
ALASKA PERMANENT FUND Corporation

**1981 Annual Report
And Financial Statements**

ALASKA PERMANENT FUND Corporation

Members of the Board of Trustees

Elmer E. Rasmuson, Chairman
Thomas K. Williams, Vice-Chairman
Peter B. McDowell, Secretary
Wilson L. Condon
Robert W. Ward
George W. Rogers

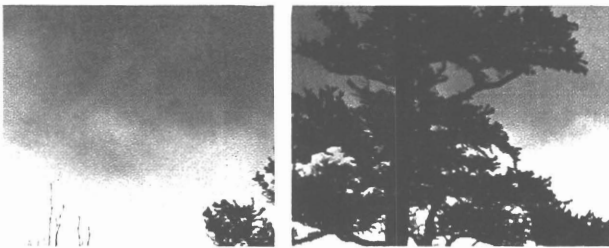
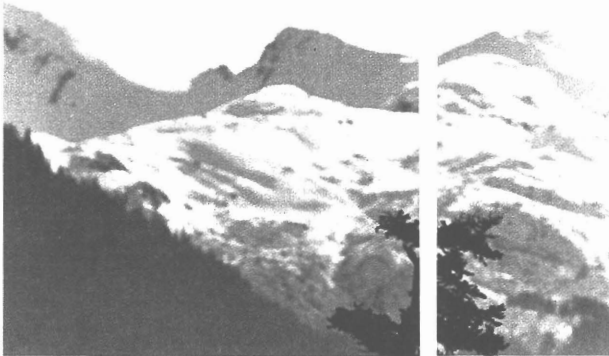
Acting Executive Director

Peter Bushre, Treasurer

Contact Address

Alaska Permanent Fund Corporation
Pouch SB
Juneau, Alaska 99811

Telephones: Juneau, (907) 465-2350
Anchorage, (907) 277-1496





Elmer Rasmuson
Chairman of the Trustees

ALASKA PERMANENT FUND CORPORATION

POUCH SB - JUNEAU, ALASKA 99811
TELEPHONE 907-465-2351

BOARD OF TRUSTEES:

ELMER E. RASMUSON - CHAIRMAN
THOMAS K. WILLIAMS - VICE-CHAIRMAN
WILSON L. CONDON
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RESPONDENT ADDRESS:

September 30, 1981

“Shaping the Future of the Permanent Fund”

In the fall of 1976, the people of Alaska made the first great change in their fiscal affairs, creating the Permanent Fund. This set aside 25% of the oil royalties and related income of the State (about 11% of all oil receipts) and the Legislature can set aside more from year to year, as it added \$900 million in 1980 and \$1.8 billion in 1981.

In truth, the Permanent Fund began chiefly with a “negative” goal, to place a part of the one-time oil wealth beyond the reach of day-to-day government spending. During these past five years, Alaskans have taken up the work of defining the “positive” goals of the Permanent Fund. The first results of that effort were in 1980, prescribing the independent management of the Fund and setting out a cautious list of investments and providing dividends for the public from the earnings of the Fund. This effort of defining positive goals continues.

For our part, we, your trustees, are convening a series of seminars to explore the possible futures of the Permanent Fund and the best ways to attain them. Meeting jointly with a select legislative delegation, we have asked the counsel of economists and other financial specialists, of major Alaskan interests, and of the general public.

We have been guided by the conviction that shaping the future of the Permanent Fund must be done in the light of **all** the oil revenues. Otherwise, there is the danger the Permanent Fund will duplicate or work against other State actions instead of complement them. Accordingly, we have brought into one public forum the issues that surround budget growth, the loan and capital programs, the equity of how the oil money is being divided—and the Permanent Fund. This is described in this Annual Report.

We are in the midst of preparing recommendations for the opening of the next legislative session. Already, I believe, there is a growing sense of which questions are the key ones: What is the fundamental purpose of the Fund (high quality savings, some kind of development program, or both if they are not in conflict); given a fundamental purpose, what is the proper size of the Fund and what adjustments in the management structure and the list of authorized investments may be necessary, especially to protect the income and capital of the Fund from surging inflation; how much income could be used for what purposes and with how much equity?

The Permanent Fund is unique in being created by the people themselves and not only for the present generation. Shaping its future is not to be done by your Trustees alone or by any one group. We ask for the help of all our fellow Alaskans.

Sincerely,



Elmer Rasmuson
Chairman of the Trustees

THE YEAR IN REVIEW

Actions of the Trustees

The six Trustees appointed as the first board of the newly created Alaska Permanent Fund Corporation were faced with a series of critical decisions in several areas: (1) organization and management; (2) establishment of investment guidelines; (3) review of the current provisions of law; and (4) examination of issues crucial to the future of the Fund.

Organization and Management

Under the provisions of the Permanent Fund Act, the Trustees were given the freedom to elect all officers of the board and to reevaluate those decisions on an annual basis. At their first annual meeting, the Trustees elected Elmer Rasmuson as Chairman, Thomas Williams as Vice-Chairman, and Deputy Commissioner of Revenue Peter Bushre, who had been chosen Acting Executive Director, as Secretary-Treasurer. The Chairman and Vice-Chairman were reelected at the second annual meeting, with Peter McDowell elected Secretary and Mr. Bushre as Treasurer.

Among other management decisions during the first year were the selection of Attorney General Wilson Condon as general counsel, the appointment of the Department of Revenue as agent for the corporation to continue managing the Fund at the Trustees' direction, taking formal action to transfer the Permanent Fund to the Alaska Permanent Fund Corporation by the end of calendar year 1980, selecting Price Waterhouse & Co. as the Fund's auditors, selecting Trustees' staff, and making decisions regarding the development of a separate entity for management of the Fund.

A paper on organization and management by Trustee Peter McDowell served as a focus in the Trustees' discussion of moving to separate or "independent" status as provided for by law. There was a consensus among the Trustees in examining the legislative history that although they were not legally bound to develop a separate corporate entity, there existed a public and legislative preference for their doing so. The Chairman appointed a subcommittee to identify the factors involved in implementing this intent, to develop a time line for effecting the move and to determine staffing requirements.

Investments

The Permanent Fund Act provides what is generally considered a very narrow range of permissible investments. Faced with an unpredictable and wildly fluctuating money market, the Trustees have followed a conservative investment strategy, directing the Fund managers in the Department of Revenue to emphasize short term money market instruments in the Permanent Fund's portfolio. Initial direction to the managers was to consider four years as the outer perimeter of acceptable investment with greater emphasis to be placed on two year maturities. As the year continued, the Trustees urged progressively shorter maturities, so that by the end of the fiscal year, the average weighted life of marketable securities in the Fund was one year one month. Since June 30, 1981, all marketable investments in the Fund have been limited to maturities of three months and shorter duration.

The Trustees adopted a plan to place 5% of the Fund in in-state federally guaranteed mortgages for owner-occupied one-to-four unit dwellings. A plan to place 5% of the Fund in in-state banks in the form of time certificates of deposit with maturities established in one year increments, funds to be rebid at maturity, was also adopted.

Review of Current Provisions

Early in the year, in a paper entitled "Thoughts of the Chairman", Mr. Rasmuson observed that the narrow range of allowable investments in the current law prevents the Trustees from providing an effective hedge against inflation. He called for consideration of modifications in the Fund legislation to allow investments which would offset inflation, and he also identified the need to coordinate any examination of the Fund, which automatically receives only about 11% of the state's oil wealth, with plans for the remaining 90% of the revenues. This approach was endorsed by the Trustees, who further agreed that the task of shaping the Fund must be a continuing process and that if the Fund is to have a stabilizing role in the Alaskan economy, any changes must be made with careful deliberation.

Subsequently, a special legislative panel was appointed to work with the Trustees. Appointments were made both by Senator Sturgulewski, Chairwoman of the Legislative Budget and Audit Committee, which has statutory oversight responsibility for the Permanent Fund, and by the presiding officers of the Legislature. A series of seminar/work sessions was scheduled and the Trustees and legislators are meeting regularly to examine the issues and discuss recommendations.

Examination of Issues

A consensus has emerged as to the questions which must be addressed and on which recommendations ought to be made.

Assuming the fundamental role of the Fund to be provision of high quality savings, with both present and future residents enjoying the income, is there also a possible development role and is that role desirable? What are the risks of concentrating investments within a single state? Is the present investment list adequate and, if not, would it be prudent to diversify into other asset classes such as equities, real estate or foreign assets? What are similar institutions doing in this regard? Given the fact that the principal and income of the Fund will be eroded by inflation, should some provision be made to pay out only "real" or inflation-adjusted income rather than all income? Should an objective rate of return over the rate of inflation be set as an overall performance measurement goal (i.e., 2% over the rate of inflation)? What management changes may be needed (such as composition of the board, size of internal staff)? What legal constraints must be considered in making recommendations? And, finally, what is the proper size of the Fund? This last question turns on how the income may be used. Several proposals for the use of income have been advanced; distribution to residents, covering some part of future state budgets, and endowing central programs in the budget, such as education, housing, or local grants, are some of the possibilities.

Guest speakers of national repute have been featured at the series of seminars. Broad questions of state spending and distribution of oil wealth were dealt with by Professor Don Gordon of City University of New York, Katherine Peden, a private industrial development consultant, Nobel laureate Kenneth Arrow from Stanford, Professor Maxwell Fry of University of California at Irvine, and Professor Richard Coffman of University of Idaho. George Russell of the Frank Russell Company, Robert Greeley, manager of corporate investments at Hewlett Packard, and Sam Nakagama of Kidder, Peabody & Co., specifically addressed investment strategy.

To obtain more detailed information on investment and management questions, representatives of the Permanent Fund, Treasury Division, the Legislative Budget and Audit Committee and the Attorney General's office had a series of meetings with prominent New York financial houses; reports were filed upon their return.

Meetings and Information

Four regular meetings and two special meetings were held during fiscal year 1981 and two meetings have been held thus far in fiscal year 1982. Dates and places are noted below. Summary minutes are available for all meetings. In addition, a compilation of papers presented by guest speakers, together with an executive summary, will be made available to the Legislature in January. Copies of that report will be furnished upon request to any interested groups or individuals.

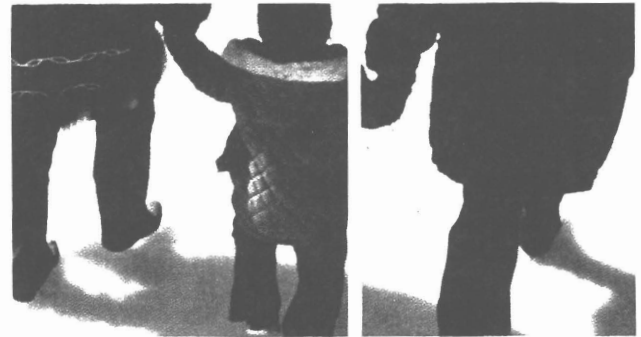
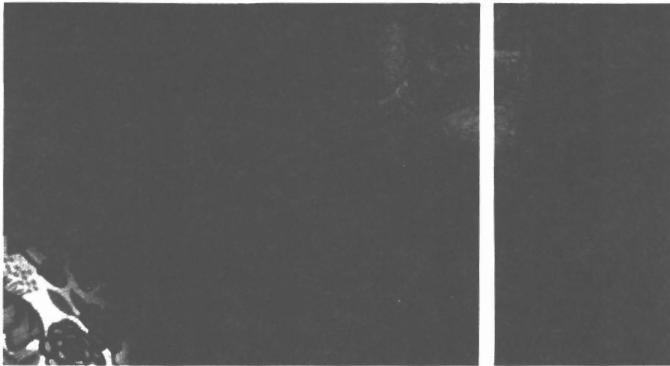
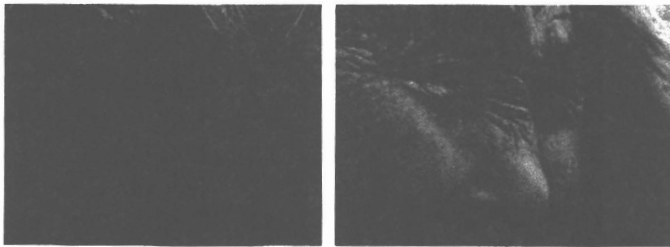
Regular Meetings

September 12, 1980 — Juneau
November 21, 1980 — Juneau
March 20, 1981 — Juneau
June 30, 1981 — Anchorage
September 10 & 11, 1981 — Juneau

Special Meetings

January 9, 1981 — Juneau
May 8, 1981 — Juneau
August 20, 1981 — Fairbanks

Future meetings are scheduled for October 22 and 23 in Anchorage, December 3 in Juneau, and at a date uncertain in January in Juneau. The public is always encouraged to attend meetings and is given an opportunity to address agenda items.



FUND PERFORMANCE DURING FY 1981

(July 1, 1980—June 30, 1981)

Investment Strategy

Fiscal year 1981 was a period characterized by extreme volatility in financial and capital markets. As measured by the accepted bond indices, the first and third quarters of calendar year 1980 were the worst two in fifty years, while the second quarter was the best ever recorded. Declining interest rates in the second quarter encouraged both consumers and corporate borrowers to resume their earlier spending patterns. As a result the economy experienced the shortest recession on record—three months—and then bounced back to produce extraordinary growth in early 1981 before weakening in the second quarter of 1981. While inflation has abated recently, there is nothing substantive to indicate that this improvement is anything more than a temporary phenomenon. Wage demands continue strong and there has been no improvement in productivity.

Fund investments during FY 81 were concentrated in two year and shorter maturities, with investments in progressively shorter maturities as the year advanced and the economic climate remained unpredictable. By mid-June, 90.7% of the Fund portfolio matured within two years, 66.9% within one year, and 49.8% within six months. On June 30, 1981, the average weighted life of marketable securities was one year one month as compared to three years one month on the same date in 1980.

Performance Versus Goals

AS 37.13.170 requires that the annual report include a comparison of corporation performance with the goals outlined in AS 37.13.020. These goals are: (1) conservation of a portion of the state's mineral resource revenues to benefit all generations of Alaskans; (2) maintain safety of principal while maximizing total return; (3) management of Fund as a savings device to allow maximum use of disposable income for purposes defined by law.

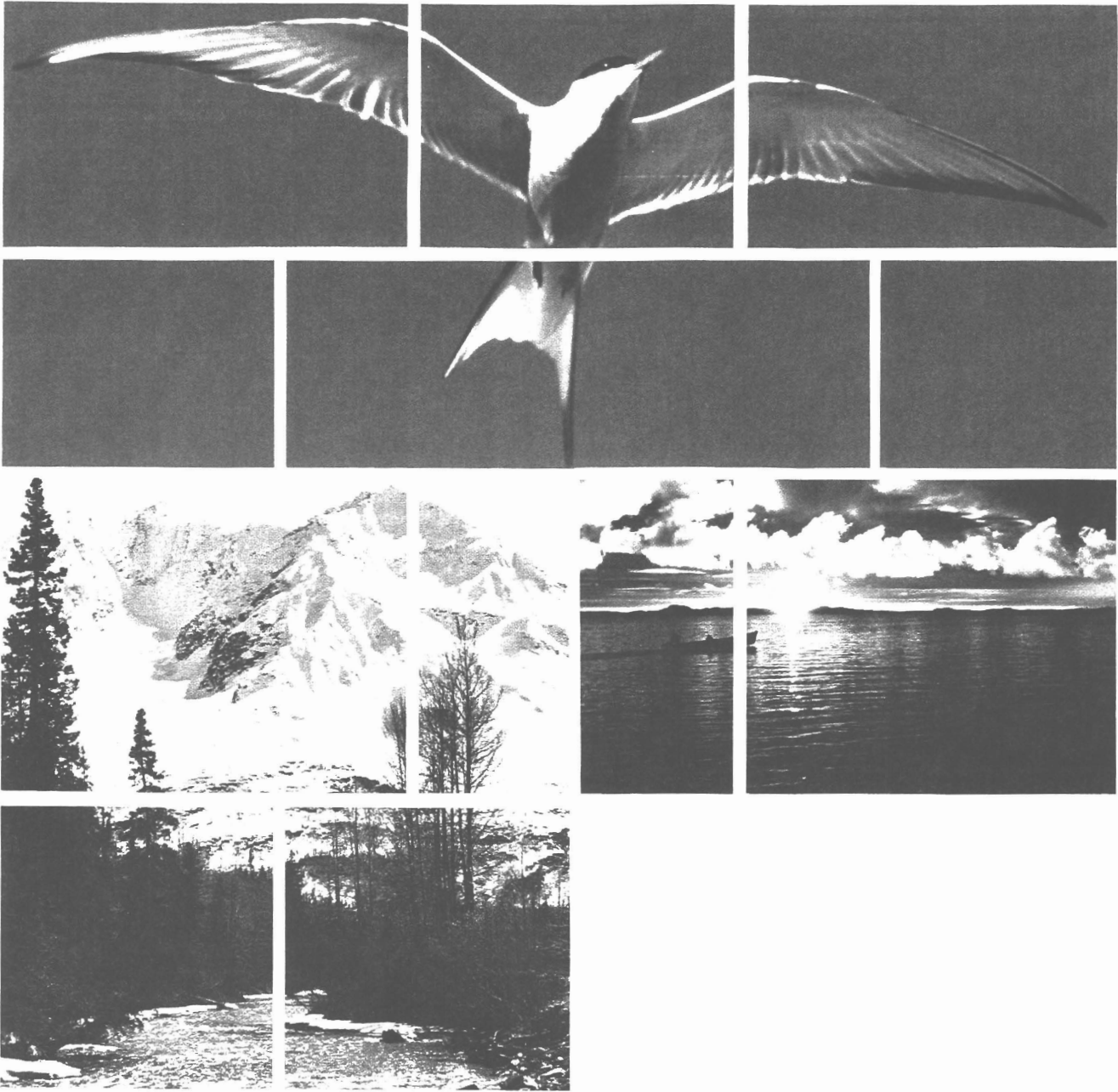
Through the regular contributions required by the constitutional amendment and by the Permanent Fund Act, plus the special appropriation of \$900 million made during the 1980 legislative session, the Permanent Fund grew from \$483,208,000 on June 30, 1980, to \$1,827,299,000 on June 30, 1981.

The realized rate of return on Fund investments has climbed steadily and was 16.0% as of June 30, 1981. The net realized gain on transactions retained in the Fund's principal during fiscal year 1981 is \$219,388. All principal contributions have been retained in the Fund's balance, and disbursement of income earned has been limited to cash amounts received.

The Permanent Fund Dividend Plan is the only provision currently in law for the use of disposable income. According to the constitutional amendment which created the Permanent Fund, all disposable income of the Fund is transferred to the General Fund and is available for expenditure by the Legislature, unless otherwise provided by law. The statutory provision for payment of dividends in proportion to duration of Alaska residence has been challenged. The Alaska Supreme Court decision upholding the dividend distribution plan is presently under review by the U.S. Supreme Court; a decision is expected sometime in early 1982.

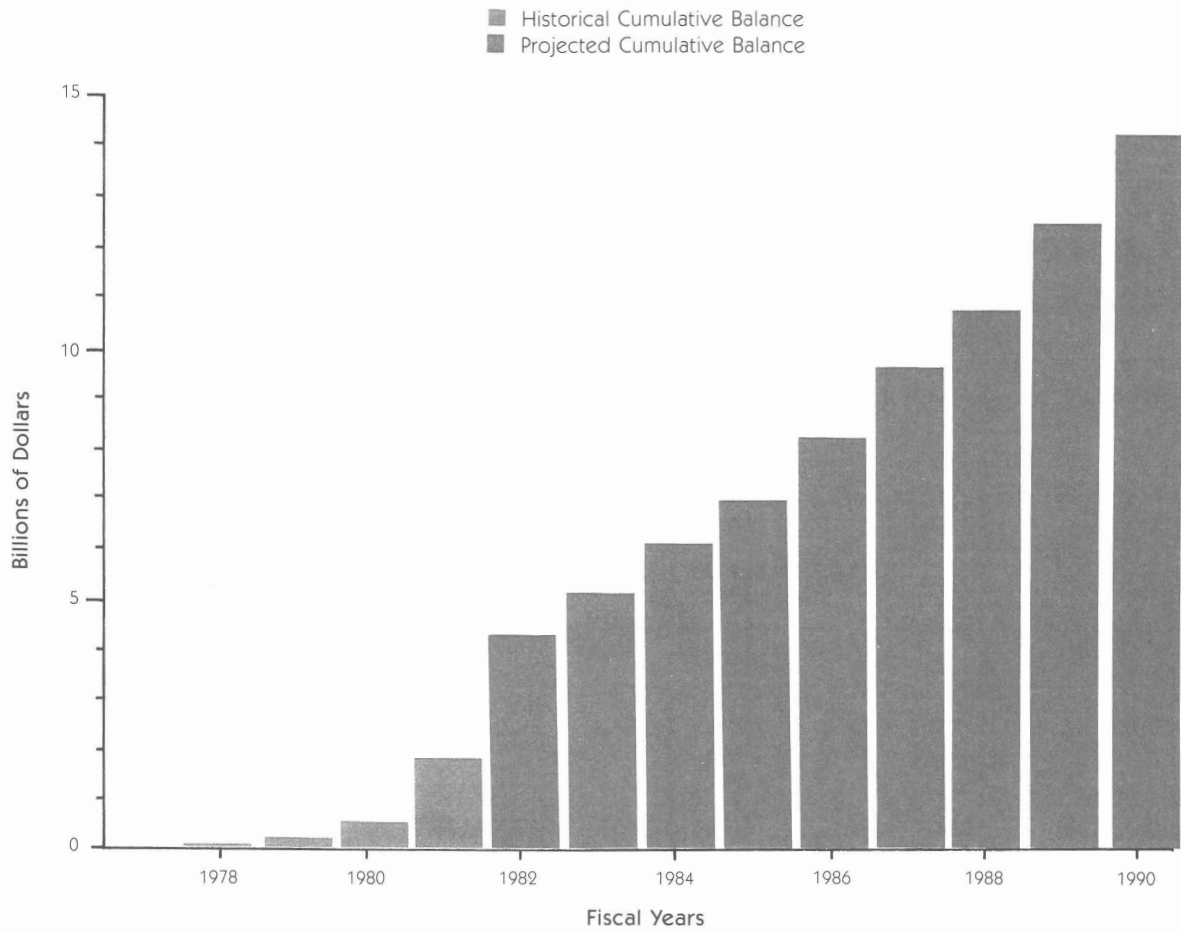
Audit

The Fund was audited by Price Waterhouse & Co., independent public accountants, for the 1981 fiscal year. The auditors expressed an unqualified opinion as to Statements of Net Assets, Investment Income and Changes in Net Assets.



OUTLOOK FOR FISCAL YEAR 1982

Cumulative Balances



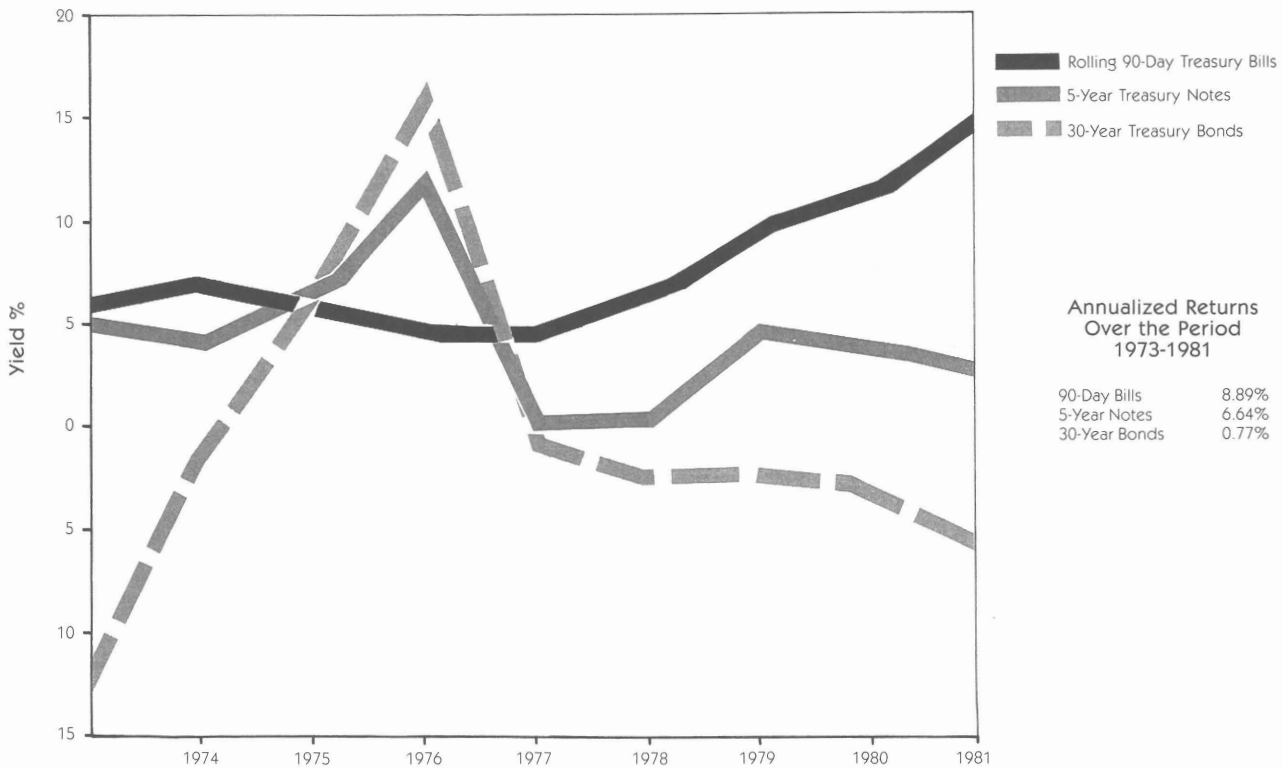
Fund Balance

During the 1981 legislative session, a special appropriation of \$1.8 billion was made to the Permanent Fund under the provisions of Chapter 61, Session Laws of Alaska 1981. With the addition of that amount plus regular contributions, the Fund is projected to be \$4,273,900,000 on June 30, 1982.

Economic Outlook and Investment Strategy

The central concern in the development of any coherent investment strategy is the willingness of the U.S. government to come to grips with inflation and the nature of policies proposed to bring it under control. The Administration's budget cutting and tax cut victories along with its defense program have raised a number of significant concerns within the investment community. There is a growing realization that the U.S. Treasury and federal agencies will continue to make heavy demands on the credit markets for the remainder of this year and 1982. The Treasury's early estimate of \$42.5 billion deficit for federal fiscal year 1982 is proving to be unrealistic, and a number of private analysts are projecting a deficit in the \$70 to \$80 billion range. The Administration is currently searching for new areas to cut spending, but any search will likely involve some extremely difficult political struggles.

Fixed Income Total Returns
(Revised Sept. 1981)



Alaska Permanent Fund

Realized rates of return, income, and portfolio balances
for the fiscal years ended June 30, 1981, 1980, 1979, & 1978

	Fiscal Year 1981	Fiscal Year 1980	Fiscal Year 1979	Fiscal Year 1978
Realized rates of return (based on accrued income)	16.00%	11.29%	8.24%	7.53%
Investment income (including amounts earned but not rec'd. by year end)	\$ 149,867,000	\$ 32,426,923	\$ 7,967,131	\$ 1,791,000
Case earnings received transferred to general fund	\$ 54,931,481	\$ 23,675,560	\$ 5,702,926	\$ 900,434
Average portfolio balance	\$ 936,243,000	\$287,255,000	\$ 96,700,000	\$ 23,800,000
Marketable securities on June 30, at cost	\$1,846,491,000	\$493,427,071	\$137,783,958	\$ 54,387,000
Marketable securities on June 30, at market	\$1,795,730,000	\$493,444,000	\$136,140,000	\$ 52,300,000

There appears to be a growing perception in the financial markets that a strict monetarist monetary policy and supply-side oriented fiscal policy are not entirely mutually compatible. Those advocating most strongly the supply side fiscal policy are already beginning to contend that high interest rates are suppressing economic growth, pushing the federal budget further out of balance and jeopardizing the tax cut's chance of success. The Federal Reserve Bank, on the other hand, is undoubtedly concerned that a significant easing in interest rates would start another inflationary surge in pent up consumer demand for housing and automobiles. These concerns are also no doubt compounded by fears that this surge could be reinforced by the administration's three year tax cut and a planned surge in defense spending. Fixed income investors seem to sense that eventually one philosophy will have to be deemphasized.

Given the volatility of the economy and interest rates, a conservative investment strategy emphasizing short term investments appears best suited to providing high rates of return while at the same time minimizing the risks of capital depreciation. Until such time as fiscal and monetary policies are brought into a more harmonious relationship, interest rates are likely to remain highly volatile.

ALASKA PERMANENT FUND Corporation
Financial Statements
June 30, 1981



101 WEST BENSON BOULEVARD
ANCHORAGE, ALASKA 99503
907-279-1424

August 13, 1981

To the Board of Trustees
Alaska Permanent Fund Corporation

In our opinion, the accompanying statements of net assets, of investment income and of changes in net assets present fairly the financial position of the Alaska Permanent Fund Corporation at June 30, 1981 and its investment income and changes in net assets for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances, including at June 30, 1981 confirmation of securities owned by correspondence with the custodians. The financial statements of the Alaska Permanent Fund Corporation for the year ended June 30, 1980 were examined by other independent accountants, whose report dated August 29, 1980 expressed an unqualified opinion on those statements.

A handwritten signature in cursive script that reads "Price Waterhouse & Co." with a small flourish at the end.

Price Waterhouse & Co.

ALASKA PERMANENT FUND Corporation

Statement of Net Assets

	June 30	
	1981	1980
Cash in Savings Account	\$ 43,000	\$ 39,000
Contributions receivable from the State General Fund	92,000	34,000
Interest Receivable	26,925,000	9,377,000
Loans and Mortgages	1,086,000	
Investment Securities, at cost		
U.S. Treasury notes and bonds	670,771,000	303,964,000
Bankers acceptances	537,715,000	23,510,000
U.S. Treasury bills	466,615,000	20,583,000
Certificates of deposit	137,600,000	111,879,000
Corporate bonds	13,487,000	13,487,000
Federal agency notes	13,004,000	13,004,000
Securities purchased under agreements to resell	7,300,000	7,000,000
	<u>1,846,492,000</u>	<u>493,427,000</u>
Amounts due to the State General Fund	<u>(47,339,000)</u>	<u>(19,669,000)</u>
Net Assets	\$1,827,299,000	\$483,208,000

See accompanying notes to financial statements

ALASKA PERMANENT FUND Corporation

Statement of Changes in Net Assets

	Year Ended June 30	
	1981	1980
Assets Were Provided By:		
Investment income	\$ 149,867,000	\$ 32,427,000
Contribution from the State of Alaska General Fund	900,000,000	
Royalties and other State receipts	385,128,000	344,396,000
	1,434,995,000	376,823,000
Total assets provided		
Transfers of investment income to State of Alaska General Fund	(90,904,000)	(32,161,000)
Increase in net assets	\$1,344,091,000	\$344,662,000
Increase (Decrease) in Components of Net Assets:		
Cash in savings account	\$ 4,000	\$ 8,000
Contributions receivable	58,000	(205,000)
Interest receivable	17,548,000	5,936,000
Loans and mortgages	1,086,000	
U.S. Treasury notes and bonds	366,807,000	231,530,000
Certificates of deposit	25,721,000	106,865,000
Bankers acceptances	514,205,000	(4,843,000)
U.S. Treasury bills	446,032,000	20,583,000
Federal agency notes and bonds		5,008,000
Securities purchased under agreements to resell	300,000	6,500,000
Commercial paper		(10,000,000)
Amounts due to the State General Fund	(27,670,000)	(17,720,000)
	\$1,344,091,000	\$344,662,000

See accompanying notes to financial statements

ALASKA PERMANENT FUND Corporation

Statement of Investment Income

	Year Ended June 30	
	1981	1980
Interest Income:		
U.S. Treasury notes and bonds	\$ 61,279,000	\$13,060,000
U.S. Treasury bills	32,229,000	808,000
Bankers acceptances	28,115,000	5,251,000
Certificates of deposit	22,636,000	10,130,000
Securities purchased under agreements to resell	1,950,000	306,000
Corporate bonds	1,140,000	1,140,000
Federal Agency notes and bonds	1,082,000	1,069,000
Commercial paper	1,062,000	387,000
Other interest income	120,000	
Savings account	35,000	10,000
	<hr/>	<hr/>
	149,648,000	32,161,000
Net securities gains	219,000	266,000
	<hr/>	<hr/>
Investment income	\$149,867,000	\$32,427,000

See accompanying notes to financial statements

ALASKA PERMANENT FUND Corporation

Notes to Financial Statements

Note 1 — Authorization

The State of Alaska Constitution was amended by voter approval in 1976 to provide for the segregation of certain mineral lease rentals, bonuses, royalties, royalty sale proceeds and federal mineral revenue sharing payments received by the State for the use and benefit of present and future residents.

Distributable income from the Corporation is defined by statute and further clarified by administrative regulation to be the lesser of the latest fiscal year's income or the average annual current income calculated using a simple average of the last five years or the number of years in existence if less than five after adjustment for capital gains and losses.

All of the Corporation's investment securities are held by a commercial lending institution pursuant to a custodial agreement, except for certain certificates of deposit purchased from Alaska banks.

Note 2 — Summary of Significant Accounting Policies:

The accounting and reporting policies of the Alaska Permanent Fund Corporation conform to generally accepted accounting principles. The more significant accounting policies are as follows:

Interest Income

Interest income on loans is accrued monthly as earned.

Interest income on investments is shown net of amortization of premium and accretion of discount.

Investment Securities

Investment securities are carried at cost adjusted for amortization of premium and accretion of discount. Investment securities are expected to be held to maturity and, therefore, will be fully realized.

Gains or losses on the sale of securities are determined on a specific identification basis.

Provision for Loan Losses

The provision for loan losses is determined from specific evaluation of delinquencies and would be charged directly to operations in the period that the loss exposure becomes known. At June 30, 1981 no provision has been made since no losses are presently anticipated.

Note 3 — Marketable Securities:

The cost and estimated market value of investment securities at June 30, were as follows:

	1981		1980	
	Cost	Market	Cost	Market
U.S. Treasury notes & bonds	\$ 670,771,000	\$ 633,501,000	\$303,964,000	\$304,967,000
Bankers acceptances	537,715,000	536,411,000	23,510,000	23,692,000
U.S. Treasury bills	466,615,000	464,330,000	20,583,000	20,924,000
Certificates of deposit	137,600,000	134,120,000	111,879,000	113,899,000
Corporate bonds	13,487,000	8,135,000	13,487,000	10,753,000
Federal Agency notes	13,004,000	10,642,000	13,004,000	12,209,000
Securities purchased under agreements to resell	7,300,000	7,300,000	7,000,000	7,000,000
	\$1,846,492,000	\$1,794,439,000	\$493,427,000	\$493,444,000

Note 4 — General Fund Contribution:

For the year ended June 30, 1981, the State of Alaska Legislature appropriated \$900,000,000 to the Corporation from the General Fund. For the year ended June 30, 1982, the Legislature appropriated an additional \$1,800,000,000 to the Corporation from the General Fund of which at least \$1,400,000,000 is to be contributed prior to June 30, 1982.

Note 5 — Administrative Expenses (Unaudited):

Administrative and other expenses are paid by the State of Alaska General Fund and are not included in the accompanying statements. The related budget and actual expenses for 1981 and budgeted expenses only for 1982 for operations of the Permanent Fund Corporation are as follows (unaudited):

	1981		1982
Budget		Actual	Budget
\$206,800		\$165,000	\$450,500

Photographs courtesy of the Division of Economic Enterprises
Department of Commerce and Economic Development.

Legislative Committee of Oversight

Legislative Budget and Audit Committee
Senator Arliss Sturgulewski, Chairwoman

Special Legislative Liaison Committee

Senator Arliss Sturgulewski, Chairwoman
Senator Patrick Rodey
Senator Vic Fischer
Senator Bob Mulcahy
Senator Ed Dankworth
Representative Al Adams
Representative Hugh Malone
Representative Bob Bettisworth
Representative Oral Freeman
Representative Sam Cotten
Representative Ernie Haugen