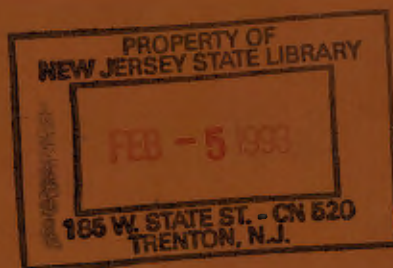




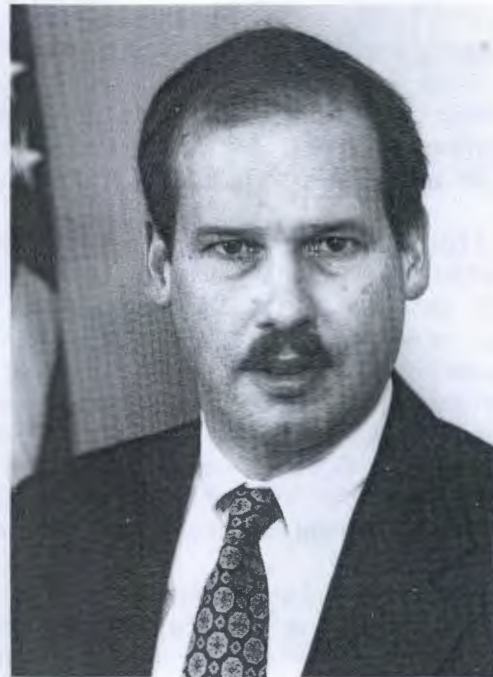
**STATE INVESTMENT COUNCIL  
DEPARTMENT OF THE TREASURY  
STATE OF NEW JERSEY**



**FORTY-SECOND ANNUAL REPORT**  
**For the Fiscal Year Ended June 30, 1992**



JIM FLORIO  
Governor



SAMUEL CRANE  
State Treasurer

A Report to  
Governor Jim Florio,  
the Members of the  
New Jersey Legislature  
and the State Treasurer

Submitted by the  
State Investment Council

For the Fiscal Year ended June 30, 1992



November 15, 1992

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, 1992, as required by Section 13, P.L. 1950, c. 170. This 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 Division of Investment.

The Division of Investment, under the jurisdiction of the State Investment Council, has the investment responsibility for 117 funds, including seven pension and annuity funds. The book value of all funds on June 30, 1992, was \$33.0 billion, compared to \$29.9 billion at the end of the prior year, and the market value of the funds was \$40.3 billion, compared with \$35.2 billion at the end of the previous fiscal year. The Council comprises ten persons appointed to fixed terms, five employee representatives appointed by their respective pension fund boards for one year terms and five gubernatorial appointees serving staggered five year terms. Recent legislation has 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. State law requires that no Council member 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. The Council is pleased to note that the returns earned on the pension funds over time have resulted in significant increases in the market values of the funds; when these market values were recognized under the pension revaluation plan that was enacted in 1992, savings of almost \$1.0 billion were reflected in the state's fiscal 1993 budget. The reduced appropriations for pension expenses of \$1.0 billion represented about 8 percent of the state's budget for fiscal 1993 and permitted the state to provide funding for other critical programs during a time of fiscal crisis, without any reduction in the appropriate level of support for the beneficiaries of the state pension funds. The \$1.0 billion in savings consists of \$773 million which was realized in fiscal 1992 and \$226 million which will be realized annually in fiscal 1993 and subsequent years. The state funds have been invested in conformity with the regulations of the Council and in accordance with policies approved by the Council. Appendix II sets forth the estimated total returns of the state administered pension funds for the past five years.

Fiscal 1992 provided strong, positive returns for the Division. The returns on book value of the pension funds met the statutory requirements set by state law. Furthermore, the estimated total return on the pension funds, which includes changes in the market values of the securities held by the funds and dividend and investment income over the year, was 13.8 percent, which compares with a 10.0 percent return in fiscal 1991. For the past five fiscal years the estimated average annual total return earned by the pension funds was 10.1 percent. These total returns of the pension funds ranked the Division in the top third of all balanced fund managers in fiscal 1992, and in the top quarter for the five year period ended June 30, 1992. Appendix II sets forth the estimated total returns of the state administered pension funds.

All investments under the supervision of the Council must conform to standards of prudence established by state law, which mandates 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 other 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 be the only factors 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 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 Governors Byrne and Kean, representing different political parties, and both commissions support the present structure and policies of the Council. Summaries of these reports are included herein.

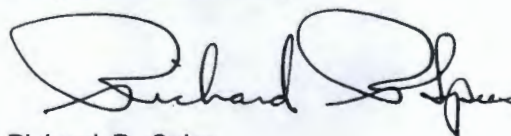
The Council is pleased to note that a large majority of the corporate debt obligations and equities held by the Division have been issued by corporations which are identified as New Jersey employers. The pension funds have investments in major companies which have their headquarters in New Jersey and in out-of-state companies which provide significant 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 do so, 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 we have declined to do so since Council members believe that it would be a violation of our fiduciary responsibilities to the beneficiaries of the funds under our supervision. Furthermore, in many instances, such programs can be funded through tax-exempt bond financing, which 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 assets among asset classes and the globalization of investments. In fiscal 1992, the Council addressed the issue of the Division's budget and staffing and concluded that the resources available to the Division in the current state budget are not sufficient to support adequately the investment programs of the state. This issue will be addressed to the appropriate state officials.

The Council members are grateful for the many years of outstanding service to the Division which were provided by Peter Pantelides, John Bulakowski and Jack Pennington, who retired during the year.

For each of the past forty-two years, the Council has requested and obtained a review of the records and procedures of the Division by an independent auditor. The auditor'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". The signature is fluid and cursive, with a large initial "R" and "S".

Richard R. Spies  
Chair



# The State Investment Council

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**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



**ROY D. BLOOM**  
State Police Retirement  
System



**REGINE BROWN**  
Public Employees'  
Retirement System



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

# Division of Investment

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ROLAND M. MACHOLD  
Director



STEVEN E. KORNRUMPF  
Deputy Director



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





Administration Group: Celeste Brennan, Cindy Everett, Roland Machold, Pat Osvai, Steve Kornrumpf and Cathy Ryan.



Portfolio Management Group: Dick McGowan, Linda Thompson, Linda Brooks, Don Haroz, Sandra Holmes, Bruce Smith and Dolores Ewanis.



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



Research Group: Tom Montalto, Denise Szeker, Brian Arena, Karin Hollinger, Linda Gaspari, Jim Vandervort, Anne McDermott and Victor Yu.



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: Charles Coleman, Olga Grozio, Linda Coughlan, Nancy Brancolino, Ken Scott and Roxanne Tyner.



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



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



# FIVE YEAR SUMMARY

	Fiscal Year Ended June 30,				
	1988	1989	1990	1991	1992
	\$ Millions				
<b>FUNDS UNDER THE SUPERVISION OF THE STATE INVESTMENT COUNCIL:</b>					
Book Value at Year End:					
Pension Funds	\$17,405	\$19,517	\$21,697	\$24,081	\$26,223
All Funds	22,443	24,115	26,286	29,924	32,981
Market Value at Year End:					
Pension Funds	\$19,892	\$23,049	\$26,335	\$29,272	\$33,490
All Funds	24,981	27,700	30,978	35,166	40,313
Market Value of Pension Funds at Year End by Category:					
Short-term obligations	\$ 643	\$ 769	\$ 976	\$ 1,011	\$ 1,006
Long-term bonds	7,332	8,311	8,712	10,139	11,794
Mortgages	2,569	3,180	3,656	3,951	3,787
Stocks	9,179	10,505	12,725	13,977	16,379
Accounting differences	169	284	266	194	524
Total	\$19,892	\$23,049	\$26,335	\$29,272	\$33,490
Investment Income:					
Pension Funds	\$ 1,174	\$ 1,360	\$ 1,517	\$ 1,653	\$ 1,829
All Funds	1,475	1,681	1,867	2,011	2,166
Total Rate of Return (1)					
Common Pension Fund A (2)	(10.2)%	16.6%	18.7%	8.0%	12.6%
Common Pension Fund B (2)	7.4	13.0	7.2	10.3	14.5
Common Pension Fund D (2)	—	—	—	—	22.3
All Pension Funds, Estimated (2)	(0.7)	14.5	13.3	10.0(3)	13.8
Supplemental Annuity Collective Trust	(10.4)	13.5	14.7	5.8	12.9
Deferred Compensation Plan—Equity	(11.4)	15.1	19.7	5.3	10.6
Deferred Compensation Plan—Debt	7.3	11.5	7.1	10.5	14.7
Returns of Various Market Indices:					
Salomon Brothers' Mortgage Index	9.4%	11.8%	9.7%	12.0%	14.0%
Salomon Brothers' High Grade Corporate Bond Index	8.5	16.2	6.0	10.6	16.8
Shearson Lehman Government/Corporate Bond Index	7.5	12.3	7.1	10.2	14.1
S&P's 500	(6.9)	20.5	16.5	7.4	13.4
S&P's Mid-cap	(2.3)	22.1	15.4	12.8	18.6
Dow Jones Industrials Average	(8.3)	18.7	22.8	4.7	17.7
Salomon Brothers' World Gov. Index—Unhedged	9.7	4.3	7.0	10.0	20.5
EAFE International Stock Index	4.1	9.5	3.3	(11.5)	(0.7)
State of New Jersey Cash Management Fund:					
Book Value of Units of Participation:					
All Participants	\$ 5,381	\$ 4,936	\$ 5,740	\$ 6,946	\$ 8,045
Other-than-State Participants	1,299	1,118	1,437	2,130	3,111
Average Annualized Daily Rate of Return:					
State Participants	6.88%	8.08%	8.57%	7.47%	5.30%
Other-than-State Participants	6.67	7.95	8.42	7.30	5.12
Number of Funds Under the Supervision of the State Investment Council	108	110	121	115	117
Total Number of Transactions	36,410	32,281	34,600	38,298	40,534

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 117 investment funds under the supervision of the Council on June 30, 1992, had a book value of \$33.0 billion. This total represents an increase of 10.4 percent over the 1991 fiscal year-end total of \$29.9 billion held by 115 funds. The investment funds had a market value of \$40.3 billion at June 30, 1992, an increase of 14.5 percent over the market value of \$35.2 billion at June 30, 1991. The market value of the seven pension funds increased from \$29.3 billion at June 30, 1991, to \$33.5 billion at June 30, 1992. The market value of the pension funds increased due to lower interest rates, which improved the prices of the bonds held by the Division, and the continuing recovery of stock prices during the fiscal year.

Investment income for all funds for fiscal 1992 amounted to \$2.2 billion as compared with \$2.0 billion last year. Income remained stable as lower interest rates offset the effect of higher fund balances.

During the year, the Division of Investment purchased securities with a par value of \$94.3 billion. Approximately 28.0 percent of this amount, or \$26.4 billion, represented the overnight investment of surplus balances in the state's cash accounts. In fiscal 1991, the Division purchased securities with a par value of \$91.8 billion, of which \$34.8 billion was generated by overnight investments. During fiscal 1992, the Division's net holdings of mortgages decreased from \$4.0 billion to \$3.8 billion, due to substantial refunding of mortgages by home owners.

The Division sold securities totaling \$7.4 billion in fiscal 1992, compared with sales of \$3.4 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 \$195 million during the year, compared with \$153 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.

## Effective Rates of Return and "Regular Interest Rates"

Prior to the passage of the pension revaluation law in June, 1992, state law required that the effective rates of the respective pension funds should maintain a relationship to the "regular interest rates" of the funds. The effective rates were based on the dividend and interest income of the funds and the book value of the funds' assets. In turn, the "regular interest rate" was used by the actuaries to project future income and asset growth of the funds for actuarial determinations. The new law utilizes market values and assumed market returns for actuarial determinations, and the relationship of income and assets based on book value is no longer used. For historical purposes, the average effective rate of the aggregate pension fund portfolios, based on book value, was 6.84 percent, compared with 7.12 percent at the end of the prior year. The rates declined during the year due to lower interest rates and a recessionary economic environment.

The pension revaluation law now sets the "regular interest rate" of the pension funds at 8¾ percent, which reflects expected income and market returns of the funds. This rate compares with a rate of 7 percent that prevailed prior to the passage of the law, but which only reflected income and the book value of assets. 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 assumed percentage rate of increase applied to salaries is 6¼ percent for the pension funds.

## Fixed Income

Total fixed income allocations for new investment in fiscal 1992 totalled \$1,683.1 million, of which \$645.0 million was allocated to the purchase of U.S. Government and corporate debt securities, and \$850.0 million was allocated for international fixed income investment through Common Pension Fund D. The remaining \$188.1 million of funds for new fixed income investment was allocated to the purchase of mortgage-backed securities issued by various agencies supported by the U.S. Government.

From July 1, 1991, through June 30, 1992, the Division purchased \$1,101.0 million of FHLMC and GNMA 15 year and 30 year mortgage-backed securities and \$262.0 million of collateralized mortgage



obligations (CMOs). Principal repayments on mortgage-backed securities held by the Division for fiscal 1992 totaled \$575.4 million.

In fiscal 1992, the Division sold \$1,174.9 million of FHLMC and GNMA mortgages and realized profits of \$78.6 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.

### **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 stocks, bonds and international investments, respectively. At June 30, 1992, the market values of the units of ownership of Common Pension Fund A, Common Pension Fund B and Common Pension Fund D were \$16.4 billion, \$10.7 billion and \$1.4 billion, respectively. The State of New Jersey Cash Management Fund provides a vehicle for the pension funds to make short-term investments.

During fiscal 1992, the Council approved the distribution of \$135.2 million of realized gains from Common Pension Fund A to the participating pension funds.

### **Total Rate of Return Calculations for Select Portfolios**

Calculations of total rate of return reflect both income and changes in 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 his-

torical returns are shown on page 7 herein.

SEI Evaluation Services has provided the Division with calculations of total return, and its data show that the total returns for Common Pension Funds A, B and D in fiscal 1992 were 12.6 percent, 14.5 percent and 22.3 percent, respectively. The remaining securities held directly by the pension funds consist primarily of mortgages and industrial bonds. If the returns provided by Indata for these portfolios are used for these holdings, then it is possible to estimate that the total return of the aggregate pension fund portfolios was approximately 13.8 percent in fiscal 1992, compared with returns of 10.0 percent in fiscal 1991 and 13.3 percent in fiscal 1990. 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 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 increased from \$6.9 billion at June 30, 1991, to \$8.0 billion at June 30, 1992, due to higher balances in the state's pension accounts and the accounts of participating municipalities and state agencies.

The net investment income of the fund was \$405 million in fiscal 1992, compared with \$432 million in fiscal 1991. The number of participating state funds increased from 115 to 117 during the year. The income of the fund fell in fiscal 1992, due to sharply lower short-term interest rates available in financial markets.

In fiscal 1992, the number of "Other-than-State" participants increased from 638 to 747, and the aggregate investment of "Other-than-State" participants was \$3.1 billion at the end of fiscal 1992, compared with \$2.1 billion at the end of fiscal 1991.



The average daily annualized rate of return to participating state accounts and accounts of the pension funds was 5.30 percent during fiscal 1992, compared with 7.47 percent during fiscal 1991. During fiscal 1992, the highest daily annualized rate of return to "Other-than-State" participants was 6.08 percent on August 12, 1991, and the lowest was 4.17 percent on June 26, 1992. The average daily annualized rate of return to "Other-than-State" participants, which is net of two small charges, was 5.12 percent in fiscal 1992, compared with 7.30 percent in fiscal 1991.

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 1992 was 5.33 percent, compared with 7.57 percent in the prior year. The lower rates of return during fiscal 1992 were the result of sharply lower interest rates available in the markets for short-term debt investments, as the Federal Reserve Bank lowered interest rates in response to a national recession.

## Historical Background

### Legislative History

Fiscal 1992 marks 42 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 117 funds in 1992, with a book value of \$33.0 billion and a market value of \$40.3 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 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 Council has requested and obtained 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 stocks, 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 act further provided that certain reports had to be filed on a quarterly and semi-annual basis. The final report to the Legislature for the period July 1, 1988, through August 27, 1988, and

cumulatively 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 remains in compliance with the law.

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 December 1992, 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.

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 General Assembly.



## **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 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, 1992, the aggregate common stock holdings of the pension funds were 48.9 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.

## **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 non-professional 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.

The Council concluded at that time that its objective for the active pension funds was to reach a 50 percent commitment to stocks, based on book value, with the provisos that an expansion of the stock program would not endanger the realization of the "regular interest rates" utilized by the actuaries and that expansion of the program be flexible in view of changing market conditions. In July, 1985, the Council acted to amend its regulations to permit commitment to stocks of up to 40 percent by the pension funds. However, at that time, the Council refrained from increasing the limitation to 50 percent in view of the prospective enactment of South Africa divestment legislation which would have the effect of limiting available stock investments to a universe of smaller companies with a higher risk profile. (Subsequent to 1985, the Division completed the divestment program, and the Council has increased the permitted investment in stock by the pension funds to 60 percent of the market value of the funds.)

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 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 concluded 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 concluded that no modifications in investment objectives were warranted.

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 that the present investment regulations provide 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.

The Council reviewed and confirmed the 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 the 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.

The Council also considered the further pooling of direct holdings of pension fund bond assets. The Council concluded that pooling of the bonds held directly by the pension funds would permit greater operating efficiencies and better measurement of pension fund performance. By the end of fiscal 1992, only a very small percentage of pension fund assets was represented by direct bond holdings.

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 state's divestment legislation had reduced the universe available for investment. Furthermore, the studies noted 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), who 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. These changes were initiated in order to provide greater diversification for pension fund investments and to increase access to asset classes which have historically provided slightly higher returns and lower risk than domestic securities.

In fiscal 1992, the Council studied the resources provided to the Division and concluded that the resources provided to the Division were not sufficient to support adequately 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 has discussed its concerns with the appropriate officials in anticipation of submission of the Division's proposed budget for fiscal 1994.

## **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, including stocks, industrial bonds, utility bonds, bank stocks and indebtedness, U.S. Government securities, mortgages and commercial paper and finance company debt. These reviews are extensive and encompass financial, economic and social factors. For instance, in fiscal 1992, the report on securities issued by utilities analyzed issues associated with the implementation of nuclear power plants and with deregulation. Similar reports on other classes of securities analyzed the exposure of American banks to real estate loans and governmental support for farm credit and mortgage programs.

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 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 have been 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 1992, approximately \$1.0 million of New Jersey mortgages were purchased by the Division under this program.

## Reports of Gubernatorial Commissions

In fiscal 1982, then 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, then 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 exposure from 25 percent of book value to 35 percent of book value is an example of a positive step already taken. A subsequent increase to 50 percent would be worthy of consideration. 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 1992, the Council again reviewed these issues and has taken them up with the appropriate authorities.

## **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 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 or are controlled by economically disadvantaged individuals, provided such investments meet the fiduciary standards of the Council and provide fair market returns.

## **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 gov-



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ernance, 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 1992, the Division voted on 368 corporate proxies. On 78 proxies the Division voted

against the recommendations of corporate management on a total of 91 individual proposals. Of these proposals, 36 concerned changes in corporate governance procedures designed to reduce shareholder voting power, eight related to corporate activities in South Africa, 27 related to executive compensation, seven related to compliance of the corporation with the MacBride principles in Northern Ireland, 11 related to confidential proxy voting, one related to state of incorporation, and one related to supporting expanded energy conservation.



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

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## REPORT OF INDEPENDENT AUDITORS

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

We have audited the amortized cost basis on 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, 1992, 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 amortized cost of the investments by fund and major category of the Division of Investment, Department of the Treasury, State of New Jersey at June 30, 1992, and the related investment income and investment activity for the year then ended, in conformity with generally accepted accounting principles.

Our audit was made for the purpose of forming an opinion on the amortized cost of investments by fund and by major category taken as a whole. The par, cost or principal amount, market value and market value over (under) amortized cost at June 30, 1992 are presented for purposes of additional analysis and are not a required part of the financial summaries. Such information has been subjected to the auditing procedures applied in our audit of the amortized cost and, in our opinion, is fairly stated in all material respects in relation to the amortized cost taken as a whole.

Princeton, New Jersey  
August 28, 1992

*Ernst & Young*



# SUMMARY OF AMOUNTS INVESTED BY FUND

## June 30, 1992

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
<b>PENSION AND ANNUITY GROUP</b>				
Consolidated Police and Firemen's Pension Fund	\$ 54,390,665	\$ 54,052,762	\$ 55,682,847	\$ 1,630,085
Judicial Retirement System of New Jersey	101,163,495	101,000,369	125,733,588	24,733,219
Police and Firemen's Retirement System	5,074,439,487	5,052,434,518	6,471,526,984	1,419,092,466
Prison Officers Pension Fund	833,224	833,224	833,224	—
Public Employees' Retirement System	9,277,462,840	9,243,172,645	11,858,575,004	2,615,402,359
State Police Retirement System	596,796,417	595,866,075	756,895,434	161,029,359
Teachers' Pension and Annuity Fund	11,214,133,897	11,175,236,522	14,221,101,447	3,045,864,925
		26,222,596,115	33,490,348,528	7,267,752,413
<b>STATIC GROUP</b>				
Trustees for the Support of Free Public Schools Fund	73,076,619	72,903,139	93,584,679	20,681,540
Waste Water Treatment Fund (Act of 1985)	48,321,430	48,321,430	48,321,430	—
Waste Water Treatment Trust Fund (Act of 1985)	56,805	56,805	56,805	—
		121,281,374	141,962,914	20,681,540
<b>DEMAND GROUP</b>				
Atlantic City Tourism Promotion Fund	1,520,670	1,520,670	1,520,670	—
Boarding House Rental Assistance Fund	19,025,183	19,025,183	19,025,183	—
Catastrophic Illness in Children Relief Fund (Act of 1987)	27,201,087	27,201,087	27,201,087	—
Clean Communities Account Fund (Act of 1985)	13,477,645	13,477,645	13,477,645	—
Development Fund—Luxury Tax	4,123,357	4,123,357	4,123,357	—
Emergency Services Fund	6,237,719	6,237,719	6,237,719	—
Enterprise Zone Assistance Fund (Act of 1983)	23,092,186	23,092,186	23,092,186	—
Health Care Cost Reduction Fund	33,450,046	33,450,046	33,450,046	—
Higher Education Assistance Fund	33,852,577	33,852,577	33,852,577	—
Luxury Tax Fund	25,529,249	25,529,249	25,529,249	—
Motor Vehicle Security Responsibility Fund	142,129	142,129	142,129	—
New Jersey Automobile Insurance Guaranty Fund	112,211,931	112,211,931	112,211,931	—
New Jersey Health Care Trust	8,154,553	8,154,553	8,154,553	—
New Jersey Insurance Development Fund	74,137,414	74,083,949	74,187,414	103,465
New Jersey Spill Compensation Fund	99,915,167	99,915,167	99,915,167	—
Outstanding Checks Account	15,798,485	15,798,485	15,798,485	—
Real Estate Guaranty Fund	472,101	472,101	472,101	—
Resource Recovery Investment Tax Fund (Act of 1985)	67,592,284	67,592,284	67,592,284	—
Sanitary Landfill Facility Contingency Fund	44,220,540	44,220,540	44,220,540	—
Solid Waste Services Tax Fund (Act of 1985)	16,580,925	16,580,925	16,580,925	—
State Disability Benefits Fund	139,591,434	139,493,317	140,978,333	1,485,016
State Recycling Fund	27,397,757	27,397,757	27,397,757	—
Unclaimed Personal Property Trust Fund	63,617,633	63,613,784	63,716,333	102,549
Unemployed Compensation Auxiliary Fund	5,062,219	5,062,219	5,062,219	—
Unsatisfied Claim and Judgment Fund	287,357,646	287,357,646	287,357,646	—
Volunteer Emergency Service Organizations Loan Fund	167,983	167,983	167,983	—
Worker and Community Right to Know Fund	7,182,447	7,182,447	7,182,447	—
Workmen's Compensation Security Fund—Mutual	4,567,941	4,567,497	4,575,541	8,044
Workmen's Compensation Security Fund—Stock	67,238,758	67,227,647	67,428,758	201,111
		1,228,752,080	1,230,652,265	1,900,185
<b>TEMPORARY RESERVE GROUP</b>				
Alcohol Education Rehabilitation and Enforcement Fund	16,376,442	16,453,592	16,768,442	314,850
Beaches and Harbor Fund (Act of 1977)	1,617,182	1,617,182	1,617,182	—
Capital City Redevelopment Loan and Grant Fund	4,499,660	4,499,660	4,499,660	—
Clean Waters Fund (Act of 1976)	7,433,552	7,433,552	7,433,552	—
Community Development Bond Fund (Act of 1981)	9,864,616	9,864,616	9,864,616	—
Correctional Facilities Construction Fund (Act of 1982)	5,588,628	5,588,628	5,588,628	—
Correctional Facilities Construction Fund (Act of 1987)	78,431,917	78,431,917	78,431,917	—
Emergency Flood Control Fund (Act of 1978)	5,018,152	5,018,152	5,018,152	—
Energy Conservation Fund (Act of 1980)	23,366,654	23,366,654	23,366,654	—
Farmland Preservation Fund (Act of 1981)	3,211,375	3,211,375	3,211,375	—
Farmland Preservation Fund (Act of 1989)	16,833,249	16,833,249	16,833,249	—
General Investment Fund	592,768,342	592,759,600	592,761,641	2,041
General Trust Fund	15,526	15,526	15,526	—
Green Acres Cultural Centers and Historic Preservation Bond Fund (Act of 1987)	61,447,866	61,447,866	61,447,866	—
Green Trust Fund (Act of 1983)	17,686,628	17,686,628	17,686,628	—
Hazardous Discharge Fund (Act of 1981)	45,821,710	45,821,710	45,821,710	—
Hazardous Discharge Site Cleanup Fund (Act of 1985)	13,642,581	13,642,581	13,642,581	—
Higher Education Buildings Construction Fund (Act of 1971)	467,545	467,545	467,545	—



## SUMMARY OF AMOUNTS INVESTED BY FUND—(CONTINUED)

June 30, 1992

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
Housing Assistance Fund (Act of 1968)	\$ 572,636	\$ 572,636	\$ 572,636	—
Human Services Facilities Construction Fund (Act of 1984)	8,717,584	8,717,584	8,717,584	—
Institutional Construction Fund (Act of 1978)	156,122	156,122	156,122	—
Institutions Construction Fund (Act of 1976)	78,014	78,014	78,014	—
Jobs, Science and Technology Fund (Act of 1984)	7,836,916	7,836,916	7,836,916	—
Jobs, Education and Competitiveness Fund (Act of 1988)	194,321,237	194,321,237	194,321,237	—
Medical Education Facilities Fund (Act of 1977)	541,386	541,386	541,386	—
Mortgage Assistance Fund (Act of 1976)	3,142,663	3,142,663	3,142,663	—
Natural Resources Fund (Act of 1980)	14,960,046	14,960,046	14,960,046	—
New Home Warranty Security Fund	65,760,438	65,877,053	66,847,378	\$ 970,325
New Jersey Bridge Rehabilitation Fund (Act of 1983)	23,911,299	23,911,299	23,911,299	—
New Jersey Bridge Rehabilitation and Improvement and Railroad Right-of-Way Preservation Fund (Act of 1989)	38,821,962	38,821,962	38,821,962	—
New Jersey Green Acres Fund (Act of 1983)	24,303,954	24,303,954	24,303,954	—
New Jersey Green Acres Fund (Act of 1989)	38,010,873	38,010,873	38,010,873	—
New Jersey Green Trust Fund (Act of 1989)	35,272,265	35,272,265	35,272,265	—
New Jersey Local Development Financing Fund	3,091,362	3,091,362	3,091,362	—
New Jersey Medical Malpractice Reinsurance Recovery Fund	4,859,740	4,859,740	4,859,740	—
New Jersey State Dental Program	10,928,588	10,928,588	10,928,588	—
Pension Adjustment Fund	14,563,520	14,563,520	14,563,520	—
Pension Payroll Investment Fund	356,173	356,173	356,173	—
Pinelands Infrastructure Trust Fund (Act of 1985)	8,651,191	8,651,191	8,651,191	—
Pollution Prevention Fund	1,623,232	1,623,232	1,623,232	—
Prescription Drug Program Fund	1,407,732	1,407,732	1,407,732	—
Public Buildings Construction Fund (Act of 1968)	688,489	688,489	688,489	—
Public Purpose Buildings and Community-Based Facilities Construction Fund (Act of 1989)	71,956,837	71,956,837	71,956,837	—
Public Purpose Buildings Construction Fund (Act of 1980)	14,679,625	14,679,625	14,679,625	—
Resource Recovery and Solid Waste Disposal Facility Fund (Act of 1985)	41,394,076	41,394,076	41,394,076	—
Safe Drinking Water Fund	10,683,543	10,683,543	10,683,543	—
Shore Protection Fund (Act of 1983)	9,834,863	9,834,863	9,834,863	—
State Facilities for Handicapped Fund (Act of 1973)	2,066,055	2,066,055	2,066,055	—
State Health Benefits Fund	189,622,435	189,771,440	191,001,935	1,230,495
State Land Acquisition and Development Fund (Act of 1978)	3,759,860	3,759,860	3,759,860	—
State Lottery Fund—Investment	59,569,622	59,569,622	59,569,622	—
State of New Jersey—Alternate Benefit Program	8,922,308	8,922,308	8,922,308	—
State of New Jersey Cash Management Fund— Administrative Expense Fund	1,338,188	1,338,188	1,338,188	—
State of New Jersey Cash Management Fund— Other than State Funds	3,112,151,739	3,112,151,739	3,112,151,739	—
State of New Jersey Cash Management Fund— Reserve Fund	19,766,995	19,766,995	19,766,995	—
State Recreation and Conservation Land Acquisition Fund (Act of 1974)	3,501,818	3,501,818	3,501,818	—
State Recreation and Conservation Land Acquisition Fund (Act of 1971)	4,930,147	4,930,147	4,930,147	—
State Transportation Fund (Act of 1968)	268,194	268,194	268,194	—
State Water Development Fund (Act of 1958)	18,619	18,619	18,619	—
Stormwater Management and Combined Sewer Overflow Abatement Fund (Act of 1989)	15,874,311	15,874,311	15,874,311	—
Transportation Rehabilitation and Improvement Fund (Act of 1979)	18,880,861	18,880,861	18,880,861	—
University of Medicine and Dentistry of New Jersey—Self-Insurance Reserve Fund	32,185,388	31,227,900	31,690,198	462,298
Veterans' Guaranteed Loan Fund	16,121	16,121	16,121	—
Water Conservation Fund (Act of 1969)	5,029,133	5,029,133	5,029,133	—
Water Supply Fund (Act of 1981)	76,299,149	76,299,149	76,299,149	—
Water Supply Replacement Trust Fund	7,567,837	7,567,837	7,567,837	—
		5,116,363,311	5,119,343,320	2,980,009



**SUMMARY OF AMOUNTS INVESTED BY FUND (CONCLUDED)**  
**June 30, 1992**

	Par, Cost Or Principal Amount— Note 1	Amortized Cost— Note 1	Market— Note 1	Market Over Amortized Cost
<b>TRUST GROUP</b>				
New Jersey State Employees' Deferred Compensation Administrative Charges	\$ 592,051	\$ 592,051	\$ 592,051	—
New Jersey State Employees' Deferred Compensation Cash Management Fund	75,546,248	75,546,248	75,546,248	—
New Jersey State Employees' Deferred Compensation Equity Fund	64,130,942	64,130,942	74,413,842	\$ 10,282,900
New Jersey State Employees' Deferred Compensation Fixed Income Fund	49,624,052	49,489,089	51,041,982	1,552,893
New Jersey State Employees' Deferred Compensation Holding Account	2,626,137	2,626,137	2,626,137	—
Supplemental Annuity Collective Trust Fund	99,168,129	99,168,129	126,302,158	27,134,029
Tischler Memorial Fund	565,778	563,407	587,733	24,326
		<u>292,116,003</u>	<u>331,110,151</u>	<u>38,994,148</u>
<b>TOTAL AMOUNTS INVESTED BY FUND</b>		<u><u>\$32,981,108,883</u></u>	<u><u>\$40,313,417,178</u></u>	<u><u>\$7,332,308,295</u></u>

See notes to investment summaries.



**SUMMARY OF INVESTMENT INCOME BY FUND**  
**Year Ended June 30, 1992**

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
<b>PENSION AND ANNUITY GROUP</b>			
Consolidated Police and Firemen's Pension Fund	\$ 5,097,254	\$ 238,980	\$ 5,336,234
Judicial Retirement System of New Jersey	6,843,921	209,732	7,053,653
Police and Firemen's Retirement System	338,289,588	16,801,554	355,091,142
Prison Officers Pension Fund	100,998	—	100,998
Public Employees' Retirement System	615,781,999	30,782,137	646,564,136
State Police Retirement System	38,566,586	566,974	39,133,560
Teachers' Pension and Annuity Fund	733,799,038	41,588,563	775,387,601
	<u>1,738,479,384</u>	<u>90,187,940</u>	<u>1,828,667,324</u>
<b>STATIC GROUP</b>			
Trustees for the Support of Free Public Schools Fund	5,774,379	288,408	6,062,787
Waste Water Treatment Fund (Act of 1985)	2,452,210	—	2,452,210
Waste Water Treatment Trust Fund (Act of 1985)	67,443	—	67,443
	<u>8,294,032</u>	<u>288,408</u>	<u>8,582,440</u>
<b>DEMAND GROUP</b>			
Atlantic City Tourism Promotion Fund	6,670	—	6,670
Boarding House Rental Assistance Fund	877,546	—	877,546
Catastrophic Illness in Children Relief Fund (Act of 1987)	1,078,745	—	1,078,745
Clean Communities Account Fund (Act of 1985)	692,010	—	692,010
Development Fund—Luxury Tax	252,423	—	252,423
Emergency Services Fund	228,494	—	228,494
Enterprise Zone Assistance Fund (Act of 1983)	1,125,236	—	1,125,236
Health Care Cost Reduction Fund	691,046	—	691,046
Higher Education Assistance Fund	1,697,704	—	1,697,704
Luxury Tax Fund	1,412,559	—	1,412,559
Motor Vehicle Security Responsibility Fund	7,573	—	7,573
New Jersey Automobile Insurance Guaranty Fund	3,816,686	—	3,816,686
New Jersey Health Care Trust	728,671	—	728,671
New Jersey Insurance Development Fund	4,386,508	—	4,386,508
New Jersey Spill Compensation Fund	5,133,579	—	5,133,579
New Jersey Uncompensated Care Trust Fund	208,800	—	208,800
Outstanding Checks Account	853,186	—	853,186
Real Estate Guaranty Fund	32,104	—	32,104
Resource Recovery Investment Tax Fund (Act of 1985)	3,534,693	—	3,534,693
Sanitary Landfill Facility Contingency Fund	2,251,521	—	2,251,521
Solid Waste Services Tax Fund (Act of 1985)	919,282	—	919,282
State Disability Benefits Fund	9,221,303	—	9,221,303
State Recycling Fund	1,461,282	—	1,461,282
Unclaimed Personal Property Trust Fund	2,455,978	—	2,455,978
Unemployment Compensation Auxiliary Fund	487,031	—	487,031
Unsatisfied Claim and Judgment Fund	12,164,913	—	12,164,913
Volunteer Emergency Service Organizations Loan Fund	11,235	—	11,235
Worker and Community Right to Know Fund	271,282	—	271,282
Workmen's Compensation Security Fund—Mutual	256,312	—	256,312
Workmen's Compensation Security Fund—Stock	3,642,590	—	3,642,590
	<u>59,906,962</u>	<u>—</u>	<u>59,906,962</u>
<b>TEMPORARY RESERVE GROUP</b>			
Alcohol Education Rehabilitation and Enforcement Fund	1,021,034	—	1,021,034
Beaches and Harbors Fund (Act of 1977)	101,783	—	101,783
Capital City Redevelopment Loan and Grant Fund	259,048	—	259,048
Clean Waters Fund (Act of 1976)	468,520	—	468,520
Community Development Bond Fund (Act of 1981)	344,902	—	344,902
Correctional Facilities Construction Fund (Act of 1982)	296,744	—	296,744
Correctional Facilities Construction Fund (Act of 1987)	4,207,060	—	4,207,060
Emergency Flood Control Fund (Act of 1978)	309,649	—	309,649
Energy Conservation Fund (Act of 1980)	1,185,456	—	1,185,456
Farmland Preservation Fund (Act of 1981)	178,746	—	178,746
Farmland Preservation Fund (Act of 1989)	987,721	—	987,721
General Investment Fund	32,433,426	136	32,433,562
General Trust Fund	826	—	826
Green Acres Cultural Centers and Historic Preservation Bond Fund (Act of 1987)	2,780,827	—	2,780,827
Green Trust Fund (Act of 1983)	1,005,568	—	1,005,568
Hazardous Discharge Fund (Act of 1981)	2,432,623	—	2,432,623
Hazardous Discharge Site Cleanup Fund (Act of 1985)	999,664	—	999,664



**SUMMARY OF INVESTMENT INCOME BY FUND—(CONTINUED)**  
**Year Ended June 30, 1992**

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
<b>TEMPORARY RESERVE GROUP—(continued)</b>			
Higher Education Buildings Construction Fund (Act of 1971)	\$ 24,931	—	\$ 24,931
Housing Assistance Fund (Act of 1968)	29,497	—	29,497
Human Services Facilities Construction Fund (Act of 1984)	360,422	—	360,422
Institutional Construction Fund (Act of 1978)	9,987	—	9,987
Institutions Construction Fund (Act of 1976)	6,211	—	6,211
Jobs, Education and Competitiveness Fund (Act of 1988)	6,966,326	—	6,966,326
Jobs, Science and Technology Fund (Act of 1984)	373,506	—	373,506
Medical Education Facilities Fund (Act of 1977)	28,843	—	28,843
Mortgage Assistance Fund (Act of 1976)	165,148	—	165,148
Natural Resources Fund (Act of 1980)	763,003	—	763,003
New Home Warranty Security Fund	4,035,164	—	4,035,164
New Jersey Bridge Rehabilitation Fund (Act of 1983)	1,360,283	—	1,360,283
New Jersey Bridge Rehabilitation and Improvement and Railroad Right-of-Way Preservation Fund (Act of 1989)	1,709,122	—	1,709,122
New Jersey Green Acres Fund (Act of 1983)	882,084	—	882,084
New Jersey Green Acres Fund (Act of 1989)	1,817,016	—	1,817,016
New Jersey Green Trust Fund (Act of 1989)	1,320,190	—	1,320,190
New Jersey Local Development Financing Fund	75,738	—	75,738
New Jersey Medical Malpractice Reinsurance Recovery Fund	332,018	—	332,018
New Jersey State Dental Program	507,011	—	507,011
Pension Adjustment Fund	311,390	—	311,390
Pension Payroll Investment Fund	352,563	—	352,563
Pinelands Infrastructure Trust Fund (Act of 1985)	602,408	—	602,408
Pollution Prevention Fund	3,232	—	3,232
Prescription Drug Program Fund	215,105	—	215,105
Public Buildings and Construction Fund (Act of 1968)	45,176	—	45,176
Public Purpose Buildings and Community-Based Facilities Construction Fund (Act of 1989)	2,262,347	—	2,262,347
Public Purpose Buildings and Construction Fund (Act of 1980)	658,793	—	658,793
Resource Recovery and Solid Waste Disposal Facilities Fund (Act of 1985)	1,297,044	—	1,297,044
Safe Drinking Water Fund	506,828	—	506,828
Shore Protection Fund (Act of 1983)	371,774	—	371,774
State Facilities for Handicapped Fund (Act of 1973)	118,316	—	118,316
State Health Benefits Fund	10,222,627	—	10,222,627
State Land Acquisition and Development Fund (Act of 1978)	323,422	—	323,422
State Lottery Fund—Investment	2,183,731	—	2,183,731
State of New Jersey—Alternate Benefits Program	842,147	—	842,147
State of New Jersey Cash Management Fund— Administrative Expense Fund	54,503	—	54,503
State of New Jersey Cash Management Fund— Other than State Funds	145,009,906	—	145,009,906
State of New Jersey Cash Management Fund— Reserve Fund	931,768	—	931,768
State Recreation and Conservation Land Acquisition Development Fund (Act of 1974)	182,324	—	182,324
State Recreation and Conservation Land Acquisition Fund (Act of 1971)	295,896	—	295,896
State Transportation Fund (Act of 1968)	27,728	—	27,728
State Water Development Fund (Act of 1958)	3,380	—	3,380
Stormwater Management and Combined Sewer Overflow Abatement Fund (Act of 1989)	832,468	—	832,468
Transportation Rehabilitation and Improvement Fund (Act of 1979)	1,078,462	—	1,078,462
University of Medicine and Dentistry of New Jersey—Self-Insurance Reserves Fund	1,545,970	—	1,545,970
Urban Development Investment Fund (Act of 1985)	81,981	—	81,981
Veterans' Guaranteed Loan Fund	833	—	833
Water Conservation Fund (Act of 1969)	206,942	—	206,942
Water Supply Fund (Act of 1981)	3,353,624	—	3,353,624
Water Supply Replacement Trust Fund	258,972	—	258,972
	243,961,757	136	243,961,893



**SUMMARY OF INVESTMENT INCOME BY FUND—(CONCLUDED)**  
**Year Ended June 30, 1992**

	Net Investment Earnings— Note 1	Net Gain— Notes 1 and 2	Total Investment Income
<b>TRUST GROUP</b>			
New Jersey State Employees' Deferred Compensation Administrative Charges	\$ 33,942	—	\$ 33,942
New Jersey State Employees' Deferred Compensation Cash Management Fund	4,234,292	—	4,234,292
New Jersey State Employees' Deferred Compensation Equity Fund	2,183,876	\$ 1,742,349	3,926,225
New Jersey State Employees' Deferred Compensation Fixed Income Fund	3,256,349	1,415,437	4,671,786
New Jersey State Employees' Deferred Compensation Holding Account	170,250	—	170,250
Supplemental Annuity Collective Trust Fund	4,560,483	6,791,030	11,351,513
Tischler Memorial Fund	43,147	—	43,147
	<u>14,482,339</u>	<u>9,948,816</u>	<u>24,431,155</u>
<b>TOTALS</b>	<u>\$2,065,124,474</u>	<u>\$100,425,300</u>	<u>\$2,165,549,774</u>

See notes to investment summaries.



# SUMMARY OF INVESTMENTS BY MAJOR CATEGORY

## June 30, 1992

	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	\$304,248,000	\$ 302,474,365	\$ 314,654,719	\$ 12,180,354
Industrial bonds and commercial paper	6,711,000	6,711,969	6,938,585	226,616
Telephone bonds	14,924,000	14,915,715	14,595,730	(319,985)
Gas, electric and water bonds	52,026,500	52,043,414	51,907,834	(135,580)
Common stocks	161,079,218	161,079,218	215,954,756	54,875,538
Mortgage-backed certificates	3,649,668,042	3,553,712,055	3,790,985,374	237,273,319
Units—Common Pension Fund A	10,280,343,509	10,280,343,509	16,410,652,521	6,130,309,012
Units—Common Pension Fund B	9,919,330,037	9,919,330,037	10,662,808,211	743,478,174
Units—Common Pension Fund D	1,200,013,854	1,200,013,854	1,354,383,785	154,369,931
Units—Cash Management Fund	7,489,705,893	7,489,705,893	7,489,705,893	—
Other investments	784,000	778,854	829,770	50,916
<b>TOTAL INVESTMENTS BY MAJOR CATEGORY</b>		<u><u>\$32,981,108,883</u></u>	<u><u>\$40,313,417,178</u></u>	<u><u>\$7,332,308,295</u></u>

See notes to investment summaries.



# SUMMARY OF INVESTMENT ACTIVITY

## Year Ended June 30, 1992

Purchases at cost, excluding common funds:		
Bonds	\$569,369,103	
Mortgages	1,524,874,041	
Stocks	<u>81,758,703</u>	\$ 2,176,001,847
Purchases of units of common funds, at cost		32,067,848,282
Discount accretion		18,241,428
Sales, at amortized cost		(1,838,597,848)
Mortgage principal payments, at amortized cost		(575,437,466)
Redemptions, at amortized cost		(44,301,378)
Maturities, at par amount		(129,314,400)
Redemptions of units of common funds		(28,617,047,193)
Premium amortization		<u>(212,675)</u>
NET INCREASE IN AMORTIZED COST OF INVESTMENTS		3,057,180,597
Total amounts invested by funds—Note 2		
Beginning of year		<u>29,923,928,286</u>
END OF YEAR		<u>\$32,981,108,883</u>

See 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.

**Amortized Cost**

Investments are stated in the Division's records at cost which includes any commissions, as adjusted for the accretion of discount or amortization of premium. State of New Jersey Cash Management Fund units are stated at a cost of \$1.00 per unit, which approximates market value.

Par, cost or principal amount and market are presented in the summaries for informational purposes. Market values of common stock 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 common stock 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. Bonds and mortgage-backed certificates are valued in accordance with fair market procedures established by the State Investment Council primarily through valuations obtained from 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.

**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 Common Pension Fund A and the State of New Jersey Cash Management Fund. No gains were distributed from Common Pension Fund B or Common Pension Fund D in fiscal year 1992.

**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, 1992. 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, 1992, all investments held by the Division are classified as Category 1.

Federal securities, including federal securities held as collateral on repurchase agreements, 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) through the custodian banks in trust for the State of New Jersey. Investment securities denominated in a foreign currency are maintained by the United Kingdom Central Gilts Office (CGO), Euroclear, and the Cedel book entry system 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.

Securities not maintained by the Federal Reserve Banks, DTC, CGO, Euroclear or Cedel 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 \$91,991,714 in fiscal year 1992, 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 \$6,046,182 in fiscal year 1992 are not reflected in the Summary of Investment Income by Fund. Undistributed interest income of \$87,884,183 as of June 30, 1992, arising from investment activity by Common Pension Fund D is not reflected in the Summary of Investment Income by Fund.



## 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, 1992 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	\$12,918,515,000	\$12,884,662,256	\$13,490,064,895	\$ 605,402,639
Industrial bonds and commercial paper	3,358,030,655	3,351,140,138	3,405,403,884	54,263,746
Foreign government bonds and notes	991,079,611	991,079,611	1,050,839,180	59,759,569
Foreign stock	44,537,258	44,537,258	44,186,446	(350,812)
Telephone bonds	265,206,000	251,485,296	265,639,000	14,153,704
Gas, electric and water bonds	673,892,500	642,409,621	677,680,341	35,270,720
Finance companies—senior debt	21,000,000	20,790,102	20,907,750	117,648
Common stocks	10,439,733,673	10,439,733,673	16,551,002,454	6,111,268,781
Mortgage-backed certificates	3,649,668,042	3,553,712,055	3,790,985,374	237,273,319
Time certificates of deposit	985,000,000	985,000,000	985,000,000	—
Other investments	183,322,000	183,675,619	196,421,975	12,746,356
Total investments		33,348,225,629	40,478,131,299	7,129,905,670
Differences in accounting by unit funds:				
Other assets		786,254,602	786,254,602	—
Other liabilities		(937,483,773)	(942,552,757)	(5,068,984)
Undistributed realized gains and other income		(209,978,655)	—	209,978,655
Other accounting practices		(5,908,920)	(8,415,966)	(2,507,046)
Total amounts invested by funds		<u>\$32,981,108,883</u>	<u>\$40,313,417,178</u>	<u>\$7,332,308,295</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, 1992. 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. Fiscal 1991 net realized gains of Common Pension Fund A were distributed in fiscal 1992. 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—SOUTH AFRICAN DIVESTITURE

By act of the New Jersey State Legislature (P.L. 1985, c.308), the Division of Investment is prohibited from holding securities of companies with a presence in the Republic of South Africa for any pension or annuity fund it manages. Under the current Attorney General's ruling, the Division is allowed three years from the date of determination of South African status to effect divestment. At June 30, 1992, the Division held no securities of companies with a presence in the Republic of South Africa.

### NOTE 5—COMMITMENTS

As of June 30, 1992, Common Pension Fund D had entered into the following forward foreign currency exchange contracts as hedges of its investments:

Contract To Deliver	In Exchange For	Settlement Date	Net Unrealized Appreciation (Depreciation)
DM 200,000,000	\$120,062,432	8/18/92	\$(10,103,530)
DM 100,000,000	60,099,766	8/18/92	(4,983,214)
\$185,162,326	DM 300,000,000	8/18/92	10,086,616
			<u>\$ (5,000,128)</u>

### NOTE 6—SUBSEQUENT EVENT

On July 7, 1992, the State of New Jersey appropriately transferred \$780,000,000 from the pension and annuity group to the General Investment Fund as mandated by Public Law 1992, Chapter 41. This transfer did not have a significant impact on the Division of Investment's operations.

# APPENDIX I

## UNAUDITED SUMMARY OF INVESTMENTS BY MAJOR CATEGORY OF INDIVIDUAL PENSION FUNDS, 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
<b>SHORT-TERM OBLIGATIONS</b>						
U.S. Government and other government securities and obligations	\$10,010	\$10,029	\$1,925	\$1,929	\$ 89,702	\$ 89,873
Commercial paper	5,677	5,677	1,092	1,092	50,874	50,875
Time certificates of deposit	2,561	2,561	492	492	22,950	22,951
	<u>18,248</u>	<u>18,267</u>	<u>3,509</u>	<u>3,513</u>	<u>163,526</u>	<u>163,699</u>
<b>LONG-TERM BONDS</b>						
U.S. Government bonds and other government securities and obligations	27,177	28,516	36,271	38,983	1,520,032	1,633,427
Industrial bonds	—	—	2,840	2,962	118,569	123,641
Gas and electric bonds	600	588	2,775	2,941	121,545	128,423
Telephone bonds	—	—	1,112	1,180	48,376	51,171
Finance companies—senior debt	3	3	94	94	3,906	3,929
Intermediate term corporate notes	498	500	1,811	1,941	76,077	81,493
Foreign Government bonds and notes	—	—	3,072	3,258	162,339	172,127
Other	—	—	1,247	1,325	60,107	63,883
	<u>28,278</u>	<u>29,607</u>	<u>49,222</u>	<u>52,684</u>	<u>2,110,951</u>	<u>2,258,094</u>
<b>MORTGAGES</b>						
Mortgage-backed certificates	<u>8,263</u>	<u>8,568</u>	<u>8,261</u>	<u>8,568</u>	<u>727,655</u>	<u>776,131</u>
<b>STOCK</b>						
Common stock (U.S.)	—	—	37,003	58,806	1,992,004	3,165,732
Common stock (Foreign)	—	—	138	137	7,295	7,238
	<u>—</u>	<u>—</u>	<u>37,141</u>	<u>58,943</u>	<u>1,999,299</u>	<u>3,172,970</u>
	54,789	56,442	98,133	123,708	5,001,431	6,370,894
Difference due to accounting practices	(736)	(759)	2,867	2,026	51,004	100,633
	<u>\$54,053</u>	<u>\$55,683</u>	<u>\$101,000</u>	<u>\$125,734</u>	<u>\$5,052,435</u>	<u>\$6,471,527</u>



**INCLUDING INVESTMENTS OWNED BY THE COMMON PENSION FUNDS AND THE STATE OF NEW JERSEY  
(000's Omitted) at June 30, 1992**

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
\$385	\$386	\$ 195,958	\$ 196,333	\$ 9,625	\$ 9,643	\$ 243,696	\$ 244,163	\$ 551,301	\$ 552,356
218	218	111,137	111,139	5,459	5,459	138,212	138,214	312,669	312,674
99	99	50,136	50,136	2,462	2,462	62,350	62,350	141,050	141,051
702	703	357,231	357,608	17,546	17,564	444,258	444,727	1,005,020	1,006,081
98	98	2,760,766	2,966,099	210,258	225,991	3,239,597	3,480,306	7,794,199	8,373,420
—	—	214,718	223,902	16,438	17,141	252,076	262,844	604,641	630,490
—	—	219,145	231,672	16,158	17,121	278,399	293,009	638,622	673,754
—	—	89,073	94,121	6,722	7,109	106,202	112,058	251,485	265,639
—	—	7,082	7,123	541	544	8,307	8,356	19,933	20,049
19	19	139,438	149,251	10,407	11,157	164,188	175,697	392,438	420,058
—	—	331,913	351,926	30,624	32,471	463,132	491,057	991,080	1,050,839
—	—	116,553	123,955	9,540	10,152	150,554	160,305	338,001	359,620
117	117	3,878,688	4,148,049	300,688	321,686	4,662,455	4,983,632	11,030,399	11,793,869
—	—	1,269,413	1,353,464	36,023	38,041	1,500,193	1,602,261	3,549,808	3,787,033
—	—	3,649,950	5,800,575	228,186	362,638	4,371,512	6,947,296	10,278,655	16,335,047
—	—	14,916	14,798	1,376	1,366	20,812	20,648	44,537	44,187
—	—	3,664,866	5,815,373	229,562	364,004	4,392,324	6,967,944	10,323,192	16,379,234
819	820	9,170,198	11,674,494	583,819	741,295	10,999,230	13,998,564	25,908,419	32,966,217
14	13	72,975	184,081	12,047	15,600	176,007	222,537	314,178	524,131
<u>\$833</u>	<u>\$833</u>	<u>\$9,243,173</u>	<u>\$11,858,575</u>	<u>\$595,866</u>	<u>\$756,895</u>	<u>\$11,175,237</u>	<u>\$14,221,101</u>	<u>\$26,222,597</u>	<u>\$33,490,348</u>

# APPENDIX II

## UNAUDITED COMMON PERFORMANCE DISCLOSURE FORM FOR PUBLIC FUNDS

	Avg. Annual Return 5 Years Ended 6/30/92	One Year Period Ended				
		6/30/88	6/30/89	6/30/90	6/30/91	6/30/92
<b>TOTAL RETURN</b>						
Aggregate of All Pension Funds	10.1%	(0.7)%	14.5%	13.3%	10.0%	13.8%
Consumer Price Index	4.3%	4.0%	5.2%	4.7%	4.7%	3.0%
<b>EQUITY TOTAL RETURNS</b>						
Common Pension Fund A Equities	8.6%	(10.5)%	16.9%	18.6%	8.1%	12.7%
Approved List—Before Divestment	10.4%	(8.1)%	20.1%	17.3%	8.6%	13.3%
Approved List—South Africa Free	9.2%	(7.0)%	18.7%	14.0%	7.6%	14.5%
Dow Jones Industrial Average	10.5%	(8.3)%	18.7%	22.8%	4.7%	17.7%
Standard & Poor's 500 Index	9.8%	(6.9)%	20.5%	16.5%	7.4%	13.4%
Standard & Poor's Mid Cap	12.9%	(2.3)%	22.1%	15.4%	12.8%	18.6%
<b>FIXED INCOME TOTAL RETURNS</b>						
Common Pension Fund B and Other Bonds	10.5%	7.4%	13.0%	7.2%	10.3%	14.7%
Shearson Lehman Government/Corporate Bond Index	10.2%	7.5%	12.3%	7.1%	10.2%	14.2%
Salomon Brothers High Grade Bond Index (AA and AAA)	11.6%	8.5%	16.2%	6.0%	10.6%	16.8%
Salomon Brothers Broad Bond Index	10.6%	8.1%	12.2%	7.7%	10.8%	14.2%
<b>MORTGAGES—TOTAL RETURNS</b>						
Pension fund holdings	11.5%	9.4%	12.1%	9.2%	12.0%	15.8%
Salomon Brothers Mortgage Index	10.6%	9.7%	11.8%	9.7%	12.0%	14.0%
<b>INTERNATIONAL TOTAL RETURNS</b>						
Common Fund D Total	—	—	—	—	—	22.3%
Common Fund D Fixed Income	—	—	—	—	—	23.4%
Common Fund D Equities	—	—	—	—	—	NM
Salomon World Gov. Bonds Index—Unhedged	10.2%	9.7%	4.3%	7.0%	10.0%	20.5%
EAFE Stock Index	0.7%	4.1%	9.5%	3.3%	(11.5)%	(0.7)%
<b>CASH EQUIVALENTS</b>						
Total Returns—Cash Management Fund	7.5%	7.2%	8.4%	8.9%	7.9%	5.5%
91-Day Treasury Bills	6.5%	5.5%	7.8%	7.9%	6.8%	4.7%

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.





In March 1992, Andrei Gromov, Dimitry Cherneiko and Svetlana Kolupaeva, representing the City of St. Petersburg, Russia, visited the Division to review benefit and investment policies.







