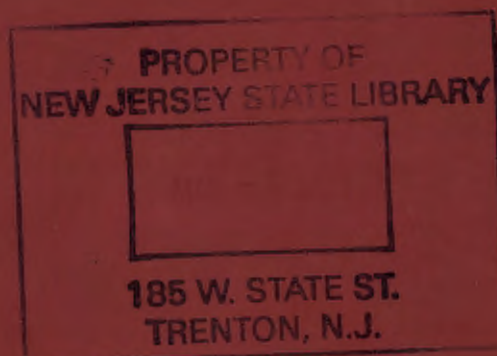




**STATE INVESTMENT COUNCIL
DEPARTMENT OF THE TREASURY
STATE OF NEW JERSEY**



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FORTY-FOURTH ANNUAL REPORT

For the Fiscal Year Ended June 30, 1994



CHRISTINE TODD WHITMAN
Governor



BRIAN W. CLYMER
State Treasurer

A Report to
Governor Christine Todd Whitman,
the Members of the
New Jersey Legislature
and the State Treasurer

Submitted by the
State Investment Council

For the Fiscal Year ended June 30, 1994

736
November 15, 1994

To The Honorable:
The Governor;
The Legislature;
The State Treasurer:

We are pleased to submit the Annual Report of the Division of Investment, Department of the Treasury, for the fiscal year ended June 30, 1994, as required by Section 13, P.L. 1950, c. 270. The report is a summary of the activities of the Division during the year. Separate reports are also prepared for the Supplemental Annuity Collective Trust and the State of New Jersey Cash Management Fund, both of which are available upon request from the Investment Division.

The Investment Division, under the jurisdiction of the State Investment Council, has the investment responsibility for 126 funds, including seven pension and annuity funds. The book value of all funds on June 30, 1994, was \$36.0 billion, compared to \$35.3 billion at the end of the prior year, and the market value of the funds was \$43.8 billion, compared with \$44.9 billion at the end of the previous fiscal year. The Council includes ten persons appointed to fixed terms. Five employee representatives are appointed by their respective pension fund boards for one year terms, and five members are appointed by the Governor for staggered five year terms. In fiscal 1992, the Legislature provided for an eleventh member of the Council, to be appointed by the Governor from a list of three candidates to be nominated jointly by the President of the Senate and the Speaker of the Assembly. The new law also provided that all gubernatorial appointments to the pension fund boards and to the Council are subject to the advice and consent of the State Senate. To date, the eleventh member of the Council has not been nominated or appointed, and three gubernatorial appointees to the Council are serving beyond the expiration of their terms while they await legislative consent for their proposed reappointment. State law requires that no Council member shall hold any office, position or employment with any political party, and none can benefit from the transactions of the Division.

The investment of state funds by the Division benefits all citizens of the State of New Jersey. The investment income generated by the pension funds contributes directly to the assets of the various pension funds and the retirement security of pension fund beneficiaries. The income generated by the investment of the pension funds and other state funds also contributes to the funding of services and benefits provided by the state to its citizens and thus directly benefits the taxpayers of New Jersey.

Pension fund returns were slightly below break-even in fiscal 1994, as the domestic stock was virtually flat and the bond market declined. International markets showed positive returns. The estimated total return of the pension funds, which includes changes in market values of the securities held by the funds and dividend and interest income over the year, was (0.7) percent, which compares with a 12.5 percent return in fiscal 1993. For the past five fiscal years the estimated average annual total return earned by the pension funds was 9.4 percent. These total returns of the pension funds ranked the Division in the bottom quarter of all State fund managers in fiscal 1994, and in the top quarter for the five and ten year periods ended June 30, 1994. Appendix II sets forth estimated total returns of the state administered pension funds for the past five years.

All investments under the supervision of the Council must conform to standards of prudence set by state law, which mandate that the Division make investments in which fiduciaries of trust estates may legally invest. Such investments are further defined as investments in property of every nature, provided the fiduciary shall exercise care and judgment under the circumstances then prevailing, which persons of ordinary prudence and reasonable discretion exercise. The Division is bound by law to make prudent investments for the sole benefit of the beneficiaries of the various funds under the supervision of the Council, and the Division may not make any concession as to rate, risk or terms which would benefit any other party at the expense of the beneficiaries of such funds.

Over the years, members of the public, political figures and lobbyists have raised the question of whether investments under the jurisdiction of the Council should be guided by non-financial considerations. Such investments could be directed regionally or toward specific capital markets or could be averted from certain areas. The Council has considered each of these issues as they have arisen and has concluded, with the concurrence of the Attorney General's office, that state law requires that the financial merits of each investment are the only factors that should be considered. Social and regional issues may have financial implications for fund beneficiaries, and the Division analyzes such implications in the determination of its investment decisions, but it is only those financial risk and return characteristics that are taken into account in making the final investment decisions. The policies of the Council regarding social investment are discussed in detail herein. Council policies have been reviewed by special gubernatorial commissions established by both Governors Byrne and Kean, representing different political parties, and both commissions support the present structure and policies of the Council. These reports are discussed further herein.

The Council is pleased to note that the large majority of the corporate debt obligations and equities held by the Division have been issued by corporations which are identified as New Jersey employers. The pension funds have investments in major companies who have their headquarters in New Jersey and in out-of-state companies which provide employment within the state. From time to time the Council has been asked to consider direct investment in personal loans, individual mortgages and loans to small businesses. The Division does not have the facilities or personnel to make such loans, but it does participate indirectly in these areas through investments in securities of U.S. Government agencies and other financial intermediaries. The Council has been asked to provide below market interest rates for New Jersey investment programs for housing and economic development, but has declined to do so since Council members believe that to do so would be a violation of their fiduciary responsibilities to the beneficiaries of the funds under their supervision. Furthermore, in many instances, such programs can be funded through tax-exempt bond financing, which generally provides favorable interest rates to borrowers.

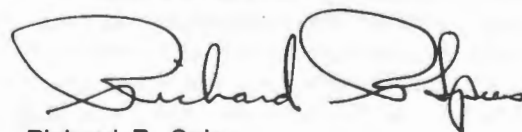
Over the years, the Council has addressed the major issues which concern fiduciaries, such as the standards for investment, the allocation of invested funds among asset classes and the globalization of investments. In fiscal 1993 and 1994, the Council addressed the issue of the Division's budget and staffing and concluded that additional resources were needed in order to support adequately the investment programs of the state. The Council addressed this issue to the appropriate state officials and members of the Legislature, and the fiscal 1994 and 1995 budgets have provided for additional funding for the Division, and the additional programs are being implemented.

In April 1994, Governor Whitman signed legislation which repealed the legislation which was enacted in 1985 and which prohibited investment by the pension and annuity funds of the State in companies doing business in South Africa. The effect of the repeal will be to provide access by the Division to a more diversified universe of securities.

The Council members are grateful for the many years of outstanding service to the Division which was provided by Dick McGowan, who retired during the year.

For each of the past forty-four years, the Council has requested and obtained a review of the records and procedures of the Division by an independent accountant. The accountant's report for the current year is included in this report.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "Richard R. Spies", is written over a horizontal line.

Richard R. Spies
Chair

The State Investment Council



RICHARD R. SPIES
Chair of the Council



ROBERT T. HOFFMAN



LESTER Z. LIEBERMAN



WILLIAM W. PRIEST, JR.



ARTHUR W. WHITE, JR.



NANCY A. NAUGHTON
Consolidated Police and
Firemen's Pension Fund;
Vice Chair of the Council



HARRY W. BALDWIN
Teachers' Pension and
Annuity Fund



STEPHEN A. FLOREK II
Public Employees'
Retirement System



M. MICHAEL DI SALVO
Police and Firemen's
Retirement System



KEVIN MCPARTLAND
State Police Retirement
System

Division of Investment



ROLAND M. MACHOLD
Director



STEVEN E. KORNRUMPF
Deputy Director



Staff of the Division on the steps of the State Street Square, 50 West State St., Trenton, New Jersey.



Administration Group: Gilles Michel, Dolores Ewanis, Celeste Brennan, Cindy Everett, Roland Machold, Cathy Ryan, Steve Kornrumpf, Pat Osvai and Linda Coughlan.



Portfolio Management Group: Linda Thompson, Bruce Smith, Sandra Holmes, Victor Yu and Linda Brooks.



Trading Group: Rob Adriaanse, Bob Schragger, Patti Hricak, Michael Wszolek, Mary Ann Smith, Celia Daino, Jack Jacknowitz, Helen Imbalzano and Tim Patton.



Research Group: Brian Arena, Denise Szeker, Ed Pittman, Jim Vandervort, Karin Hollinger, Tom Montalto and Linda Gaspari.



Common Fund Accounting Group: Mary Vassiliou, Dan Costanzo, Manick Jhingade, Andrea Szul, John Jusiewicz, Madeline Amico, Elsie Lawrence, Carletha Murray, Patty DiMemmo and Joe Adubato.



Bookkeeping Group: Roxanne Tyner, Nancy Brancolino, Ken Scott, Olga Grozio and Charles Coleman.



Cashier Group: Bea Wolfe, Kass Cole, Loretta Sytnik, Rosetta Muccie, John Giovannetti, Bart Pericoloso and Melissa Cook.



Data Processing Group: Ed Meyers, Karen Consalvi, Nick Maximenia and Sandi Glass.

FIVE YEAR SUMMARY

Fiscal Year Ended June 30,					
1990	1991	1992	1993	1994	
\$ Millions					
\$21,697	\$24,081	\$26,223	\$26,911	\$27,394	
26,286	29,924	32,981	35,309	35,990	
\$26,335	\$29,272	\$33,490	\$36,413	\$35,167	
30,978	35,166	40,313	44,875	43,787	
\$ 976	\$ 1,011	\$ 1,006	\$ 671	\$ 411	
8,712	10,139	11,794	13,673	12,836	
3,656	3,951	3,787	2,662	2,104	
12,725	13,977	16,379	18,633	19,351	
266	194	524	774	465	
<u>\$26,335</u>	<u>\$29,272</u>	<u>\$33,490</u>	<u>\$36,413</u>	<u>\$35,167</u>	
\$ 1,517	\$ 1,653	\$ 1,829	\$ 1,721	\$ 1,522	
1,867	2,011	2,166	2,053	1,823	
18.7%	8.0%	12.6%	12.2%	(0.7)%	
7.2	10.3	14.5	14.0	(1.6)	
—	—	22.3	9.8	2.7	
13.3	9.3 (3)	13.8	12.5	(0.7)	
14.7	5.8	12.9	13.4	(0.7)	
19.7	5.3	10.6	11.9	(0.1)	
7.1	10.5	14.7	10.5	0.1	
9.7%	12.0%	14.0%	9.1%	(0.9)%	
6.0	10.6	16.8	16.3	(3.6)	
7.1	10.2	14.2	13.2	(1.5)	
16.5	7.4	13.4	13.6	1.4	
22.8	4.7	17.1	9.2	6.0	
7.0	10.0	20.5	10.9	5.1	
3.3	(11.5)	(0.7)	20.3	17.0	
\$ 5,740	\$ 6,946	\$ 8,045	\$ 9,570	\$ 9,023	
1,437	2,130	3,111	4,018	3,488	
8.57%	7.47%	5.30%	3.63%	3.46%	
8.42	7.30	5.12	3.42	3.30%	
121	115	117	121	126	
34,600	38,298	40,534	39,282	44,544	

1. Total rate of return includes income and changes in market prices for securities held by the funds during the period shown.
2. Common Pension Funds A, B and D are the principal vehicles for investment by the pension funds in domestic stocks, domestic bonds, and international securities, respectively. The returns cited are for the whole portfolios and reflect a small amount of cash equivalents. Returns for stocks and bonds alone are shown in Appendix II, as are estimated total returns for the pension funds.
3. In the course of fiscal 1991, the Division initiated a new Common Pension Fund D for the purpose of pooling investments of the pension funds in international securities. The estimated return of the pension funds for fiscal 1991 reflects the initial returns of investments in the new fund.

The Year's Activities

Summary Financial Information

The 126 investment funds under the supervision of the Council on June 30, 1994, had a book value of \$36.0 billion. This total represents an increase of 2.0 percent over the 1993 fiscal year-end total of \$35.3 billion held by 121 funds. The investment funds had a market value of \$43.8 billion at June 30, 1994, a decrease of 2.4 percent from the market value of \$44.9 billion at June 30, 1993. The market value of the seven pension funds decreased from \$36.4 billion at June 30, 1993, to \$35.2 billion at June 30, 1994. The market value of the pension funds fell slightly due to flat to down markets during the year and lower levels of employer contributions.

Investment income for all funds for fiscal 1994 amounted to \$1.8 billion as compared with \$2.1 billion last year. Income decreased slightly as interest rates declined during the year and the pension funds' commitment to stocks was increased.

During the year, the Division of Investment purchased securities with a par value of \$82.3 billion. Approximately 25.0 percent of this amount, or \$20.6 billion, represented the overnight investment of surplus balances in the State's cash accounts. In fiscal 1993, the Division purchased securities with a par value of \$83.2 billion, of which \$18.0 billion was generated by overnight investments. During fiscal 1994, the Division's net holdings of mortgages decreased from \$2.6 billion to \$1.7 billion, due to maturities and continuing refunding of mortgages by home owners.

The Division sold securities totaling \$13.8 billion in fiscal 1994, compared with sales of \$12.5 billion in the prior year. Many of the sales were made to meet cash requirements or to take advantage of market opportunities. Such sales resulted in net realized profits of \$1.2 billion during the year, compared with \$443 million for the prior year. The transactions information in this paragraph includes transactions effected within the common funds, which are not included separately in the financial summaries in this report.

"Regular Interest Rates"

The pension revaluation law, which was enacted in June, 1993, sets the "regular interest rate" of the pension funds at 8¾ percent, which reflects expected income and market returns of the funds over time. The law further provides that the "regular interest

rate" shall bear a reasonable relationship to the rate of earnings on investments, based on the market value of assets, but shall not exceed the assumed percentage rate of increase applied to salaries plus 3 percent. At present the average of the assumed percentage rate of increase applied to salaries is 5.95 percent.

Fixed Income

Total fixed income allocations for new investment in fiscal 1994 totalled \$1,490 million, of which \$100 million was allocated to the purchase of U.S. Government and corporate debt securities, and \$1,390 million was allocated for international fixed income investment through Common Pension Fund D.

In fiscal 1994, the Division purchased \$370 million of FHLMC and FNMA 15 year and 30 year mortgage-backed securities and \$39 million of collateralized mortgage obligations (CMOs). Principal repayments on mortgage-backed securities held by the Division for fiscal 1994 totaled \$350 million.

In fiscal 1994, the Division sold \$633 million of FHLMC and FNMA mortgages and realized profits of \$32.7 million on the sales.

In October 1985, the Division developed a program for the state pension funds to purchase eligible mortgage pools from interested New Jersey financial institutions. The Division calls such institutions on a monthly basis and offers to purchase eligible mortgage pools at the prevailing market prices for similar pools.

In fiscal 1992, a law was enacted which allocated up to 10% of the Police and Firemen's Retirement Fund to mortgages for members of the Fund. In fiscal 1994, the fund purchased \$179 million of such mortgages.

Common Pension Funds

Under the authority granted by P.L. 1970, c. 270, the Division has created Common Pension Fund A, Common Pension Fund B and Common Pension Fund D to consolidate investments of five of the pension systems in domestic stocks, domestic bonds and international investments, respectively. At June 30, 1994, the market value of the units of ownership of Common Pension Fund A, Common Pension Fund B and Common Pension Fund D were \$18.3 billion, \$10.7 billion and \$3.4 billion, respectively. The State

of New Jersey Cash Management Fund provides a vehicle for the pension funds to make short-term investments.

Total Rate of Return Calculations for Select Portfolios

Calculations of total rate of return reflect both income and changes of market values of securities in a portfolio over a specific period of time. The calculation includes unrealized market gains or losses and thus is not indicative of the cash returns on the portfolio. It would be indicative of cash returns if the portfolio were liquidated at the end of each period of measurement, but such liquidation would be impractical for portfolios of the size managed by the Division. Furthermore, the calculation is historical and is not predictive of future returns. However, the calculation of total rate of return is a means of comparing returns of varying types of portfolios by a common standard.

At the present time the Division is only able to calculate total rate of return for the pension fund portfolios and selected other portfolios. These historical returns are shown on page 7 herein.

SEI Evaluation Services has provided the Division with calculations of total return, and their data shows that the total returns for Common Pension Funds A, B and D in fiscal 1994 were (0.7) percent, (1.6) percent and 2.7 percent, respectively. The estimated total return of the aggregate pension fund portfolios was approximately (0.7) percent in fiscal 1994, compared with returns of 12.5 percent in fiscal 1993 and 13.8 percent in fiscal 1992. It is difficult for public pension funds to find a common basis for reporting. However, several states have developed a format for common reporting practices and the Investment Division has provided these estimates in response to this format in Appendix II to this report.

The estimated total returns for the pension funds do not include the mortgage loan program of the Police and Firemen's Retirement System. This program was established by law in fiscal 1992, and provides that members of the fund may receive mortgages from the fund at rates which are fixed by formula. The law further provides that the fund may not sell the mortgages, and no independent market exists for them. Consequently, the Council has taken action to exclude the program from calculations of the total return for the fund. The attached financial statements include \$484 million of assets of the

mortgage loan program at both book and market value at June 30, 1994.

The State of New Jersey Cash Management Fund

The Division initiated the first investment in the State of New Jersey Cash Management Fund in May 1977. The fund provides the state and its municipalities with a vehicle for short term investment. At that time state statutes provided that only certain state funds were eligible to participate in the fund, but, in November 1977, legislation was enacted (P.L. 1977, c. 281), which permitted counties, municipalities, school districts and the agencies and authorities created by any of these entities or the state ("Other-than-State" participants) to participate in the fund on a voluntary basis.

The total book value of the units of participation in the fund decreased from \$9.6 billion at June 30, 1993 to \$9.0 billion at June 30, 1994, due to increased withdrawals from the State's pension accounts and the accounts of participating municipalities and state agencies.

The net investment income of the fund was \$309 million in fiscal 1994, compared with \$344 million in fiscal 1993. The number of participating state funds increased from 121 to 126 during the year. The income of the fund decreased in fiscal 1994, due to lower interest rates available in financial markets.

In fiscal 1994, the number of "Other-than-State" participants increased from 827 to 881, and the aggregate investment of "Other-than-State" participants was \$3.5 billion at the end of fiscal 1994, compared with \$4.0 billion at the end of fiscal 1993.

The average daily annualized rate of return to participating state accounts and accounts of the pension funds was 3.46 percent during fiscal 1994, compared with 3.63 percent in fiscal 1993. During fiscal 1994, the highest daily annualized rate of return to "Other-than-State" participants was 4.14 percent on June 30, 1994, and the lowest was 3.10 percent on August 16, 1993 and September 3, 1993. The average daily annualized rate of return to "Other-than-State" participants, which is net of two small charges, was 3.30 percent in fiscal 1994, compared with 3.42 percent in fiscal 1993.

These rates are the average of all daily rates realized during the year and do not reflect the compounding effect of leaving moneys on deposit over time. The compound rate of return for "Other-than-

State" funds in fiscal 1994 was 3.46 percent, compared with 3.61 percent in the prior year. The lower rates of return during fiscal 1994 were the result of lower interest rates available in the markets for short-term debt investments, as interest rates were lowered in response to a national recession. However, by the end of the year, short-term interest rates moved upwards as the economy recovered.

In December, 1994, Orange County, California,

declared bankruptcy due to losses incurred by its short-term investment fund. Published reports indicate that these losses were the result of borrowings by that fund and investment in long-term securities and derivatives. None of these practices are permitted for the State of New Jersey Cash Management Fund under the Council's regulations, which only permit conservative investment practices appropriate for such a fund.

Historical Background

Legislative History

Fiscal 1994 marks forty-four years of operation of the Division of Investment of the Department of the Treasury of New Jersey. During that time the investment responsibility of the State Investment Council has increased from 20 funds in 1950, with a book value of \$350 million, to 126 funds in 1994, with a book value of \$36.0 billion and a market value of \$43.8 billion.

The Division was created by P.L. 1950, c. 270, which became effective on July 1, 1950. An important objective of the statute creating the Division was to centralize all functions relating to purchases, sales or exchanges of securities for the state's diverse funds under experienced and professional management.

The statute provides for a State Investment Council and a Director. The original legislation provided that the Council consisted of ten members, five appointed for staggered five-year terms by the Governor and five appointed for one-year terms by the respective boards of trustees of five of the pension systems. The statute was amended by P.L. 1992, c. 125 to provide for an eleventh member of the Council, to be appointed by the Governor from among three persons nominated jointly by the President of the Senate and the Speaker of the General Assembly. The eleventh member serves for a five year term. The new law also provides that all Gubernatorial appointments to the Council are subject to the advice and consent of the Senate. The statute provides that no member of the Council shall hold any office, position or employment in any political party, nor shall any member benefit directly or indirectly from any transaction made by the Director of the Division. Members of the Council serve without compensation.

The statute vests investment authority in the Director of the Division. The Director is appointed by the

State Treasurer from candidates for the office selected by the Council.

The role of the Council is to formulate investment procedures and policies to be followed by the Director. State legislation provides that the Council may issue regulations which specifically approve and authorize any form of investment. New regulations adopted by the Council from time to time are formal documents which are filed with the Secretary of State and reported in the New Jersey Register.

The Council periodically reviews the investment objectives of all of the individual funds under its supervision. With respect to the pension funds, the primary investment objectives are the preservation of capital and the realization over time of earnings sufficient to meet or exceed the regular interest rate established for the actuaries in their determinations of the assets and liabilities of each pension fund system. The Council sets as a further investment objective the realization of the greatest possible returns on investment, commensurate with the standards of risk and prudence set forth within the Regulations of the Council.

Prior to 1950, investment was limited by law to United States Government and municipal obligations. P.L. 1950, c. 270, provided that investment could also be made in obligations which are legal investments for savings banks within the state. Since 1950 the Legislature has enacted a number of amendments to P.L. 1950, c. 270, which were designed to increase the scope of potential investment opportunities and provide a foundation for achieving better portfolio balance and diversification.

Such legislation broadened the authority of the Division to include investment in short-term debt obligations, including commercial paper and certificates of deposit, and certain Canadian government and provincial obligations payable in U.S. dollars

(P.L. 1952, c. 17, and P.L. 1971, c. 176); and subsequently, investment in property of every nature, provided the fiduciary shall exercise care and judgment under the circumstances then prevailing, which persons of ordinary prudence and reasonable discretion exercise (P.L. 1975, c. 337).

The Legislature has also enacted laws which permit the operation of common funds. P.L. 1970, c. 270, permits the Director to combine, for the purpose of investment, money and property belonging to the various funds in the custody of the State Treasurer. Under this authority the Council and the Division have established Common Pension Fund A, Common Pension Fund B and Common Pension Fund D, which pool a portion of the investments of five pension funds in domestic stocks, domestic bonds and international investments, respectively. This law also authorized the creation of the State of New Jersey Cash Management Fund, which was created in 1977 to pool investments in short-term debt obligations by certain state funds, including the pension funds. In fiscal 1978, legislation (P.L. 1977, c. 281) was enacted which permits counties, municipalities, school districts and the agencies and authorities created by any of these entities or the state to participate in the fund. Such participation began in January 1978.

In August 1985, Governor Kean signed into law an act, P.L. 1985, c. 308, which states that "no assets of any pension and annuity fund shall be invested in any bank or financial institution which directly or through a subsidiary has outstanding loans to the Republic of South Africa or its instrumentalities, and no assets shall be invested in the stocks, securities or other obligations of any company engaged in business in or with the Republic of South Africa." Furthermore, the Council and the Division shall effect divestment "within three years of the effective date of the act." The final report to the Legislature for the period August 27, 1985 through August 27, 1988 was attached in full as Appendix II to the Council's Annual Report for fiscal 1988. This report showed that the Division's divestment program was completed in full, and the Division has remained in compliance with the law. In April 1994, Governor Whitman signed legislation (P.L. 1994, c. 19) which repealed the state's South African sanctions, and the Division can now invest in a broader universe of domestic and international securities.

In July 1987, Governor Kean signed into law an act, P.L. 1987, c. 177, which directs the Director of the Division of Investment to investigate the extent to

which United States' corporations doing business in Northern Ireland, in which the assets of any State pension or annuity fund are invested, adhere to principles of non-discrimination in employment and freedom of workplace opportunity, as defined in the law by various standards commonly referred to as the MacBride principles. Furthermore, the law requires the Director to file an annual report with the Legislature and to initiate and support shareholder petitions or initiatives requiring adherence to the MacBride principles. Subsequent to the enactment of the law, the Council adopted procedures to comply with the law, and the Director has filed the required reports, copies of which are available upon request.

In June 1992, Governor Florio signed an act (P.L. 1992, c. 41) which provided for the revaluation of the pension funds from a book valuation basis to a market valuation basis for the purposes of actuarial calculations. The act changed the economic assumptions of the funds to reflect market valuations and modified the actuarial methodologies for the funds. The act also provided for an eleventh member of the Council, to be appointed by the Governor from a list to be submitted jointly by the President of the Senate and the Speaker of the Assembly.

In December 1991, Governor Florio signed into law an act (P.L. 1991, c. 414) which provides that up to 10 percent of the assets of the Police and Firemen's Retirement System may be made available to eligible members of that fund for mortgage loans at rates which are set by formula. The law provides that the Treasurer shall delegate the administration of the mortgage loan program to the New Jersey Housing and Mortgage Finance Agency, and, with certain advice, the Treasurer shall set the mortgage loan standards. In June 1992, this law was amended by an act (P.L. 1992, c. 78) which clarified that the mortgage loan program is an investment program to be administered as part of the state's general investment program. At its meeting in July 1992, the Council distinguished the mortgage loan program from other investment programs under the supervision of the Council and specified that the returns of the pension funds will be segregated from the mortgage loan program for the purposes of performance reporting.

Regulations of the State Investment Council

In addition to the investment guidelines established by law, the State Investment Council sets specific

investment policies by regulations in accordance with the authority provided to it by P.L. 1950, c. 270.

Present regulations of the State Investment Council limit the authority of the Director to invest in common stock. At present, the Council limits the permissible level of the aggregate market value of pension fund stock holdings in Common Pension Funds A and D to 60 percent of the market value of any one pension fund. At June 30, 1994, the aggregate common stock holdings of the pension funds were 55.0 percent of the total market value of the funds. Attached hereto as Appendix I is an unaudited summary of investments by major category for individual pension funds.

The regulations of the State Investment Council also set criteria for the Division's investments in long-term debt obligations. These regulations require issuers of debt to meet certain standards, which, depending on the type of security and the nature of the issuer, may refer to the capitalization, operating history, interest coverage, bond rating or other criteria relating to the issuer.

In the case of mortgages, Council regulations require, in almost all cases, that the securities be directly or indirectly supported by the Federal government. One regulation permits investment in pools of conventional mortgages which meet specific eligibility standards.

All of the regulations of the State Investment Council, including the regulations which pertain to the common funds, have been published in the New Jersey Register and are on file with the Secretary of State.

The Council constantly reviews its regulations which govern the activities of the Division. As a result, a number of regulations are revised during each year. These refinements keep the Council's policies abreast of economic, fiscal and accounting trends.

As a consequence of the State's sunset law all of the regulations of the Council were resubmitted to the legislative review process in fiscal 1991 and were readopted with various modifications and clarifications early in fiscal 1992.

In fiscal 1994, the Council acted to reduce the required rating of sovereign countries from double-A by both rating agencies to double-A by only one agency. The standard affects the Division's purchases of international stocks and bonds, and the effect of the revision was to permit investments in Italy and Portugal.

Reviews of Major Policy Issues in Recent Years

During fiscal 1984 and 1985, the Council reviewed a number of major policy issues which had been raised by Governor Kean's Pension Study Commission and its own review and analysis. Early in fiscal 1985, the Council made the following findings and recommendations.

The Council members agreed that the salary structure, budget limitations of the Division, lack of personnel depth and the inflexibility of the Civil Service system posed grave dangers for the successful management of state funds and state-administered pension plans. The Council agreed that any complete solution to the budgeting, staffing, salary and Civil Service issues would provide that: (a) funding of the Division's budget would be made from pension fund income and other fees, with all expenses of the Division subject to the discretion of the Council; (b) all professional employees would serve at the pleasure of the Council, although nonprofessional employees could remain in the Civil Service salary structure and system; (c) professional salaries would be set by the Council and possibly could be designed to incorporate performance bonuses; and (d) the Council would have the flexibility to provide necessary personnel depth for the Division. The Council has taken these matters up with appropriate State Officials, but, to date, only the first part of item (a) above has been implemented.

At that time, the Council also confirmed the investment objectives for the pension funds, which are as follows: "primary investment objectives are the preservation of capital and the realization over time of earnings sufficient to meet or exceed the regular interest rate established for the actuaries in their determination of the assets and liabilities of each pension fund system. The Council sets as a further investment objective the realization of the greatest possible returns on investment commensurate with the standards of risk and prudence set forth within the Regulations of the Council."

At that time, the Council reviewed the stated objectives and discussed the possibility of amending them to include reference to specific market indices, the rate of inflation or percentile rankings of other managers. They also considered whether a higher risk profile for the portfolios would be appropriate, under the assumption that a diversified portfolio of higher risk securities could, in the aggregate, provide higher returns over the long term. The Council con-

cluded that the pension funds' primary objectives were preservation of capital and income, and that these requirements were inherent in the state prudence and pension laws.

The Council noted that its regulations had broadened the permissible investment universe of the Division in recent years to include options, real estate, conventional mortgages and a broader list of common stocks. The Council concluded at that time that the investment regulations provided for a satisfactory range of investment opportunities within the Council's fiduciary standards, and that new investment opportunities could be considered in the traditional manner as they arose.

At that time, the Council also reviewed and confirmed present standards for selecting stocks which are set forth below:

a. The company should have growth in revenues and earnings which exceed growth in the Gross National Product;

b. The company should have a strong market franchise, unique products and proven marketing capability;

c. The company's management should have demonstrated the ability to preserve profit margins, to avoid earnings surprises and to take the needed initiatives to preserve and improve upon the company's strengths;

d. The company should have a capitalization which is not heavily leveraged, thereby allowing it more flexibility to finance future expansion; the company should not be unduly capital intensive, which might expose it to the necessities of raising capital at times when capital markets were unduly expensive; and, the company should demonstrate that it can generate capital internally for growth;

e. The market for the company's shares should have enough liquidity to permit the orderly acquisition and disposition of a full position; and

f. The company should have conservative accounting practices.

The standards are only meant to serve as guidelines. The Council agreed that not all companies on its Approved List will meet all of these guidelines; however, a failure to meet most of these guidelines will be cause for concern. In addition, the Council believes that good corporate citizenship enhances the value of a company, and, conversely, that poor corporate citizenship detracts from a company's value.

The Council considered the use of outside managers. However, opinions from the Attorney

General's office indicated that the use of outside managers by the Division is not legal under state law. The Council concluded that it might like to use outside managers in specialized circumstances, such as equity real estate investment, but that it would be necessary to modify the state's general prudence law to permit such use. The Division has supported such legislation when it has been introduced. At present, a revision of the state prudence law is being considered by the state legislature. The proposed revisions would include the "whole plan" principle, which would broaden the range of potential investment by fiduciaries.

In fiscal 1990, the Council continued to review the legislative and regulatory definitions of risk and return for the pension funds and studied various asset allocation and portfolio optimization simulations. As a result of these reviews and studies, in July 1990, the Council approved four new regulations which enabled the Division to invest in international stocks and bonds. In doing so, the Council acknowledged that the world is approaching a global economy, wherein large corporations based abroad have major manufacturing plants and significant numbers of employees in the United States, and, conversely, many corporations based in the United States maintain substantial operations abroad. Finally, the studies showed that international investments in developed countries had historically provided higher returns with lower levels of risk than had investments limited to the United States.

During fiscal 1990, the Council received the reports of two independent actuarial firms, Buck Consultants and Actuarial Science Associates (ASA), which had been retained by the Treasury Department to provide comprehensive analyses of the Public Employees' Retirement System, including both benefit and investment issues. With respect to the state's investment program, Buck Consultants concluded that "the state's present portfolio appears to be carefully thought out and, in terms of modern portfolio theory, efficient within the constraints of the fund," and ASA stated that "the current asset allocation was appropriate." Both reports endorsed the concept of international investing as a means of adding diversification to the portfolio and thus reducing portfolio risk.

In fiscal 1991, the Council once again reviewed all of its regulations in view of their prospective expiration under the provisions of the State's sunset law. Many regulations were readopted without change, and others were modified in minor ways to add clarity and

to modernize them in accordance with current financial practices. As was noted before, the most significant changes permitted the Division to invest up to 60 percent of total pension fund assets in stocks, and up to 15 percent of total assets in international securities.

In fiscal 1993, the Council studied the resources provided to the Division and concluded that the resources provided to the Division were not adequate to fully fund the Division's investment programs, including several programs which had the potential to provide significant additional returns to the state funds over the years. The Council discussed its concerns with the appropriate state officials and with members of the legislature, and the state's budget for fiscal 1995 includes additional funding for the Division.

Also, in both fiscal 1993 and 1994, the Council again reviewed the asset allocation policies set forth in the Council regulations for the state administered pension funds, and decided that such policies continued to be appropriate.

Council Procedures and Reports

The State Investment Council meets at least six

times a year, and the Executive Committee of the Council may meet in intervening months. In addition to reviewing and formulating all major policy issues related to the state's investments, the Council reviews the investment programs and returns of each fund on a periodic basis. Furthermore, each year the Council reviews each of the major classes of assets held by the Division.

Almost all of the investment transactions of the Division are effected through competitive bidding. In specific markets which require that the Division exercise discretion in the choice of a bank or broker, such discretion is exercised according to an allocation plan prepared by the Director on the basis of the Division's evaluation of the merits of the services provided by each bank or broker. The allocation plan is reviewed by the State Investment Council, and the final allocation of commissions is audited by the Division's independent accountants.

The provisions of P.L. 1950, c. 270, also require that the Director of the Division prepare and make available to the public a monthly report of all transactions effected by the Division. This report lists all sales, purchases, exchanges and commissions paid by the Division for all of the Division's transactions. The report is provided to the legislature, state officials, the press and the public.

Social Investment

There has been a spirited public debate for many years on the subject of "strategic" or "targeted" investment, whereby investments are either directed towards areas which are deemed to be socially desirable or withheld from areas which are deemed to be socially undesirable. The Council has taken the position that the Division is bound by law to make prudent investments for the sole and direct financial benefit of the beneficiaries of the various funds under its supervision and that the Division may not make any concession as to rate, risk or terms which would benefit any other party at the expense of the beneficiaries of the funds.

The Council and the Division are open to any investment program which would benefit socially desirable purposes, particularly investment within the State of New Jersey. All such investment programs are reviewed by the Division and the Council on a case-by-case basis from a financial point of view, and

investment decisions are made in the light of such a review and the prudence standards cited above.

In fiscal 1982, the Council reviewed two investment concepts which would have directed pension fund assets to mortgage markets in New Jersey. The Council found that one of these was concessionary and thus was prohibited by state law. In the second instance, the Council reviewed a complex concept for investing in growing equity mortgages and concluded that the concept was feasible; however, no investments were initiated due to changing market conditions.

In fiscal 1986, the Division initiated a program whereby on a monthly basis the Division offered to purchase New Jersey mortgages from New Jersey banking institutions at market rates as mandated by prudence law. Once a month the Division determines the true market level for a package of mortgages backed by any eligible agency supported by the U.S.

Government. The Division immediately offers this price to interested New Jersey financial institutions for identical mortgages which originate in New Jersey. In effect, the Division creates an "open window" to buy at market prices New Jersey mortgages supported by the U.S. Government. In fiscal 1994, approximately \$1 million of New Jersey mortgages were purchased by the Division under this program.

Reports of Gubernatorial Commissions

In fiscal 1982, former Governor Brendan Byrne created a task force to study the use of state pension funds to spur economic activity within the State. The task force did not find evidence that pension funds can be invested to achieve secondary objectives without compromising the primary goal of maximizing the investment return for the beneficiaries, and the task force concluded that no formal change in investment policy should be made. The report of this task force is described in greater detail in annual reports of prior years.

During fiscal 1983, former Governor Kean created the Governor's Pension Study Commission to review all aspects of the state-administered pension funds. The Commission's conclusions relating to the policies and practices of pension fund investment, as reported on March 15, 1984, are quoted below in their entirety:

"1. The current structure within which New Jersey's pension investments are made is, in our judgment, both sensible and appropriate for the task and should not be changed in any substantive way. The balance which exists between the accountability of the pension investment fiduciaries to the beneficiaries of the funds with the insulation from political influence is of decisive importance. It is crucial that the twin pillars of fiduciary responsibility—namely, prudence and loyalty—be maintained. The current structure allows for and facilitates that to a better extent than any other we have seen or considered.

2. The Division of Investment should continue to consider investment alternatives with respect to improving potential returns. An increase in the equity is an example of a positive step already taken. The Investment Council should also consider other investment options such as venture capital pools, options, commercial real estate and a broader universe of stocks as long as these investment options meet the fiduciary standards of the Council.

3. The resources of the Division of Investment are too limited. The relatively small staff of 61 is not commensurate with the responsibility of the Division. Moreover, the salaries which attract high quality investors are not currently available. We noted that the committee

whose report led to the creation of the Division and the State Investment Council recommended that the investment managers be paid at a level commensurate with their responsibilities. This is not being done currently and should be addressed as soon as possible.

If the State were to allow the operation of the Division to be funded from the returns on investment, this would make available money for outside counsel of a technical sort. Legal counsel, data processing specialists, and investment advisors would be made available to the Division to enhance returns to fund the operation of the investment structure. New Jersey should take advantage of this.

4. All investment professionals of the Division of Investment should serve at the discretion of the State Investment Council. This would be consistent with the statutory purpose of the Investment Council. Current Civil Service regulations are an impediment to fostering the best investment operation.

5. The Investment Council should consider non-economic criteria in its decision-making process only insofar as these criteria have a direct impact on economic criteria. Socially dictated investments and socially sensitive investments are, in the long run, counter-productive. Nonetheless, the efforts which the Division and the Council have made to take into account non-economic criteria have been laudable. The consideration of generally accepted corporate practices, such as those covered by the Sullivan principles, have been a healthy factor in New Jersey's investment policy. These considerations should continue to be made and the Council and the Division should be alert to non-economic considerations which may adversely affect the pension portfolio.

6. The beneficiaries of the pension funds should be the sole concern of the State Investment Council and the Division. Non-beneficiaries should not be taken into account by the Council or the Division in its investment programs. Consequently, it would be appropriate for State statutes to include the ERISA language stipulating the 'sole benefit' provision of that federal law."

Studies commissioned by two governors of different political parties have reviewed and confirmed the mandate of state law that the Division make prudent investments for the sole and direct benefit of the beneficiaries of the several funds.

The Council has responded in full to those recommendations over which the Council has jurisdiction, such as the appropriate asset allocation and breadth of potential investment of the pension funds. However, the Council cannot independently respond to recommendations regarding staffing, compensation and budget support, which are the prerogative of the legislature. During fiscal 1994, the Council again reviewed these issues and has taken them up with the appropriate authorities. As a result of these

concerns, the fiscal 1994 and 1995 budgets have provided incremental funding for the Division for certain investment programs.

Policies of the Council Towards Social Investment

The State Investment Council has determined that social and financial considerations are not mutually exclusive, and many social considerations may have significant financial implications. Furthermore, investments which benefit the fund beneficiaries need not exclude investments in New Jersey or those which advance other social goals. All of the members of the Council are New Jersey residents, and for many years the Division and the Council have reflected concerns of New Jerseyans through internal policy guidelines. In 1984 these were codified, and they are listed below:

1. The Division of Investment should prefer investments in New Jersey in instances where such investments provide the same or better terms and returns in the marketplace as are available for out-of-state investment and where such investments meet the prudence standards set by law and the State Investment Council.

2. The Division of Investment should review all reasonable investment proposals presented by New Jersey corporations and should report any consequent investment decision to the State Investment Council at one of its regularly scheduled publicly advertised meetings.

3. The Division of Investment should prefer a New Jersey broker, bank or securities dealer in instances where identical bids are received in purchase or sale transactions involving publicly traded homogeneous securities such as money market investments, certificates of deposit and eligible mortgage pools.

4. The Division of Investment should recognize in its evaluation of corporate securities that good corporate citizenship enhances the financial prospects for a corporation, and, conversely, that poor corporate citizenship detracts from such prospects.

5. The Division of Investment should consider the financial effects of citizenship issues in the determination of proxy votes at corporate shareholder meetings.

6. The Division of Investment should prefer investments in New Jersey mortgages in instances where such mortgages meet the fiduciary standards of the Council and provide fair market returns.

7. The Division of Investment should be prepared to identify New Jersey employers on any "approved lists" provided under regulations of the State Investment Council for the purchase of common stocks, commercial paper and certificates of deposit.

8. The Division of Investment should prefer investments in companies which advance the economic development of New Jersey, support alternative energy sources, provide for improvement of the environment, or are controlled by economically disadvantaged individuals, provided such investments meet the fiduciary standards of the Council and provide fair market returns.

In April 1994, Governor Whitman signed legislation which repealed the South Africa sanctions which had been enacted in 1985. The sanctions were repealed after an historic agreement had been reached in South Africa to provide for a transition towards majority rule. The effect of the repeal of the sanctions is to permit the pension and annuity funds of the State to diversify their investments into the securities of corporations and banks which are engaged in business in South Africa. Over the ten fiscal years from 1985 through 1994, the sanctions constrained the potential returns of the pension and annuity funds. In the case of stocks, the Division's unconstrained approved list of stocks provided a return of 14.1% a year for the period, which coincided with the annual return of the S&P's 500 over the same period. By comparison, the return of the constrained approved list of stocks was 13.1% a year for the period, which coincided with the annual return realized by the stock portfolio of the funds.

Voting of Proxy Statements

Each year the Division votes on issues raised in corporate proxy statements. Many of these issues deal not only with routine matters of corporate governance, but also reflect political and social issues. The Division reviews all such issues on a case-by-case basis from a financial point of view. In prior years the Division has supported shareholder resolutions which call for a report on employment practices in South Korea, require companies to leave South Africa, require compliance with World Health Organization standards for the sale of infant formula in underdeveloped countries and require compliance with the MacBride principles in Northern Ireland.

During fiscal 1994, the Division voted on 456 cor-

porate proxies. On 133 proxies the Division voted against the recommendations of corporate management on a total of 164 individual proposals. Of these proposals, 38 concerned changes in corporate governance procedures designed to reduce shareholder voting power, 113 related to executive compensation,

two related to compliance of the corporation with the MacBride principles in Northern Ireland, six related to confidential proxy voting, two related to the election of directors and one each related to non-discriminatory hiring practices, the elimination of preemptive rights and the selection of auditors.

**DIVISION OF INVESTMENT
DEPARTMENT OF THE TREASURY
STATE OF NEW JERSEY**

INDEX TO INVESTMENT SUMMARIES

Report of Independent Accountants	19
Summary of Amounts Invested by Fund as of June 30, 1994	20
Summary of Investment Income by Fund for the Year Ended June 30, 1994	23
Summary of Investments by Major Category as of June 30, 1994	26
Summary of Investment Activity for the Year Ended June 30, 1994	27
Notes to Investment Summaries—June 30, 1994	28

OTHER FINANCIAL INFORMATION

Appendix I: Unaudited Summary of Investments by Major Category of Individual Pension Funds	32
Appendix II: Unaudited Common Performance Disclosure Form for Public Funds	34

REPORT OF INDEPENDENT ACCOUNTANTS

To the Members of the
State Investment Council,
Division of Investment,
Department of the Treasury,
State of New Jersey

We have audited the accompanying summaries of amounts invested by fund and investments by major category of the Division of Investment, Department of the Treasury, State of New Jersey, as of June 30, 1994, and the related summaries of investment income by fund and investment activity for the year then ended. These summaries are the responsibility of the Division of Investment's management. Our responsibility is to express an opinion on these summaries based on our audit.

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

In our opinion, the summaries referred to above present fairly, in all material respects, the investments by fund and major category of the Division of Investment, Department of the Treasury, State of New Jersey, at June 30, 1994, and the related investment income and investment activity for the year then ended, in conformity with generally accepted accounting principles.

Princeton, New Jersey
August 18, 1994

Coopers + Lybrand LLP

SUMMARY OF AMOUNTS INVESTED BY FUND
as of June 30, 1994

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
PENSION AND ANNUITY GROUP				
Consolidated Police and Firemen's Pension Fund	\$ 42,823,653	\$ 42,649,372	\$ 42,936,829	\$ 287,457
Judicial Retirement System of New Jersey	105,383,997	105,302,601	131,801,064	26,498,463
Police and Firemen's Retirement System	5,608,037,142	5,602,058,576	7,119,870,446	1,517,811,870
Prison Officers Pension Fund	569,296	569,296	569,296	—
Public Employees' Retirement System	9,490,612,935	9,480,205,934	12,265,905,591	2,785,699,657
State Police Retirement System	602,782,396	602,721,150	777,422,597	174,701,447
Teachers' Pension and Annuity Fund	11,575,918,977	11,560,478,772	14,828,841,790	3,268,363,018
		27,393,985,701	35,167,347,613	7,773,361,912
STATIC GROUP				
Trustees for the Support of Public Schools	80,761,224	80,514,302	89,395,959	8,881,657
Waste Water Treatment Fund (Act of 1985)	99,657,461	99,657,461	99,657,461	—
Waste Water Treatment Trust Fund (Act of 1985)	1,487,678	1,487,678	1,487,678	—
		181,659,441	190,541,098	8,881,657
DEMAND GROUP				
Atlantic City Casino Parking Fund	6,210,032	6,210,032	6,210,032	—
Atlantic City Tourism Promotion Fund	652,328	652,328	652,328	—
Boarding House Rental Assistance Fund	21,164,494	21,164,494	21,164,494	—
Casino Simulcasting Special Fund	1,013,446	1,013,446	1,013,446	—
Casino Simulcasting Fund	101,468	101,468	101,468	—
Catastrophic Illness in Children Relief Fund (Act of 1987)	23,424,047	23,424,047	23,424,047	—
Clean Communities Account Fund (Act of 1985)	12,486,076	12,486,076	12,486,076	—
Development Fund—Luxury Tax	1,593,729	1,593,729	1,593,729	—
Emergency Services Fund	4,577,068	4,577,068	4,577,068	—
Enterprise Zone Assistance Fund	45,583,211	45,583,211	45,583,211	—
Hazardous Discharge Fund (Act of 1986)	5,034,304	5,034,304	5,034,304	—
Health Care Subsidy Fund	101,775,622	101,775,622	101,775,622	—
Higher Education Assistance Fund	28,981,881	28,981,881	28,981,881	—
Luxury Tax Fund	1,244,368	1,244,368	1,244,368	—
Motor Vehicle Security Responsibility Fund	139,347	139,347	139,347	—
New Jersey Automobile Insurance Guaranty Fund	89,184,054	89,184,054	89,184,054	—
New Jersey Insurance Development Fund	49,704,362	49,704,362	49,704,362	—
New Jersey Spill Compensation Fund	73,514,374	73,514,374	73,514,374	—
Outstanding Checks Account	24,217,970	24,217,970	24,217,970	—
Petroleum Overcharge Reimbursement Fund	57,183,854	57,183,854	57,183,854	—
Real Estate Guaranty Fund	1,337,039	1,337,039	1,337,039	—
Resource Recovery Investment Tax Fund (Act of 1985)	46,987,964	46,987,964	46,987,964	—
Safe Neighborhoods' Services Fund	14,728,398	14,728,398	14,728,398	—
Sanitary Landfill Facility Contingency Fund	46,338,890	47,236,880	45,915,490	(1,321,390)
Solid Waste Services Tax Fund (Act of 1985)	12,648,215	12,648,215	12,648,215	—
State Disability Benefits Fund	155,348,316	155,160,994	153,743,416	(1,417,578)
State Recycling Fund	26,811,522	26,811,522	26,811,522	—
Tourism Improvement Development District Act Fund	7,233	7,233	7,233	—
Unclaimed County Deposits Trust Fund	1,699,059	1,699,059	1,699,059	—
Unclaimed Personal Property Trust Fund	67,314,427	67,311,138	67,217,027	(94,111)
Unemployed Compensation Auxiliary Fund	14,848,641	14,848,641	14,848,641	—
Unsatisfied Claim and Judgment Fund	370,308,240	370,308,240	370,308,240	—
Volunteer Emergency Service Organizations Loan Fund	338,496	338,496	338,496	—
Worker and Community Right to Know Fund	5,949,293	5,949,293	5,949,293	—
Worker's Compensation Security Fund—Mutual	4,145,820	4,148,337	4,127,670	(20,667)
Worker's Compensation Security Fund—Stock	66,218,189	66,224,258	65,762,189	(462,069)
Workforce Development Partnership Fund	53,181,106	53,181,106	53,181,106	—
		1,436,712,848	1,433,397,033	(3,315,815)
TEMPORARY RESERVE GROUP				
Alcohol Education Rehabilitation and Enforcement Fund	13,424,234	13,549,102	13,536,734	(12,368)
Beaches and Harbors Fund (Act of 1977)	1,406,648	1,406,648	1,406,648	—
Capital City Redevelopment Loan and Grant Fund	3,419,884	3,419,884	3,419,884	—
Clean Waters Fund (Act of 1976)	5,054,783	5,054,783	5,054,783	—
Community Development Bond Fund (Act of 1981)	2,020,794	2,020,794	2,020,794	—
Correctional Facilities Construction Fund (Act of 1982)	5,030,238	5,030,238	5,030,238	—
Correctional Facilities Construction Fund (Act of 1987)	44,635,692	44,635,692	44,635,692	—
Emergency Flood Control Fund (Act of 1978)	2,940,634	2,940,634	2,940,634	—
Emergency Medical Technician Training Fund	1,319,455	1,319,455	1,319,455	—
Energy Conservation Fund (Act of 1980)	12,413,876	12,413,876	12,413,876	—

SUMMARY OF AMOUNTS INVESTED BY FUND—(CONTINUED)
as of June 30, 1994

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
TEMPORARY RESERVE GROUP—(continued)				
Farmland Preservation Fund (Act of 1981)	\$ 1,419,374	\$ 1,419,374	\$ 1,419,374	—
Farmland Preservation Fund (Act of 1989)	1,107,108	1,107,108	1,107,108	—
General Investment Fund	1,757,661,171	1,757,658,432	1,757,646,046	\$ (12,386)
General Trust Fund	15,222	15,222	15,222	—
Green Acres Cultural Centers and Historic Preservation Bond Fund (Act of 1987)	49,548,836	49,548,836	49,548,836	—
Green Trust Fund (Act of 1983)	9,529,429	9,529,429	9,529,429	—
Hazardous Discharge Fund (Act of 1981)	14,775,002	14,775,002	14,775,002	—
Hazardous Discharge Site Cleanup Fund (Act of 1985)	28,479,167	28,479,167	28,479,167	—
Higher Education Buildings Construction Fund (Act of 1971)	58,136	58,136	58,136	—
Higher Education Facility Renovation and Rehabilitation Fund	2,369,178	2,369,178	2,369,178	—
Housing Assistance Fund (Act of 1968)	557,822	557,822	557,822	—
Human Services Facilities Construction Fund (Act of 1984)	1,119,036	1,119,036	1,119,036	—
Institutional Construction Fund (Act of 1978)	105,074	105,074	105,074	—
Institutions Construction Fund (Act of 1976)	27,833	27,833	27,833	—
Jobs, Education and Competitiveness Fund (Act of 1988)	19,762,456	19,762,456	19,762,456	—
Jobs, Science and Technology Fund (Act of 1984)	5,007,167	5,007,167	5,007,167	—
Medical Education Facilities Fund (Act of 1977)	530,796	530,796	530,796	—
Mortgage Assistance Fund (Act of 1976)	3,226,590	3,226,590	3,226,590	—
Natural Resources Fund (Act of 1980)	10,257,160	10,257,160	10,257,160	—
New Home Warranty Security Fund	67,456,836	67,322,757	67,360,116	37,359
New Jersey Bridge Rehabilitation and Improvement and Railroad Right-of-Way Preservation Fund	23,183,516	23,183,516	23,183,516	—
New Jersey Bridge Rehabilitation Fund (Act of 1983)	18,200,544	18,200,544	18,200,544	—
New Jersey Green Acres Fund (Act of 1983)	19,648,775	19,648,775	19,648,775	—
New Jersey Green Acres Fund (Act of 1989)	6,933,318	6,933,318	6,933,318	—
New Jersey Green Acres Fund (Act of 1992)	4,593,474	4,593,474	4,593,474	—
New Jersey Green Trust Fund (Act of 1989)	10,987,462	10,987,462	10,987,462	—
New Jersey Local Development Financing Fund	2,280,621	2,280,621	2,280,621	—
New Jersey Medical Malpractice Reinsurance Recovery Fund	14,251,186	14,251,186	14,251,186	—
New Jersey State Dental Program	15,398,736	15,398,736	15,398,736	—
Pension Adjustment Fund	975,532	975,532	975,532	—
Pension Payroll Investment Fund	5,209,438	5,209,438	5,209,438	—
Pinelands Infrastructure Trust Fund (Act of 1985)	6,791,225	6,791,225	6,791,225	—
Pollution Prevention Fund	3,693,346	3,693,346	3,693,346	—
Prescription Drug Program Fund	22,203,317	22,203,317	22,203,317	—
Public Buildings Construction Fund (Act of 1968)	255,378	255,378	255,378	—
Public Purpose Buildings and Community-Based Facilities Construction Fund	53,041,798	53,041,798	53,041,798	—
Public Purpose Buildings Construction Fund (Act of 1980)	11,895,155	11,895,155	11,895,155	—
Resource Recovery and Solid Waste Disposal Facilities Fund (Act of 1985)	24,349,478	24,349,478	24,349,478	—
Safe Drinking Water Fund	10,929,305	10,929,305	10,929,305	—
Shore Protection Fund (Act of 1983)	8,367,122	8,367,122	8,367,122	—
State Facilities for Handicapped Fund (Act of 1973)	1,789,138	1,789,138	1,789,138	—
State Health Benefits Fund	473,494,052	473,949,287	473,052,202	(897,085)
State Land Acquisition and Development Fund (Act of 1978)	926,961	926,961	926,961	—
State Lottery Fund—Investment	77,786,839	77,786,839	77,786,839	—
State of New Jersey—Alternate Benefit Program	20,418,917	20,418,917	20,418,917	—
State of New Jersey Cash Management Fund— Administrative Expense Fund	2,039,316	2,039,316	2,039,316	—
State of New Jersey Cash Management Fund— Other than State Funds	3,487,717,948	3,487,717,948	3,487,717,948	—
State of New Jersey Cash Management Fund— Reserve Fund	32,256,158	32,256,158	32,256,158	—
State Recreation and Conservation Land Acquisition and Development Fund (Act of 1974)	1,363,069	1,363,069	1,363,069	—
State Recreation and Conservation Land Acquisition Fund (Act of 1971)	2,138,060	2,138,060	2,138,060	—
State Transportation Fund (Act of 1968)	119,664	119,664	119,664	—
Stormwater Management and Combined Sewer Overflow Abatement Fund	15,522,653	15,522,653	15,522,653	—
Transportation Rehabilitation and Improvement Fund (Act of 1979)	5,706,761	5,706,761	5,706,761	—

SUMMARY OF AMOUNTS INVESTED BY FUND—(CONCLUDED)
as of June 30, 1994

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
TEMPORARY RESERVE GROUP—(continued)				
University of Medicine and Dentistry of New Jersey—Self-Insurance Reserve Fund	\$ 60,323,401	\$ 59,723,754	\$ 57,876,409	\$ (1,847,345)
Veterans' Guaranteed Loan Fund	17,303	17,303	17,303	—
Water Conservation Fund (Act of 1969)	1,387	1,387	1,387	—
Water Supply Fund (Act of 1981)	95,664,437	95,664,437	95,664,437	—
Water Supply Replacement Trust Fund	9,194,845	9,194,845	9,194,845	—
		<u>6,614,192,904</u>	<u>6,611,461,079</u>	<u>(2,731,825)</u>
TRUST GROUP				
New Jersey State Employees' Deferred Compensation Administrative Charges	319,333	319,333	319,333	—
New Jersey State Employees' Deferred Compensation Cash Management Fund	76,733,412	76,733,412	76,733,412	—
New Jersey State Employees' Deferred Compensation Equity Fund	100,304,263	100,304,263	108,865,470	8,561,207
New Jersey State Employees' Deferred Compensation Fixed Income Fund	82,439,741	82,522,463	81,535,677	(986,786)
New Jersey State Employees' Deferred Compensation Holding Account	3,602,997	3,602,997	3,602,997	—
Supplemental Annuity Collective Trust Fund	99,863,072	99,863,072	112,479,848	12,616,776
Tischler Memorial Fund	597,678	596,334	585,873	(10,461)
		<u>363,941,874</u>	<u>384,122,610</u>	<u>20,180,736</u>
TOTAL AMOUNTS INVESTED BY FUND		<u>\$35,990,492,768</u>	<u>\$43,786,869,433</u>	<u>\$7,796,376,665</u>

See notes to investment summaries.

SUMMARY OF INVESTMENT INCOME BY FUND
for the Year Ended June 30, 1994

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
PENSION AND ANNUITY GROUP			
Consolidated Police and Firemen's Pension Fund	\$ 2,266,285	\$ 33,209	\$ 2,299,494
Judicial Retirement System of New Jersey	6,077,726	7,507	6,085,233
Police and Firemen's Retirement System	306,257,601	4,575,754	310,833,356
Prison Officers Pension Fund	44,750	—	44,750
Public Employees' Retirement System	524,990,235	13,181,632	538,171,867
State Police Retirement System	33,773,007	514,404	34,287,411
Teachers' Pension and Annuity Fund	620,169,346	9,938,555	630,107,900
	<u>1,493,578,950</u>	<u>28,251,061</u>	<u>1,521,830,011</u>
STATIC GROUP			
Trustees for the Support of Public Schools	5,109,613	223,821	5,333,434
Waste Water Treatment Fund (Act of 1985)	3,033,303	—	3,033,303
Waste Water Treatment Trust Fund (Act of 1985)	50,511	—	50,511
	<u>8,193,427</u>	<u>223,821</u>	<u>8,417,248</u>
DEMAND GROUP			
Atlantic City Casino Parking Fund	120,032	—	120,032
Atlantic City Tourism Promotion Fund	18,011	—	18,011
Boarding House Rental Assistance Fund	675,208	—	675,208
Casino Simulcasting Special Fund	13,446	—	13,446
Casino Simulcasting Fund	1,468	—	1,468
Catastrophic Illness in Children Relief Fund (Act of 1987)	785,780	—	785,780
Clean Communities Account Fund (Act of 1985)	473,916	—	473,916
Development Fund—Luxury Tax	54,864	—	54,864
Emergency Services Fund	155,407	—	155,407
Enterprise Zone Assistance Fund (Act of 1983)	1,247,744	—	1,247,744
Hazardous Discharge Fund (Act of 1986)	39,304	—	39,304
Health Care Cost Reduction Fund	880,464	—	880,464
Health Care Subsidy Fund	1,885,346	—	1,885,346
Higher Education Assistance Fund	1,102,662	—	1,102,662
Luxury Tax Fund	32,530	—	32,530
Motor Vehicle Security Responsibility Fund	4,791	—	4,791
New Jersey Automobile Insurance Guaranty Fund	3,764,761	—	3,764,761
New Jersey Health Care Trust	91,260	—	91,260
New Jersey Insurance Development Fund	2,194,591	—	2,194,591
New Jersey Spill Compensation Fund	2,610,303	—	2,610,303
Outstanding Checks Account	567,671	—	567,671
Petroleum Overcharge Reimbursement Fund	1,638,854	—	1,638,854
Real Estate Guaranty Fund	28,193	—	28,193
Resource Recovery Investment Tax Fund (Act of 1985)	1,826,079	—	1,826,079
Safe Neighborhoods' Services Fund	401,398	—	401,398
Sanitary Landfill Facility Contingency Fund	2,204,860	—	2,204,860
Solid Waste Services Tax Fund (Act of 1985)	457,314	—	457,314
State Disability Benefits Fund	6,107,012	—	6,107,012
State Recycling Fund	925,700	—	925,700
Tourism Improvement Development District Act Fund	4,233	—	4,233
Unclaimed County Deposits Trust Fund	64,025	—	64,025
Unclaimed Personal Property Trust Fund	2,330,165	—	2,330,165
Unemployment Compensation Auxiliary Fund	390,795	—	390,795
Unsatisfied Claim and Judgment Fund	9,174,860	—	9,174,860
Volunteer Emergency Service Organizations Loan Fund	14,299	—	14,299
Worker and Community Right to Know Fund	169,785	—	169,785
Worker's Compensation Security Fund—Mutual	153,463	—	153,463
Worker's Compensation Security Fund—Stock	2,436,263	—	2,436,263
Workforce Development Partnership Fund	1,627,595	—	1,627,595
	<u>46,674,452</u>	<u>—</u>	<u>46,674,452</u>
TEMPORARY RESERVE GROUP			
Alcohol Education Rehabilitation and Enforcement Fund	654,390	—	654,390
Beaches and Harbors Fund (Act of 1977)	49,208	—	49,208
Capital City Redevelopment Loan and Grant Fund	137,223	—	137,223
Clean Waters Fund (Act of 1976)	140,843	—	140,843
Community Development Bond Fund (Act of 1981)	151,718	—	151,718
Correctional Facilities Construction Fund (Act of 1982)	173,782	—	173,782
Correctional Facilities Construction Fund (Act of 1987)	1,708,813	—	1,708,813
Emergency Flood Control Fund (Act of 1978)	110,962	—	110,962

SUMMARY OF INVESTMENT INCOME BY FUND—(CONTINUED)
for the Year Ended June 30, 1994

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
TEMPORARY RESERVE GROUP—(continued)			
Emergency Medical Technician Training Fund	\$ 19,455	—	\$ 19,455
Energy Conservation Fund (Act of 1980)	514,935	—	514,935
Farmland Preservation Fund (Act of 1981)	76,124	—	76,124
Farmland Preservation Fund (Act of 1989)	228,877	—	228,877
General Investment Fund	41,005,734	—	41,005,734
General Trust Fund	522	—	522
Green Acres Cultural Centers and Historic Preservation Bond Fund (Act of 1987)	1,766,507	—	1,766,507
Green Trust Fund (Act of 1983)	470,316	—	470,316
Hazardous Discharge Fund (Act of 1981)	648,116	—	648,116
Hazardous Discharge Site Cleanup Fund (Act of 1985)	560,336	—	560,336
Higher Education Buildings Construction Fund (Act of 1971)	5,522	—	5,522
Higher Education Facility Renovation and Rehabilitation Fund	58,069	—	58,069
Housing Assistance Fund (Act of 1968)	17,445	—	17,445
Human Services Facilities Construction Fund (Act of 1984)	86,634	—	86,634
Institutional Construction Fund (Act of 1978)	3,939	—	3,939
Institutions Construction Fund (Act of 1976)	1,030	—	1,030
Jobs, Education and Competitiveness Fund (Act of 1988)	2,581,317	—	2,581,317
Jobs, Science and Technology Fund (Act of 1984)	207,426	—	207,426
Medical Education Facilities Fund (Act of 1977)	18,253	—	18,253
Mortgage Assistance Fund (Act of 1976)	111,458	—	111,458
Natural Resources Fund (Act of 1980)	345,014	—	345,014
New Home Warranty Security Fund	3,088,000	—	3,088,000
New Jersey Bridge Rehabilitation Fund (Act of 1983)	670,641	—	670,641
New Jersey Bridge Rehabilitation Fund and Improvement and Railroad Right-of-Way Preservation Fund	975,818	—	975,818
New Jersey Green Acres Fund (Act of 1983)	710,530	—	710,530
New Jersey Green Acres Fund (Act of 1989)	367,416	—	367,416
New Jersey Green Acres Fund (Act of 1992)	38,474	—	38,474
New Jersey Green Trust Fund (Act of 1989)	615,229	—	615,229
New Jersey Local Development Financing Fund	98,066	—	98,066
New Jersey Medical Malpractice Reinsurance—Recovery Fund	446,014	—	446,014
New Jersey State Dental Program	477,423	—	477,423
Pension Adjustment Fund	336,406	—	336,406
Pension Payroll Investment Fund	196,264	—	196,264
Pinelands Infrastructure Trust Fund (Act of 1985)	251,843	—	251,843
Pollution Prevention Fund	82,997	—	82,997
Prescription Drug Program Fund	666,867	—	666,867
Public Buildings Construction Fund (Act of 1968)	12,065	—	12,065
Public Purpose Buildings and Community-Based Facilities Construction Fund	1,979,465	—	1,979,465
Public Purpose Buildings and Construction Fund (Act of 1980)	448,405	—	448,405
Resource Recovery and Solid Waste Disposal Facilities Fund (Act of 1985)	660,097	—	660,097
Safe Drinking Water Fund	355,412	—	355,412
Shore Protection Fund (Act of 1983)	293,322	—	293,322
State Facilities for Handicapped Fund (Act of 1973)	64,068	—	64,068
State Health Benefits Fund	15,524,931	—	15,524,931
State Land Acquisition and Development Fund (Act of 1978)	20,648	—	20,648
State Lottery Fund—Investment	1,695,392	—	1,695,392
State of New Jersey—Alternate Benefits Program	566,499	—	566,499
State of New Jersey Cash Management Fund— Administrative Expense Fund	61,822	—	61,822
State of New Jersey Cash Management Fund— Other than State Funds	128,673,996	—	128,673,996
State of New Jersey Cash Management Fund— Reserve Fund	1,038,204	—	1,038,204
State Recreation and Conservation Land Acquisition and Development Fund (Act of 1974)	56,938	—	56,938
State Recreation and Conservation Land Acquisition Fund (Act of 1971)	103,982	—	103,982
State Transportation Fund (Act of 1968)	4,198	—	4,198
State Water Development Fund (Act of 1958)	3	—	3
Stormwater Management and Combined Sewer Overflow Abatement Fund	533,790	—	533,790
Transportation Rehabilitation and Improvement Fund (Act of 1979)	479,894	—	479,894

SUMMARY OF INVESTMENT INCOME BY FUND—(CONCLUDED)
for the Year Ended June 30, 1994

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
TEMPORARY RESERVE GROUP—(continued)			
University of Medicine and Dentistry of New Jersey—Self-Insurance Reserves Fund	\$ 2,835,368	—	\$ 2,835,368
Veterans' Guaranteed Loan Fund	586	—	586
Water Conservation Fund (Act of 1969)	9,617	—	9,617
Water Supply Fund (Act of 1981)	3,354,842	—	3,354,842
Water Supply Replacement Trust Fund	<u>301,943</u>	<u>—</u>	<u>301,943</u>
	219,951,443	—	219,951,443
TRUST GROUP			
New Jersey State Employees' Deferred Compensation Administrative Charges	16,724	—	16,724
New Jersey State Employees' Deferred Compensation Cash Management Fund	2,451,989	—	2,451,989
New Jersey State Employees' Deferred Compensation Equity Fund	2,544,614	2,461,891	5,006,505
New Jersey State Employees' Deferred Compensation Fixed Income Fund	4,917,759	—	4,917,759
New Jersey State Employees' Deferred Compensation Holding Account	152,332	—	152,332
Supplemental Annuity Collective Trust Fund	3,019,073	10,470,092	13,489,165
Tischler Memorial Fund	<u>33,137</u>	<u>—</u>	<u>33,137</u>
	13,135,628	12,931,983	26,067,611
TOTALS	<u>\$1,781,533,900</u>	<u>\$41,406,865</u>	<u>\$1,822,940,765</u>

See notes to investment summaries.

SUMMARY OF INVESTMENTS BY MAJOR CATEGORY
as of June 30, 1994

	Par, Cost or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over (Under) Amortized Cost
U.S. Government and other government bonds and obligations	\$ 430,822,000	\$ 431,378,550	\$ 424,522,259	(\$6,856,291)
Industrial bonds and commercial paper	4,500,000	4,499,041	4,527,115	28,074
Telephone bonds	10,100,000	10,089,260	9,907,310	(181,950)
Gas, electric and water bonds	13,312,500	13,341,741	13,241,581	(100,160)
Common stocks	204,742,500	204,742,500	233,733,738	28,991,238
Time certificates of deposit	100,000,000	100,000,000	100,000,000	—
Mortgage-backed certificates	2,184,013,892	2,151,693,902	2,103,916,843	(47,777,059)
Units—Common Pension Fund A	11,250,480,862	11,250,480,862	18,325,253,817	7,074,772,955
Units—Common Pension Fund B	10,379,344,032	10,379,344,032	10,746,644,420	367,300,388
Units—Common Pension Fund D	2,980,160,359	2,980,160,359	3,360,372,215	380,211,856
Units—Cash Management Fund	8,464,715,260	8,464,715,260	8,464,715,260	—
Other investments	50,000	47,261	34,875	(12,386)
TOTAL INVESTMENTS BY MAJOR CATEGORY		<u>\$35,990,492,768</u>	<u>\$43,786,869,433</u>	<u>\$7,796,376,665</u>

See notes to investment summaries.

SUMMARY OF INVESTMENT ACTIVITY
for the Year Ended June 30, 1994

Purchases at cost, excluding common funds:		
Bonds	\$ 266,261,739	
Mortgages	902,649,868	
Stocks	<u>74,437,543</u>	\$ 1,243,349,150
Purchases of units of common funds, at cost		31,832,508,265
Unrealized depreciation		(1,728,796,656)
Discount accretion		9,045,849
Sales, at market		(1,228,800,818)
Mortgage principal payments, at amortized cost		(314,648,102)
Redemptions, at market		(40,363,134)
Maturities, at par amount		(121,497,000)
Redemptions of units at common funds		(30,737,807,753)
Premium amortization		<u>(1,609,475)</u>
NET DECREASE IN INVESTMENTS		(1,088,619,674)
Total amounts invested by funds—Note 2		
Beginning of year		<u>44,875,489,107</u>
Total amounts invested by funds—		<u>\$43,786,869,433</u>
END OF YEAR		

See notes to investment summaries.

NOTES TO INVESTMENT SUMMARIES

NOTE 1—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Administration

The operations of the Division of Investment are governed by Chapter 270, Public Law of 1950, as amended, for the purpose of investing in securities for various funds under the jurisdiction of the Department of the Treasury, State of New Jersey. The Division acts in an investment capacity only and receipt and disbursement of cash is a direct function of the respective funds. These financial summaries present the amounts invested by the various pension and other State funds maintained by the Division and are not intended to be a complete presentation of the various funds nor the Division's financial position or results of operations.

Investment Valuation

Investments are stated at market value. State of New Jersey Cash Management Fund units are stated at a cost of a \$1.00 per unit, which approximates market value.

Market values of securities traded on a national securities exchange or reported on the NASDAQ national market are presented at the last reported sales price on the day of valuation. Other securities traded in the over-the-counter market and listed securities for which no sale was reported on that date are presented at the last quoted bid price. Other non-traded securities are valued by a commercial pricing service. Market values of Common Pension Fund A, Common Pension Fund B, and Common Pension Fund D are based on the net asset values of the respective fund in which the underlying investment securities are valued via the previously prescribed methods. Par, cost or principal amount, and amortized cost are presented in the summaries for informational purposes.

Investment Transactions

Investment transactions are accounted for on their trade date. Gains or losses from investment transactions are calculated on the average cost basis and recognized as investment income when they occur.

Discount and Premium

Accretion of discount and amortization of premium are recorded on the straight-line basis for investments which mature within one year. For other investments, the effective interest rate method is utilized.

Investment Income

Investment income includes interest earned, dividends, and discount accretion, reduced for premium amortization. Interest and dividend income is accounted for on the accrual basis.

Net Investment Gain

Net investment gain includes realized gains and losses on security transactions and distributed gains from the State of New Jersey Cash Management Fund. No gains were distributed from Common Pension Fund A, Common Pension Fund B or Common Pension Fund D in fiscal year 1994.

Administrative Expenses

Administrative expenses allocable to the Division are paid by the Department of the Treasury, State of New Jersey and, therefore, are not included in the accompanying Summary of Investment Income by Fund.

NOTE 2—INVESTMENT ACTIVITY

Statutes of the State of New Jersey and regulations of the State Investment Council authorize the Division of Investment to invest in obligations of the U.S. Treasury, U.S. Government agencies, and their instrumentalities; obligations of the State of New Jersey or municipal or political subdivisions of the State; commercial paper; bankers acceptances; revenue obligations of public authorities; debt instruments of banks; collateralized notes and mortgages; certificates of deposit; repurchase agreements; equity and convertible equity securities, international debt and equity securities, currencies, and currency futures, options and other common types of investment securities. Investee institutions and organizations are prescribed by the statutes and regulations based on minimum capital, credit history, and other evaluation factors.

The purchase, sale, receipt of income, and other transactions affecting investments are governed by custodial agreements between the investing funds through the State Treasurer and custodian banks as agents for the funds. State laws and policies set forth the requirements of such agreements and other particulars as to the size of the custodial institution, amount of the portfolio to be covered by the agreements, and other pertinent matters.

GASB Statement No. 3 requires disclosure of the level of investment risk assumed by the Division at June 30, 1994. Category 1 includes investments that are insured or registered, or securities held by the Division or its agent in the Funds' name. Category 2 includes uninsured and unregistered investments held by the Fund's trust department or agent in the Funds' name. Category 3 includes uninsured and unregistered investments held by a broker or dealer, or held by the Fund's trust department or agent but not in the Funds' name. As of June 30, 1994, all investments held by the Division are classified as Category 1.

Federal securities, including federal securities held as collateral on repurchase agreements (\$30,000,000 at June 30, 1994 secured by federal securities), are maintained at Federal Reserve Banks in Philadelphia and New York through the custodian banks in trust for the State of New Jersey. A significant portion of corporate equity and debt securities are maintained by the Depository Trust Company (DTC) or Participants Trust Company (PTC) through the custodian banks in trust for the State of New Jersey.

Investment securities denominated in a foreign currency are maintained by the various established book entry systems, in the countries where available, through the custodian bank in trust for the State of New Jersey. In addition, certain investment securities denominated in a foreign currency are physically maintained by sub-custodian banks within the foreign country. The custodian banks, as agents for the State funds, maintain internal accounting records identifying the securities as securities owned by or pledged to the State funds.

Domestic securities not maintained by the Federal Reserve Banks, DTC or PTC are in the name of a designated nominee representing the securities of a particular State fund which establishes the State fund's unconditional right to the securities.

The investments of the various State of New Jersey counties, municipalities and school districts and the agencies or authorities created by any of these entities, other than their investments in the Cash Management Fund, are not a direct responsibility of the State Investment Council. That investment function is being performed by the Division of Investment as a service under a provision in the law providing that each county, municipality and school district and the agencies or authorities created by any one of these entities may avail itself of the services of any State department or agency as it may require. Accordingly, the accompanying summaries do not include the investments or results of non-cash management fund investment transactions made on behalf of the authorities and agencies.

Realized gains and losses arising from investment activity by Common Pension Fund A, Common Pension Fund B, and Common Pension Fund D consisting of net gains of \$1,129,042,236 in fiscal year 1994, are not reflected in the Summary of Investment Income by Fund. Realized losses arising from foreign currency related transactions by Common Pension Fund D of \$15,005,575 in fiscal year 1994 are not reflected in the Summary of Investment Income by Fund. Undistributed investment income of \$191,250,901 as of June 30, 1994, arising from investment activity by Common Pension Fund D is not reflected in the Summary of Investment Income by Fund. These amounts are not reflected as they were not distributed to the holders of the Funds.

NOTES TO INVESTMENT SUMMARIES

NOTE 3—SUMMARY OF INVESTMENTS BY MAJOR CATEGORY INCLUDING INVESTMENTS OWNED BY THE COMMON PENSION FUNDS AND THE STATE OF NEW JERSEY CASH MANAGEMENT FUND (THE "UNIT FUNDS")

The following is a summary of investments by major category at June 30, 1994, including investments owned by the Common Pension Funds and the State of New Jersey Cash Management Fund, the "Unit Funds." In the Total Amounts Invested by Funds shown in the investment summaries, the Common Pension Funds and the State of New Jersey Cash Management Fund are shown at their unit value.

	Par, Cost Or Principal Amount	Amortized Cost	Market	Market Over (Under) Amortized Cost
U.S. Government and other government bonds and obligations	\$13,612,449,000	\$13,747,203,189	\$13,762,520,348	\$ 15,317,159
Industrial bonds and commercial paper	4,358,802,831	4,350,378,902	4,364,516,133	14,137,231
Foreign government bonds and notes	2,065,073,348	2,065,073,348	2,062,351,970	(2,721,378)
Foreign stock	1,099,648,954	1,099,648,954	1,154,371,783	54,722,829
Telephone bonds	139,400,000	137,307,524	131,713,833	(5,593,691)
Gas, electric and water bonds	394,135,500	385,374,945	373,566,246	(11,808,699)
Common stocks	12,506,155,024	12,506,155,024	18,430,384,875	5,924,229,851
Mortgage-backed certificates	2,184,013,892	2,151,693,902	2,103,916,843	(47,777,059)
Time certificates of deposit	1,255,000,000	1,255,000,000	1,255,000,000	—
Repurchase agreements	30,000,000	30,000,000	30,000,000	—
Other investments	156,324,000	157,993,399	162,430,432	4,437,033
Total investments		37,885,829,187	43,830,772,463	5,944,943,276
Differences in accounting by unit funds:				
Other assets		3,146,053,087	3,146,053,087	—
Other liabilities		(3,517,991,584)	(3,209,724,188)	308,267,396
Undistributed realized gains and other income		(1,523,267,805)	—	1,523,267,805
Other accounting practices		(130,117)	19,768,071	19,898,188
Total amounts invested by funds		<u>\$35,990,492,768</u>	<u>\$43,786,869,433</u>	<u>\$7,796,376,665</u>

The following describes the accounting differences between the total amounts invested by Fund and total investments, primarily relating to unit funds:

- I. The summary of investments by major category (page 26) includes the "Par, Cost, or Principal Amount" and "Amortized Cost" of the units of participation at the total purchase price of the units by the participating funds. The total investments shown above reflects the "Par, Cost, or Principal Amount" and "Amortized Cost" of the investments held by the Unit Funds.
- II. Market value as shown for total amounts invested by fund represents the net asset value of the Common Pension Funds and the State of New Jersey Cash Management Fund as of June 30, 1994. The market value included in the total investments shown above reflects the market value of the investments held by the Unit Funds.
- III. Total investments shown above does not reflect the other assets and liabilities of the Unit Funds, e.g., cash, accrued interest receivable, amounts due for investments sold or owed for investments purchased, and undistributed income due to participants. These items are included in calculating the net asset value of the Unit Funds.
- IV. Total amounts invested by funds do not reflect cumulative net realized gains from Unit Funds' investment transactions which have not been distributed to the participating funds. Common Pension Funds A, B and D cumulative net realized gains are distributed at the discretion of the State Investment Council.

NOTES TO INVESTMENT SUMMARIES

NOTE 4—COMMITMENTS

As of June 30, 1994, Common Pension Fund D had entered into the following forward currency exchange contracts as hedges of its investments:

Contract To Deliver	In Exchange For	Settlement Date	Net Unrealized Appreciation (Depreciation)
US\$ 47,778,309	YEN 5,000,000,000	7/1/94	2,976,053
YEN 5,000,000,000	US\$ 48,668,432	7/1/94	(2,085,930)
US\$ 47,738,166	YEN 5,000,000,000	7/6/94	3,032,533
US\$ 63,379,389	DM 100,000,000	7/6/94	(351,531)
DM 100,000,000	US\$ 56,957,339	7/6/94	(6,070,519)
YEN 5,000,000,000	US\$ 47,619,048	7/6/94	(3,151,651)
US\$ 39,349,423	SKR 300,000,000	7/7/94	(228,343)
SKR 300,000,000	US\$ 36,057,692	7/7/94	(3,063,388)
C\$ 65,000,000	US\$ 49,023,305	7/14/94	2,071,557
YEN 2,500,000,000	US\$ 24,435,539	7/29/94	(987,423)
US\$ 78,364,148	YEN 8,000,000,000	8/1/94	3,000,996
YEN 8,000,000,000	US\$ 74,717,475	8/1/94	(6,647,669)
US\$ 24,254,890	YEN 2,500,000,000	8/2/94	1,173,761
US\$ 26,604,707	FFR 150,000,000	8/2/94	939,961
FFR 150,000,000	US\$ 25,093,263	8/2/94	(2,451,405)
PTA 3,000,000,000	US\$ 20,818,876	8/2/94	(1,909,774)
YEN 2,500,000,000	US\$ 24,532,894	8/2/94	(895,757)
US\$ 38,275,681	YEN 4,000,000,000	8/16/94	2,455,567
YEN 4,000,000,000	US\$ 39,385,585	8/16/94	(1,345,663)
US\$ 34,650,035	FFR 200,000,000	8/26/94	2,056,642
DM 75,000,000	US\$ 43,352,601	8/26/94	(3,897,446)
FFR 200,000,000	US\$ 33,115,872	8/26/94	(3,590,805)
YEN 5,000,000,000	US\$ 47,991,553	8/26/94	(2,963,186)
US\$ 56,327,450	SKR 450,000,000	9/8/94	1,975,544
SKR 450,000,000	US\$ 55,245,227	9/8/94	(3,057,767)
SKR 300,000,000	US\$ 39,133,838	9/30/94	317,980
US\$ 49,621,881	YEN 5,000,000,000	10/3/94	1,484,574
YEN 5,000,000,000	US\$ 49,005,195	10/3/94	(2,101,260)
PND 30,000,000	US\$ 44,196,000	10/5/94	(2,058,000)
BFR 500,000,000	US\$ 13,638,843	10/11/94	(1,604,223)
FFR 150,000,000	US\$ 25,040,482	10/11/94	(2,466,303)
SKR 100,000,000	US\$ 11,973,180	10/11/94	(956,907)
LIT 23,000,000,000	US\$ 13,982,188	10/25/94	(377,530)
FFR 300,000,000	US\$ 49,920,958	11/3/94	(5,079,500)
PTA 6,000,000,000	US\$ 42,501,948	11/3/94	(2,636,356)
YEN 8,500,000,000	US\$ 82,604,470	11/28/94	(4,685,405)
SFR 50,000,000	US\$ 33,451,529	12/2/94	(4,148,110)
YEN 5,500,000,000	US\$ 53,517,563	12/13/94	(3,036,718)
A\$ 50,000,000	US\$ 36,435,000	12/16/94	63,428
DM 85,000,000	US\$ 48,744,122	12/19/94	(4,843,068)
YEN 5,000,000,000	US\$ 49,301,885	12/19/94	(2,137,545)
C\$ 90,000,000	US\$ 66,725,979	12/23/94	2,394,314
DKR 325,000,000	US\$ 46,824,574	1/5/95	(4,867,753)
FFR 400,000,000	US\$ 66,522,535	1/5/95	(6,761,698)
C\$ 65,000,000	US\$ 49,038,099	1/6/95	2,609,528
SKR 450,000,000	US\$ 53,580,997	1/10/95	(4,293,095)
PND 50,000,000	US\$ 74,005,000	2/2/95	(3,015,000)
LIT 32,000,000,000	US\$ 18,131,853	2/2/95	(1,674,703)
FFR 360,000,000	US\$ 59,292,444	2/13/95	(6,625,927)
DKR 290,000,000	US\$ 42,670,904	3/1/95	(3,402,528)
PTA 7,000,000,000	US\$ 47,964,917	3/13/95	(4,259,897)
US\$ 34,914,982	FFR 200,000,000	3/17/95	1,687,569
FFR 200,000,000	US\$ 34,208,501	3/17/95	(2,394,050)
YEN 5,000,000,000	US\$ 50,632,911	3/23/95	(1,256,701)
US\$ 36,120,208	DM 60,000,000	4/28/95	1,753,798
DM 60,000,000	US\$ 35,885,811	4/28/95	(1,988,195)
PND 25,000,000	US\$ 37,443,750	5/3/95	(1,028,750)
PTA 4,000,000,000	US\$ 28,985,507	5/5/95	(766,193)
PTA 4,000,000,000	US\$ 28,514,399	5/16/95	(1,218,105)
FFR 150,000,000	US\$ 26,325,026	5/17/95	(1,102,292)
DM 85,000,000	US\$ 51,816,630	6/16/95	(1,861,930)
YEN 9,000,000,000	US\$ 90,264,022	6/16/95	(3,871,542)
DM 100,000,000	US\$ 63,694,268	6/29/95	535,044
			<u>(98,688,691)</u>

APPENDIX I

SUMMARY OF INVESTMENTS BY MAJOR CATEGORY OF INDIVIDUAL PENSION FUNDS (TRADE DATE) CASH MANAGEMENT FUND

	Consolidated Police & Firemen's Pension Fund		Judicial Retirement System of New Jersey		Police & Firemen's Retirement System	
	Amortized Cost	Quoted Market	Amortized Cost	Quoted Market	Amortized Cost	Quoted Market
SHORT-TERM OBLIGATIONS						
U.S. Government and other government securities and obligations	\$ 5,773	\$ 5,772	\$ 490	\$ 490	\$ 23,120	\$ 23,117
Commercial paper	8,608	8,609	730	730	34,475	34,475
Time certificates of deposit	2,861	2,861	243	243	11,457	11,457
	<u>17,242</u>	<u>17,242</u>	<u>1,463</u>	<u>1,463</u>	<u>69,052</u>	<u>69,049</u>
LONG-TERM BONDS						
U.S. Government bonds and other government securities and obligations	18,873	19,296	41,954	42,163	1,801,837	1,810,802
Industrial bonds	—	—	2,329	2,330	99,928	99,990
Gas and electric bonds	200	200	1,734	1,680	76,206	73,837
Telephone bonds	—	—	593	568	26,443	25,340
Finance companies—senior debt	—	—	—	—	—	—
Intermediate term corporate notes	—	—	1,728	1,792	74,144	76,891
International Government bonds and notes	—	—	6,195	6,187	364,279	363,799
Other	—	—	845	838	44,580	44,514
	<u>19,073</u>	<u>19,496</u>	<u>55,378</u>	<u>55,558</u>	<u>2,487,417</u>	<u>2,495,173</u>
MORTGAGES						
Mortgage-backed certificates	6,256	6,073	2,422	2,347	730,288	729,173
STOCKS						
Common stock (U.S.)	—	—	45,210	66,876	2,386,475	3,530,151
Common stock (International)	—	—	3,299	3,463	193,978	203,631
	<u>—</u>	<u>—</u>	<u>48,509</u>	<u>70,339</u>	<u>2,580,453</u>	<u>3,733,782</u>
	42,571	42,811	107,772	129,707	5,867,210	7,027,177
Difference due to accounting practices	78	126	(2,469)	2,094	(265,151)	92,693
	<u>\$42,649</u>	<u>\$42,937</u>	<u>\$105,303</u>	<u>\$131,801</u>	<u>\$5,602,059</u>	<u>\$7,119,870</u>

INCLUDING INVESTMENTS OWNED BY THE COMMON FUNDS AND THE STATE OF NEW JERSEY
(000's Omitted) at June 30, 1994 (UNAUDITED)

Prison Officers Pension Fund		Public Employees' Retirement System		State Police Retirement System		Teachers' Pension and Annuity Fund		Totals	
Amortized Cost	Quoted Market	Amortized Cost	Quoted Market	Amortized Cost	Quoted Market	Amortized Cost	Quoted Market	Amortized Cost	Quoted Market
\$233	\$233	\$ 43,044	\$ 43,039	\$ 3,746	\$ 3,746	\$ 61,310	\$ 61,302	\$ 137,716	\$ 137,699
348	348	64,184	64,184	5,586	5,586	91,419	91,421	205,350	205,353
115	115	21,330	21,330	1,857	1,857	30,381	30,381	68,244	68,244
696	696	128,558	128,553	11,189	11,189	183,110	183,104	411,310	411,296
203	201	3,215,495	3,231,470	241,236	242,427	3,785,927	3,802,824	9,105,525	9,149,183
—	—	178,240	178,352	13,347	13,355	205,801	205,930	499,645	499,957
—	—	134,442	130,247	9,938	9,625	159,076	154,174	381,596	369,763
—	—	46,981	45,031	3,398	3,254	56,400	54,114	133,815	128,307
—	—	—	—	—	—	—	—	—	—
—	—	132,250	137,150	9,903	10,270	152,698	158,357	370,723	384,460
—	—	699,440	698,519	41,714	41,660	953,444	952,188	2,065,072	2,062,353
—	—	82,977	83,002	5,295	5,273	107,945	108,284	241,642	241,911
203	201	4,489,825	4,503,771	324,831	325,864	5,421,291	5,435,871	12,798,018	12,835,934
—	—	622,067	600,146	7,659	7,241	783,003	758,938	2,151,695	2,103,918
—	—	4,378,182	6,476,349	268,893	397,756	5,222,654	7,725,520	12,301,414	18,196,652
—	—	372,451	390,986	22,213	23,318	507,708	532,973	1,099,649	1,154,371
—	—	4,750,633	6,867,335	291,106	421,074	5,730,362	8,258,493	13,401,063	19,351,023
899	897	9,991,083	12,099,805	634,785	765,368	12,117,766	14,636,406	28,762,086	34,702,171
(330)	(328)	(510,877)	166,101	(32,064)	12,055	(557,287)	192,436	(1,368,100)	465,177
\$569	\$569	\$9,480,206	\$12,265,906	\$602,721	\$777,423	\$11,560,479	\$14,828,842	\$27,393,986	\$35,167,348

APPENDIX II

UNAUDITED COMMON PERFORMANCE DISCLOSURE FORM FOR PUBLIC FUNDS

	Avg. Annual Return 5 Years Ended 6/30/94	One Year Period Ended				
		6/30/90	6/30/91	6/30/92	6/30/93	6/30/94
TOTAL RETURN						
Aggregate of All Pension Funds	9.4%	13.3%	9.3%	13.8%	12.5%	-0.7%
Consumer Price Index	3.6%	4.7%	4.7%	3.0%	3.0%	2.5%
STOCK TOTAL RETURNS						
Common Pension Fund A—All Stocks	10.0%	18.6%	8.1%	12.7%	12.3%	-0.7%
Common Pension Fund A—Small Capitalization Stocks	—	—	29.3% (1)	32.6%	21.2%	5.9%
Approved List—Before Divestment	10.6%	17.3%	8.6%	13.3%	13.0%	1.6%
Approved List—South Africa Free	10.2%	14.0%	7.6%	14.5%	14.6%	1.1%
Dow Jones Industrial Average	11.9%	22.8%	4.7%	17.1%	9.2%	6.0%
Standard & Poor's 500 Index	10.3%	16.5%	7.4%	13.4%	13.6%	1.4%
FIXED INCOME TOTAL RETURNS						
Common Pension Fund B and Other Bonds	8.8%	7.2%	10.3%	14.7%	14.0%	-1.4%
Shearson Lehman Government/Corporate Bond Index	8.5%	7.1%	10.2%	14.2%	13.2%	-1.5%
Salomon Brothers High Grade Bond Index (AA and AAA)	9.0%	6.0%	10.6%	16.8%	16.3%	-3.6%
Salomon Brothers Broad Bond Index	8.6%	7.7%	10.8%	14.1%	12.0%	-1.2%
MORTGAGES—TOTAL RETURNS						
Pension fund holdings	8.7%	9.2%	12.0%	15.8%	9.2%	-1.6%
Salomon Brothers Mortgage Index	8.7%	9.7%	12.0%	14.0%	9.1%	-0.9%
INTERNATIONAL TOTAL RETURNS						
Common Fund D Total—Hedged	—	—	—	22.3%	9.8%	2.7%
Common Fund D Fixed Income	—	—	—	23.4%	9.4%	-0.1%
Common Fund D Stocks	—	—	—	NM	15.6%	13.3%
Approved List—International Stocks	—	—	—	—	18.6%	13.7%
Salomon World Gov. Bonds Index—Unhedged	10.6%	7.0%	10.0%	20.5%	10.9%	5.1%
EAFE International Stock Index	5.0%	3.3%	(11.5)%	(0.7)%	20.3%	17.0%
CASH EQUIVALENTS						
Total Returns—Cash Management Fund	5.9%	8.9%	7.9%	5.5%	3.8%	3.6%
91-Day Treasury Bills	5.1%	7.9%	6.8%	4.7%	3.1%	3.2%

(1) For six months ended June 30, 1991

Several public funds have voluntarily undertaken to create common standards for reporting returns. This table is provided in accordance with the Division's desire to further comparability of public fund reporting.

The aggregate total returns shown on the above table are estimates, and are shown for illustrative purposes only. The Division does not have the resources to price all of its securities on a periodic basis, which would be necessary for an accurate calculation of total returns which includes both income and changes in market values.

UNIVERSITY OF CALIFORNIA, BERKELEY INVESTMENT DISCLOSURE FORM

For the Fiscal Year

Investment Category	1994	1995	1996	1997	1998
Domestic Equity	10.5	11.2	12.1	13.5	14.8
International Equity	8.2	9.1	10.5	11.8	13.2
Fixed Income	5.1	5.8	6.5	7.2	8.1
Real Estate	3.4	3.9	4.5	5.1	5.8
Private Equity	2.1	2.5	3.1	3.8	4.5
Commodities	1.2	1.5	1.8	2.1	2.5
Other	0.8	1.1	1.4	1.7	2.1
Total	31.3	35.2	40.9	47.4	53.0
Domestic Equity	10.5	11.2	12.1	13.5	14.8
International Equity	8.2	9.1	10.5	11.8	13.2
Fixed Income	5.1	5.8	6.5	7.2	8.1
Real Estate	3.4	3.9	4.5	5.1	5.8
Private Equity	2.1	2.5	3.1	3.8	4.5
Commodities	1.2	1.5	1.8	2.1	2.5
Other	0.8	1.1	1.4	1.7	2.1
Total	31.3	35.2	40.9	47.4	53.0

The following table shows the percentage of the total portfolio invested in each of the investment categories listed above. The percentages are based on the end of the fiscal year. The percentages may not add to 100% due to rounding.

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