,000	265,000
Real estate investment trust dividends	51,696,000	46,746,000
Private equity real estate net rental income	81,712,000	106,101,000
Absolute return cash flow	(2,753,000)	0
Loaned securities and other income	15,515,000	14,190,000
Total real estate and other income	\$ 146,438,000	167,302,000

No. 20 Foreign exchange contracts and off-balance sheet risk

Asset managers for the Corporation entered into foreign currency forward exchange contracts (FX forward contracts) to buy and sell, on behalf of the Fund, specified amounts of foreign currencies at specified rates on specified future dates for the purpose of protecting existing or anticipated positions in these currencies. The maturity periods for outstanding contracts at fiscal year end ranged from one to five months.

The counterparties to the FX forward contracts consisted of a diversified group of financial institutions. The Fund is exposed to credit risk to the extent of non-performance by these counterparties; however, the Corporation considers the risk of default to be remote. The Fund's market risk as of June 30, 2005 is limited to the difference between contractual rates and forward market rates determined at the end of the fiscal year.

On behalf of the Fund, asset managers of the Corporation had net sale contracts receivable totaling \$3,969,000 as of June 30, 2005 and net purchase contracts payable totaling \$9,401,000 as of June 30, 2004. FX forward contracts resulted in net unrealized gains of \$13,352,000 for the year ended June 30, 2005, and net unrealized losses of \$16,608,000 for the year ended June 30, 2004, including prior year reversals in each year. FX forward contracts resulted in realized losses of \$1,402,000 and \$15,891,000 for the years ended June 30, 2005 and June 30, 2004, respectively.



No. 21 Expenditures

Fund expenditures for the years ended June 30 are summarized as follows:

	2005	2004
Corporation expenditures paid by the Fund		
Salaries and benefits	\$ 3,149,000	2,779,000
Travel	221,000	271,000
Communications	786,000	761,000
Custody and safekeeping fees	1,752,000	1,709,000
Consulting fees	539,000	427,000
Investment management fees	39,658,000	34,402,000
Legal and audit fees	374,000	441,000
Public information and subscriptions	232,000	390,000
Rent	324,000	305,000
Property and equipment	152,000	191,000
Other expenses	548,000	495,000
Total operating expenditures	47,735,000	42,171,000
Other Fund appropriations from corporate receipts		
Department of Law	1,477,000	1,477,000
Department of Natural Resources	4,977,000	3,211,000
Department of Revenue	367,000	897,000
Total other Fund appropriations	6,821,000	5,585,000
Total expenditures	\$ 54,556,000	47,756,000

No. 22 Pension plan

All full-time, regular employees of the Corporation participate in the State of Alaska Public Employees Retirement System (PERS), and all employees of the Corporation participate in the Alaska Supplemental Annuity Plan (SBS-AP). PERS is a defined benefit multiple-employer public employee retirement system. Employees were required to contribute 6.75 percent of their annual salaries to PERS in the years ended June 30, 2005 and 2004. The Corporation contributed a matching 12.65 and 7.20 percent to the PERS system for the benefit of each employee during the years ended June 30, 2005 and 2004, respectively. The SBS-AP is a defined contribution multiple-employer plan that was created under Alaska statutes effective January 1, 1980, pursuant to Internal Revenue Code section 401(a), to provide benefits in lieu of those provided by the Federal Social Security System. All Corporation employees are required to contribute 6.13 percent of their annual salaries to SBS-AP, and the Corporation contributes a matching 6.13 percent to the plan for the benefit of each employee, up to a specified maximum each year. Total salaries for employees covered by PERS for the years ended June 30, 2005 and 2004 amounted to \$2,304,000 and \$2,136,000, respectively. Total salaries for employees covered by SBS-AP for the years ended June 30, 2005 and 2004 amounted to \$2,329,000 and \$2,161,000, respectively.

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Photo Captions: Pg. 2: Carl Brady, Chairman; William A. Corbus, Trustee; Steve Frank, Vice Chair; Bill Hudson, Trustee; Eric E. Wohlforth, Trustee; David Márquez, Trustee; Pg. 4: Michael J. Burns, Executive Director; Pg. 8: Governor Jay Hammond; Pg. 18: Seth Holden, APFC summer intern; Pg. 19: Esa Wiegert, APFC summer intern.

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