

SB

51

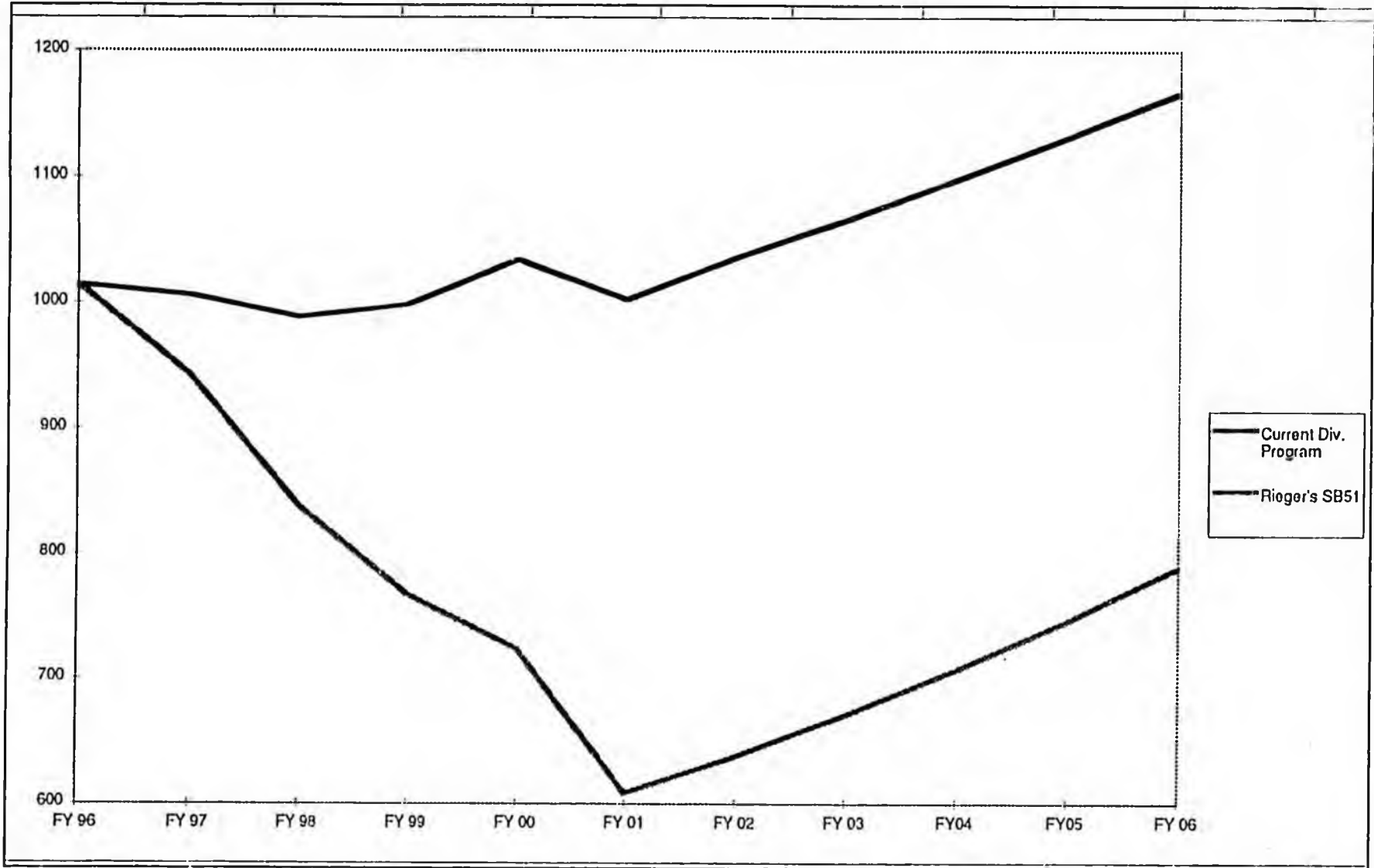
SFIN

FILE

5FC-96

5FC-96
3/29/96
R.H.
Cully

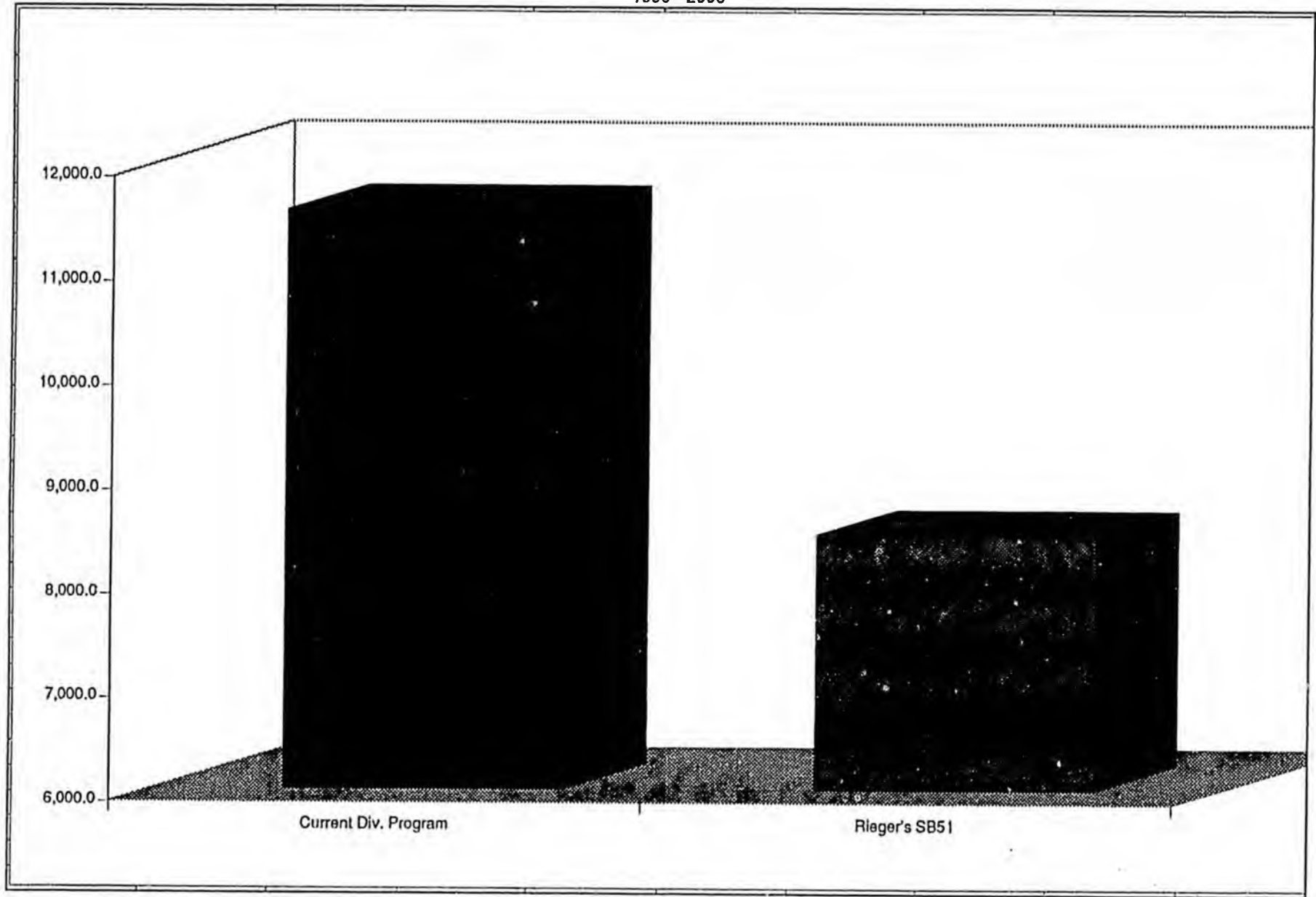
Real 1996 Dollars



Attachment A

Total Permanent
Fund Dividends
1996 - 2006

JFC-96
3/29/96
RH
(14114)





Post-it® Fax Note 7671 Date 3/28 # of pages 1

To *Bertin* From *J. Kelly*

Co/Dept. *Mr. Reizus Jr.* Co. *AKC*

Phone # _____ Phone # *465-2059*

Fax # *465-2069* Fax # *465-1473*

3/29/96
SR

Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS
(in millions)

as of December 31, 1995

GROWTH OF FUND PRINCIPAL						
FY	FY Begin Balance	Appropriations	Dedicated State Revenue ⁽¹⁾	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
78						
79						
80	4,838	2,700	2,424	817	5,741	
81	5,741		323	216	6,281	
82	6,281	1,264 ⁽²⁾	170	148	7,864	
83	7,864		418	303	8,585	
84	8,585		228	380	9,173	
85	9,173		267	454	9,894	
86	9,894		435	559	10,888	
87	10,888		338	477	11,703	
88	11,703	5 ⁽³⁾	315	362	12,385	
89	12,385	6	210	372	12,973	
90	12,973	8	318	348	13,645	
91	13,645	514 ⁽⁴⁾	218	398	14,775	
92	14,775	9	216	448	15,448	
93	15,448	13	217	499	16,176	
94	16,176	14	229	522	16,941	
95	16,941	15	231	547	17,733	
96	17,733	18	233	572	18,554	
97	18,554	17	239	598	19,409	
98	19,409	19	238	625	20,292	
99	20,292	21	237	653	21,203	
00	21,203	22	229	682	22,138	
01	22,138	24	218	712	23,090	
02	23,090	26	209	742	24,007	
03	24,007	28	203	773	25,072	
04	25,072	31	202	805	26,109	
05	26,109	33	198	838	27,178	
06	27,178	38	195	872	28,280	
07	28,280	39	191	907	29,417	
08	29,417	42	184	943	30,586	
09	30,586	46	178	980	31,790	
10	31,790	50	159	1,018	33,026	
Cumulative Totals Projected						
For FY 1996 - 2015: 4,233 14,132						

USE OF FUND INCOME							
Net Income	Distributions			Reserves			FY End Balance
	Inflation-Proofing	Dividends	Per Capita Dividends	General Fund	Add (Delete)	FY End Balance	
78							
79							
80	2,219	617	653	\$404.00	186	763	763
81	1,021	218	303	\$556.26		501	1,264
82	1,069	148	391	\$708.19		529	529
83	789	303	424	\$826.93		82	591
84	868	360	460	\$873.16	4	44	635
85	916	454	487	\$952.63	4	(30)	605
86	1,030	559	488	\$931.34	4	(24)	581
87	1,036	477	488	\$931.34	5	64	645
88	1,226	362	632	\$949.46	5	320	965
89	1,098	372	558	\$983.90	11	151	1,117
90	1,013	348	565	\$990.30	8	86	1,203
91	1,701	388	631	\$1,049.00		658	1,361
92	1,167	448	636	\$1,030.00		374	1,734
93	1,815	499	645	\$1,022.00		659	2,393
94	1,938	522	678	\$1,051.00		723	3,116
95	2,069	547	732	\$1,110.00		775	3,892
96	2,207	572	725	\$1,071.00		894	4,785
97	2,359	696	803	\$1,164.00		840	5,725
98	2,517	825	864	\$1,228.00		1,009	6,734
99	2,583	653	928	\$1,294.00		1,081	7,815
00	2,568	682	988	\$1,320.00		895	8,710
01	2,727	712	1,006	\$1,349.00		985	9,695
02	2,897	742	1,047	\$1,379.00		1,082	10,777
03	3,079	773	1,091	\$1,411.00		1,187	11,964
04	3,272	805	1,137	\$1,445.00		1,299	13,263
05	3,478	838	1,216	\$1,523.00		1,390	14,653
06	3,894	872	1,301	\$1,604.00		1,485	16,139
07	3,922	907	1,381	\$1,689.00		1,585	17,724
08	4,162	943	1,487	\$1,777.00		1,690	19,414
09	4,414	980	1,589	\$1,869.00		1,799	21,213
10	4,678	1,018	1,696	\$1,984.00		1,915	23,127
57,643 14,132 20,571 \$19,436							

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 98:	9.80%	2.77%	7.03%
FY 97: ⁽¹⁾	6.98%	2.99%	3.99%
FY 98 - 2015: ⁽¹⁾	8.42%	3.18%	5.24%

⁽¹⁾ Department of Revenue Fall 1995 Mid-Case Revenue Forecast.

⁽²⁾ Earnings reserve appropriated to principal July 1, 1987 and 1995

⁽³⁾ Transferred to principal from earnings reserve account per AS 37.13.145(d).

⁽⁴⁾ Based on 1995 Callan capital market assumptions.

SENATE BILL NO. 51, ALL SURPLUS EARNINGS IN ERA, AND \$280 OF EXISTING UNREALIZED GAINS REALIZED EACH YEAR FROM 1997-2004

SENATE FINANCE COMMITTEE

SB 51 DISPOSITION OF PERMANENT FUND INCOME

PLEASE SIGN IN BELOW

NAME: Jim Kelly
Co./DEPT./TITLE: Dir of Communications PHONE: _____
ADDRESS: ABFC ZIP: _____
Do you wish to testify? Yes No Respond to questions

NAME: _____
Co./DEPT./TITLE: _____ PHONE: _____
ADDRESS: _____ ZIP: _____
Do you wish to testify? Yes No Respond to questions

NAME: _____
Co./DEPT./TITLE: _____ PHONE: _____
ADDRESS: _____ ZIP: _____
Do you wish to testify? Yes No Respond to questions

NAME: _____
Co./DEPT./TITLE: _____ PHONE: _____
ADDRESS: _____ ZIP: _____
Do you wish to testify? Yes No Respond to questions

Revision Date: _____ Dept. Affected: Revenue
 Title: An Act Relating to Income of the Permanent BRU: APFC
Fund and Providing for an Effective Date. Component: APFC
 Sponsor: Senator Rieger/Pearce
 Requestor: Senate Finance COMPONENT SERIAL NO. 109

Expenditures/Revenues:

(Thousands of Dollars)

OPERATING EXPENDITURES	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
----------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
------------------------	--	--	--	--	--	--

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY96) cost \$ _____

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

No fiscal impact.

Prepared by: Byron I. Mallott, Executive Director
 Division: Alaska Permanent Fund Corporation
 Approved by Commissioner: [Signature]
 Agency: Department of Revenue

Phone: 465-2047
 Date: 3/26/96
 Date: _____

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2/14/95 #1
 (S) STA, FIN

FISCAL NOTE

STATE OF ALASKA
 1995 LEGISLATIVE SESSION

BILL NO. SB 51

Revision Date: _____ Dept. Affected: Revenue
 Title: An Act Relating to Income of the Permanent Fund and Providing for an Effective Date BRU: APFC
 Component: APFC
 Sponsor: Senator Rieger/Pearce
 Requester: (S)STA COMPONENT SERIAL NO. 109

Expenditures/Revenues (Thousands of Dollars)

OPERATING EXPENDITURES	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY95) cost: \$ _____

POSITIONS

FULL-TIME						
PART-TIME						
TEMPORARY						

No fiscal impact.

Prepared by: Martin R. Pihl, Acting Executive Director Phone: 465-2047
 Division: Alaska Permanent Fund Corporation Date: 2/13/95
 Approved by: _____
 Commissioner: Deborah Vogt Date: 2/13/95
 Agency: Revenue

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SB 51

FISCAL NOTE

No. 1

Bill Version: SB 51

STATE OF ALASKA
1995 LEGISLATIVE SESSION

BILL (S) Publish Date: 3/3/95

Revision Date: _____ Dept. Affected: _____ Revenue _____
 Title: An Act Relating to Income of the Permanent Fund and Providing for an Effective Date BRU: APFC
 Component: APFC
 Sponsor: Senator Rieder/Pearce
 Requester: (S)STA COMPONENT SERIAL NO. 109

Expenditures/Revenues (Thousands of Dollars)

OPERATING EXPENDITURES	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
----------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY95) cost: \$ _____

POSITIONS

FULL-TIME						
PART-TIME						
TEMPORARY						

No fiscal impact.

Prepared by: Martin R. Pihl, Acting Executive Director Phone: 465-2047
 Division: Alaska Permanent Fund Corporation Date: 2/13/95
 Approved by: _____
 Commissioner: Deborah Voigt Date: 2/13/95
 Agency: Revenue

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Alaska State Senate

SENATOR STEVE RIEGER
District I

Senate Finance Committee
Chair, Senate Transportation Committee

Legislative Budget and Audit Committee
Administrative Regulation Review Committee
Legislative Council



During Session:
State Capitol, Room 516
Juneau, Alaska 99801
(907) 465-3879

716 West 4th Avenue, Suite 530
Anchorage, Alaska 99501
(907) 258-8185

Information on SB 51 – Relating to income of the permanent fund

- **Sponsor Statement** by Senator Steve Rieger
- **Editorial** – "Real Dollars Now Means Real Dividends Later" by Tim Bradner, *Anchorage Daily News*, January 8, 1995
- **Trustee's Position on SB 51** – Alaska Permanent Fund Corporation
- **Alaska Population Projections**, March 1992
- **Report by Ibbotson Associates, Inc.** – Asset Allocation Study for the Alaska Permanent Fund
- **Executive Summary** – Knowles/Ulmer Policy Transition Teams' Report, January 1995

Alaska State Senate

SENATOR STEVE RIEGER
District 1

Senate Finance Committee
Chair, Senate Transportation Committee

Legislative Budget and Audit Committee
Administrative Regulation Review Committee
Legislative Council

During Session:
State Capitol, Room 516
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(907) 465-3879

716 West 4th Avenue, Suite 530
Anchorage, Alaska 99501
(907) 258-8188

Sponsor Statement

SB 51 – An Act relating to the income of the Permanent Fund

Senate Bill 51 places into statute the concept of "real earnings" and applies that concept to the provisions for the uses of Permanent Fund earnings.

Concept of Real Earnings

There are several ways in which income of a fund can be calculated. When all cash receipts are counted without regard to the effects of inflation, the earnings are often referred to as "*nominal earnings*." In contrast, "*real earnings*" are the amount by which nominal earnings exceed inflation.

For any long-term preservation of a fund, and particularly in times of any significant inflation, the concept of real earnings is extremely important to the management of an endowment fund. Any endowment which is designed to last for a sustained period of time must be concerned about its purchasing power and earning power. Inflation tends to erode a fund; to offset this a fund must grow (in nominal terms) at the same rate as inflation just to preserve its purchasing or earning power. In this context, a fund can afford only to pay out earnings which are in excess of the rate of inflation – real earnings.

Appropriateness for the Permanent Fund

I believe that voters, in establishing the Permanent Fund, intended for the Fund to be truly permanent in the sense that its purchasing power and earning power should not be eroded over time. In this context, a real earnings approach is most appropriate for the Permanent Fund. The only money which should be put on the table for use each year is real earnings.

SB 51 - An Act relating to the income of the Permanent Fund
Sponsor Statement
Page Two

In contrast, under present statutes all of the *nominal* earnings are put on the table for appropriation each year. The Legislature then allocates the earnings to dividends, inflation-proofing, and the earnings reserve account. With SB 51, the inflation-proofing would be automatic and the Legislature would provide for the allocation of real earnings between the dividends and the earnings reserve account.

Effect on Permanent Fund Earnings Reserve

Since there would be no further need to reserve earnings for inflation-proofing, the required size of the Permanent Fund Earnings Reserve (PFER) is not as great. There would, however, be a reason to retain some amount in the PFER to cover 5-year averaging provisions, such as the rule on dividends, regardless of whether the real earnings concept is used. SB 51 is silent on the issue of the PFER and does not require any change from present PFER policy.

Effect on Dividends

The bill leaves untouched the underlying formula for calculation of dividends. This formula prescribes a payment of approximately half of earnings. However, since the earnings on which dividends are based are real earnings rather than nominal earnings, the underlying formula will indicate a slower rate of long-term growth in dividends, and could indicate a temporary drop in the amount transferred to the dividend fund, depending on the Permanent Fund's actual performance in the next few years.

It should be pointed out that the amount actually transferred to pay dividends each year has been made by legislative appropriation. Even with SB 51, the legislature maintains its ability to appropriate an amount different from that prescribed by the underlying formula. The legislature may choose to pay an amount higher than the formula indicates, but SB 51 is designed to deter appropriations greater than the fund's *total* real earnings performance.

Other Changes

One additional change, although minor, is that the effect of inflation on the fund will be calculated using the average annual balance of the Fund, rather than the Permanent Fund's present practice of using the balance as of the end of the year.

Summary

The overall effect of SB 51 will be that the Permanent Fund will be made more **permanent**, because the question of inflation-proofing will be removed from the annual process of allocating earnings. Earnings will be more realistic, as they are reflective of the actual economic earnings of the Fund. However, the effect of converting to a real earnings basis for the annual allocation process will also lower the amount put on the table for appropriation each year. The result of passing SB 51 will be better protection for the Fund, and a better representation to the State of the maximum amount which properly could be used each year.



TIM BRADNER

Real dollars now means real dividends later

One of the most sensible public policy proposals I've heard recently is state Sen. Steve Rieger's idea for requiring the Alaska Permanent Fund to report its annual profits in real, or inflation-adjusted, dollars, rather than the nominal, or inflation-eroded dollars, as is now the practice.

The idea has merit not only because it is sound from a financial point of view — most big endowment funds look at their earnings this way — but it solves some problems in the way the fund must manage its income.

In effect, Rieger's plan would change the procedure the legislature set up more than a decade ago when it passed the law setting out how fund profits are to be used in paying the annual permanent fund dividend to Alaskans and making payments into the corpus of the fund to offset inflation.

The direction legislators gave was for the fund to pay dividends first and inflation-proofing second. Over time, this could cause a shortfall in the amount of profits available for inflation-proofing.

BRADNER: Accounting in real dollars makes sense

Continued from Page C-1

Under the current formulas, which pay dividends first, there may not be enough to pay both dividends and inflation-proofing. Latest estimates by the Permanent Fund Corp. are that the shortfall will start about 2000, and eventually will reach hundreds of millions of dollars yearly.

Either inflation proofing will be shorted by this amount, or money to inflation proof will have to be taken from the permanent fund earnings reserve, the account of accumulated profits not used for dividends or inflation proofing. That reserve now totals about \$1.2 billion. In the meantime the state may want these reserves for public services. The legislature may, in fact, take them.

Allowing inflation to erode the fund to sustain

the growth of the dividend is shortsighted. If we solve the problem now we could not only sustain dividends for our children and grandchildren, but also help pay for public services and keep their taxes low.

In effect, Rieger's plan would reverse the priority of paying dividends first and for inflation second. By reporting the fund's profits in real, inflation-adjusted dollars, the "inflation-proofing" automatically occurs first. The dividend will be paid on the basis of inflation-adjusted earnings. Rieger argues this is the way to really protect the permanent fund for future generations and I agree with him.

A second attraction the Anchorage Republican's idea has is that it would make room, after a few years, for the permanent fund to make a substantial amount of money available

for the general state treasury, helping narrow the fiscal gap.

This happens because when the fund manages itself on real instead of nominal dollars, there not only will be enough money for dividends but some left over for the general treasury to help keep taxes low when oil revenue declines. This won't eliminate the need for budget cuts, but it make cuts more manageable without major tax increases.

Obviously this extra money has to come from somewhere. It comes, in fact, from dividends that might not grow as fast as they will under the current formula. Dividends could even dip for a short time before starting to grow again. The legislature could choose to avoid this dip by using some money from the earnings reserve to support the dividend.

What I really like about

this is that it's a far better way to put the dividend on a more rational base, and to have the permanent fund make more of a contribution toward covering the fiscal gap, than other proposals on the table like capping the dividend at present levels or even rolling it back.

Rieger's plan will be more easily accepted by the public. The amount of money for dividends still grows, although more slowly. More important, the fund is effectively protected against inflation, which means those dividends really will be there, as the politicians like to say, for future generations.

|| Tim Bradner writes for an Alaska economic reporting service. His private clients include petroleum companies. His opinion column appears every fourth Sunday.

Anchorage Daily News 1/8/95



RECEIVED FEB 28 1995

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

MEMORANDUM

DATE: February 27, 1995

TO: Senator Steve Rieger

FROM: Byron I. Mallott *Byron I. Mallott*
Executive Director

SUBJECT: Trustees' Position on SB 51

This is to inform you that the Board of Trustees did discuss Senate Bill No. 51 at their meeting on February 24. They stated that they did not intend to take a position on the bill itself, but that they were supportive of any changes to existing law which would enhance their ability to protect the principal of the Permanent Fund. Certainly, that portion of SB 51 which makes inflation-proofing the highest priority use would be such a change.

There is another portion of the bill which would change the dividend formula by basing it on "real" income rather than "net" income. That proposal falls outside the scope of what previous boards -- as well as the current board -- view as their area of responsibility.

I would request that the Board be given the opportunity to comment again at a later date if the bill undergoes any substantive changes as it moves through the legislative process.

As always, the staff of the Corporation would be pleased to respond to any requests for financial analysis of any legislative proposal relating to the Permanent Fund.

c: Board of Trustees
Pat Pourchot, Governor's Legislative Director
Jim Kelly, Research & Liaison Officer

ALASKA
POPULATION PROJECTIONS

1990 - 2010

State of Alaska

Walter J. Hickel, Governor

Department of Labor

Nancy Bear Usera, Commissioner

Administrative Services Division

David Teal, Director

**Research and Analysis
Chuck Caldwell, Chief**

Prepared by Demographics Unit

**Gregory Williams, State Demographer
Bob Elliott, Economist
Kristen Tromble, Statistical Technician**

Publications Unit

**J. Penelope Goforth, Editor
Jim Fowler, Graphic Artist
In Ruby, Typesetter**

**November 1991
Second Printing March 1992**

Table F.
Annual Projections and Components Of Change
For the Total Population of Alaska, 1990-2010.

Part A. Middle Series

Calendar Year	Population change July 1 to July 1							
	↓ July 1 Population	Net Change	Natural increase	Births	Deaths	Net Migration	In	Out
1990	553,600	—	—	—	—	—	—	—
1991	574,000	20,400	9,654	11,826	2,172	10,746	57,654	46,908
1992	593,100	19,100	10,017	12,283	2,266	9,083	57,720	48,637
1993	607,500	14,400	10,320	12,676	2,356	4,080	54,733	50,653
1994	622,300	14,800	10,506	12,942	2,436	4,294	56,174	51,880
1995	637,300	15,000	10,690	13,204	2,514	4,310	57,451	53,141
1996	652,500	15,200	10,849	13,437	2,588	4,351	58,769	54,418
1997	668,000	15,500	11,004	13,678	2,674	4,496	60,207	55,711
1998	683,900	15,900	11,194	13,949	2,755	4,706	61,737	57,031
1999	700,000	16,100	11,398	14,241	2,843	4,702	63,088	58,386
2000	716,500	16,500	11,608	14,545	2,937	4,892	64,650	59,758
2001	732,800	16,300	11,853	14,878	3,025	4,447	65,613	51,166
2002	749,000	16,200	12,092	15,217	3,125	4,108	66,664	62,556
2003	764,900	15,900	12,333	15,551	3,218	3,567	67,505	63,938
2004	780,700	15,800	12,572	15,878	3,306	3,228	68,522	65,294
2005	796,200	15,500	12,775	16,182	3,407	2,725	69,365	66,640
2006	811,400	15,200	12,968	16,477	3,509	2,232	70,193	67,961
2007	826,200	14,800	13,169	16,770	3,601	1,631	70,887	69,256
2008	840,700	14,500	13,331	17,034	3,703	1,169	71,685	70,516
2009	854,700	14,000	13,476	17,268	3,792	524	72,274	71,750
2010	868,300	13,600	13,593	17,474	3,881	7	72,947	72,940

Calendar Year	Rate per 100 mid year population (%)							
	July 1 Population	Average Annual Change	Natural Increase	Births	Deaths	Net Migration	In	Out
1990	553,600	—	—	—	—	—	—	—
1991	574,000	3.62	1.68	2.06	0.38	1.87	10.04	8.17
1992	593,100	3.27	1.69	2.07	0.38	1.53	9.73	8.20
1993	607,500	2.40	1.70	2.09	0.39	0.67	9.01	8.34
1994	622,300	2.41	1.69	2.08	0.39	0.69	9.03	8.34
1995	637,300	2.38	1.68	2.07	0.39	0.68	9.01	8.34
1996	652,500	2.36	1.66	2.06	0.40	0.67	9.01	8.34
1997	668,000	2.35	1.65	2.05	0.40	0.67	9.01	8.34
1998	683,900	2.35	1.64	2.04	0.40	0.69	9.03	8.34
1999	700,000	2.33	1.63	2.03	0.41	0.67	9.01	8.34
2000	716,500	2.33	1.62	2.03	0.41	0.68	9.02	8.34
2001	732,800	2.25	1.62	2.03	0.41	0.61	8.95	8.35
2002	749,000	2.19	1.61	2.03	0.42	0.55	8.90	8.35
2003	764,900	2.10	1.61	2.03	0.42	0.47	8.83	8.36
2004	780,700	2.04	1.61	2.03	0.42	0.41	8.78	8.36
2005	796,200	1.97	1.60	2.03	0.43	0.34	8.71	8.37
2006	811,400	1.89	1.60	2.03	0.43	0.28	8.65	8.38
2007	826,200	1.81	1.59	2.03	0.44	0.20	8.58	8.38
2008	840,700	1.74	1.59	2.03	0.44	0.14	8.53	8.39
2009	854,700	1.65	1.58	2.02	0.44	0.06	8.46	8.39
2010	868,300	1.58	1.57	2.01	0.45	0.00	8.40	8.40

Source: Alaska Department of Labor, Research & Analysis, Demographics Unit



Alaska Permanent Fund Corporation

P.O. Box 25500 Juneau, Alaska 99802-5500

(907) 465-2047

January 13, 1994

Senator Randy Phillips
Legislative Budget & Audit Committee, Chairman
State Capitol Building, Room 103
Juneau, AK 99801-1182

Dear Senator Phillips:

Thank you for providing us with Ibbotson's report on the asset allocation of the Alaska Permanent Fund Corporation (APFC). We are pleased to provide this initial response to the report. Communication on this issue will continue as the board commences its annual review of APFC's asset allocation at the February 3 meeting in Juneau.

Since April 1993, the APFC has been involved with a significant portfolio restructuring program under the direction of the Board of Trustees. Upon completion, the APFC will place significantly less emphasis on passive investment and more on active management of the equity securities portfolio. This program has been undertaken with our investment consultant, Callan Associates, Inc. (Callan), providing recommendations and advice at each step of the program. Once completed, a number of the issues mentioned in the Ibbotson Associates Asset Allocation study will have been addressed.

After reading the Ibbotson report, Callan made the following observations:

1. Recent performance has been good because the board and staff have done a good job of adopting sound strategic allocation policies and employing good managers.
2. Movement toward current strategic targets at an accelerated pace may be particularly important since much of the strong performance over the past several years is attributable to extraordinary bond returns which are unlikely to continue given the current low level of interest rates. Obviously, we all agree with this

assessment and you, through significant funding of global portfolios in recent months, have already essentially reached the strategic target allocations.

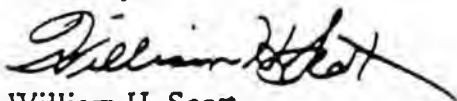
3. Diversification within the domestic equity portfolio could be improved with a greater commitment to the small and mid-cap sector. Callan shares this view and your staff recognizes the under-representation in this area and plans to address it through the hiring of two small/mid-cap domestic equity managers in the first half of 1994.
4. Diversification within the fixed-income portfolio could be improved with explicit allocations to major segments such as mortgages. As discussed at length at our recent meeting, the effects of statutory limitations on fixed-income management must be carefully considered. The use of derivative securities, lower-rated bonds and non-US\$ denominated bonds are all influenced by current (statutory) restrictions. In addition, managing liquidity to meet annual dividend requirements is increasingly affecting the fixed-income portfolio. Nonetheless, broader diversification of the fixed-income effort warrants further discussion and already has been scheduled for the upcoming board meeting. As an aside, I was pleased to see that Ibbotson recognized the fee savings and good performance that has been achieved to date. It also is important to note that at least over the past several years an allocation to mortgages would have hindered performance.
5. Ibbotson's expected equity returns are extraordinarily high relative to the firm's expected bond returns. While I sincerely hope that they are correct, the very large premiums and the high absolute levels may result in an underestimation of near-term risk associated with more aggressive strategies. Relatedly, we, staff and the board have all acknowledged that heavier equity commitment would result in greater expected returns over the long run but we all also recognize that shorter-term consistency in returns is particularly important to the Fund since the annual dividend is potentially at issue. Finally, it is important to note that the "aggressive" alternative suggested results in full utilization of the statutory equity maximum of 50%.
6. Ibbotson very clearly advises that the board control asset allocation at a more micro level than it has in the past. Specially, the study advises that the board set specific allocations within the fixed-income and domestic equity areas and make extensive use of specialists in the international area. The directions suggested are contrary to the board's movement toward providing less restrictive guidelines to its managers, particularly the global managers. I think that this is an important issue that already has been discussed at length during 1993 and warrants continued close monitoring

and review as we gain experience with the current structure. My current view is that the board's basic asset allocation plan, while theoretically vulnerable to the actions of the managers, will not be adversely affected. Each manager has indicated that it is highly unlikely that they would make sudden dramatic shifts from domestic to international portfolios. We, therefore, will be able to identify any potential problem before it undermines the program. You are continuing to use some specialists internationally and are planning to add specialists in domestic mid-cap securities. In sum, Ibbotson's management structure comments are important and I agree that the structure, particularly the domestic structure, should be on the board's agenda for 1994.


The staff of the APFC agree with Callan's remarks. Should the Legislative Budget & Audit Committee (LB&A) like to discuss in greater detail these conclusions, we recommend that myself and a representative of Callan Associates, Inc. be invited to appear before the Committee. The APFC would be pleased to make the necessary arrangements.

We would like to express our appreciation for LB&A's efforts and those of Ibbotson in conducting this review. It is always helpful to receive more than one independent view of this most important subject of asset allocation. In addition, we would be pleased to have Ibbotson present their report to the Board of Trustees at its meeting on February 3, 1994 at the APFC offices in Juneau.

Sincerely,



William H. Scott
Executive Director



ASSET ALLOCATION STUDY
FOR
THE ALASKA PERMANENT FUND

Prepared by Ibbotson Associates, Inc.
January, 1994




Summary of Recommendations

Currently, the Alaska Permanent Fund is a well diversified portfolio that has enjoyed tremendous success in recent years. This success is mainly due to the Board's knowledge of the importance of asset allocation and its commitment to diversification. This has resulted in the Fund earning high rates of return at relatively conservative levels of risk. The Fund is well positioned to reap the benefits of diversification, having made investments in many different asset classes, both domestic and international. Also, the Fund appears to be efficiently managed, employing reputable and capable managers for both its equity and fixed income assets. The Fund has been able to manage its substantial fixed income portfolio entirely in-house, keeping administrative costs and outside management fees to a minimum. Several important issues must be addressed, however, in order to ensure the Fund's continued success.

Our analysis suggests the Permanent Fund should alter its asset allocation policy in order for the Fund to enjoy returns similar to those it has earned in recent years. Specifically, the Board should consider the following actions:

- ▶ Revise its current three-year target asset mix to include a larger allocation to domestic mid and small capitalization equities, European, Pacific Rim and emerging market equities, and mortgage-backed securities.
- ▶ Adopt a more aggressive investment style by allocating a larger percentage of Fund assets to equity assets and real estate.
- ▶ Revise its equity management plan by setting specific allocations for international and domestic mid and small capitalization equity managers.
- ▶ Set specific target allocations across fixed income sectors.

By implementing these changes, the Board can help ensure that the Permanent Fund will achieve the highest expected return for its chosen risk level. This will help the Board achieve its statutory goals of maximizing total Fund return and providing the maximum amount of disposable income to Alaska's citizens.



This report presents recommendations concerning the Alaska Permanent Fund. The first section provides background information on the procedures we used to perform the asset allocation study. The second section suggests improvements for those portfolios, and outlines a third portfolio suited to a more aggressive investment philosophy. The final section provides guidance on several important implementation issues.

I. Analyzing an Investment Portfolio

A first step in analyzing an investment portfolio is determining whether the portfolio adequately compensates the investor for taking risk. Ideally, the portfolio is *efficient* in providing return to the investor; i.e., the portfolio provides the most return possible for the amount of risk taken. In reality, however, few portfolios accomplish this objective.

Defining Asset Classes

In order to analyze the Fund's portfolio, we had to decide which assets to include in the Fund's investment universe. Currently, the Fund invests in 12 different asset classes that comprise six main categories. The benchmarks used to represent each asset class in our analysis are listed in Appendix A at the end of this report. The asset classes used in our study are as follows:

U.S. Equity Assets

Large Capitalization
Mid/Small Capitalization

Non-U.S. Equity Assets

Canada
Europe
Pacific
Emerging Markets

Other Assets

Real Estate

Non-U.S. Fixed Income Assets

Intermediate-Term Government/Corporate Bonds
Long-Term Government/Corporate Bonds
Mortgage-Backed Securities

Non-U.S. Fixed Income Assets

Non-U.S. Government Bonds

Cash

U.S. Treasury Bills



Forecasting Return

We also had to forecast three estimates for each asset class: expected return, expected risk (as measured by standard deviation), and expected return correlation between assets. Summary tables of our forecasts are provided in Appendix B. It is important to note that our return, risk, and correlation forecasts are *long-term* -- they apply to an investment horizon of 10 years or more. Our forecasts are passive in nature and, therefore, would not change dramatically if we were to recalculate them a year from now. Consequently, the portfolio allocations we recommend will remain stable over a very long time period, and will require few changes over a long-term investment horizon.


The basis for our equity return forecasts is the risk-free rate of return and the historical premium, called an equity risk premium, that is demanded by investors for holding risky assets. We use the historical premium because the amount by which common stocks have outperformed risk-free government bonds has been consistent over time. The long-term equity risk premium for large capitalization domestic equities over the period January 1926 to September 1993 was 7.25 percent. Also, many researchers have found that, as the risk of an investment increases, so does its expected return. For this reason, we forecast the expected return of other equity asset classes, such as domestic small capitalization equities and international equities, to have greater expected returns.

The basis of our fixed income return forecasts is the current risk-free rate of return, as proxied by the current yield on a risk-free government bond with a maturity matching the investment time horizon. Currently, this rate is 6.31 percent, the current yield on 20-year U.S. Treasury bond. To this rate, we add the appropriate maturity premium (additional return required by investors for relinquishing the use of their money for long time periods) and default premium (additional return that compensates investors for buying bonds that have default risk, such as corporate bonds) for each class of bonds for which we are forecasting returns.

For international fixed income assets, we forecast returns as if the assets were denominated in U.S. dollars. Since currency fluctuations are expected to average to zero over time, any short-term currency gains or losses will not affect the long-term return on international assets. Currency fluctuations do increase risk, however, and are accounted for in our risk forecasts of non-U.S. fixed income assets.

Forecasting Risk

When forecasting the risk of an asset, we typically assume that the future will equal the past. Therefore, we forecast risk by calculating the historical standard deviation using a long time period over which we have reliable data, and data that is representative of possible future scenarios. Although investment risk can be quantified in a number of



ways for asset allocation purposes, we believe that risk is best modeled as the annual volatility of returns, and standard deviation provides an estimate of how much actual returns may deviate from the average, expected return over time. We use shorter time periods only when we can identify a permanent and dramatic process shift in the behavior of an asset class, such as the late 1960s when bond market volatility increased noticeably from its observed volatility during the previous 40 years.

Forecasting Return Correlation


Return and risk are not the only factors that determine how a portfolio performs. The correlation between the returns of two assets also plays an important role in portfolio performance. Correlation measures how much the returns of two assets tend to move together or move separately. If the returns move together, the assets are positively correlated. If they move in opposite directions, the assets are negatively correlated. If no pattern can be detected in the way the assets' returns move, the assets have a return correlation of zero.

Portfolios comprised only of assets that have high, positive correlations with each other are not well diversified. This tends to exaggerate both upside and downside volatility, and the risk of the portfolio. On the other hand, portfolios with assets that have low or negative return correlations will provide more stable returns because, even though some assets may perform poorly, other portfolio assets will perform better, serving to reduce portfolio volatility. The benefits of diversification, therefore, are a direct result of relatively low return correlations among portfolio assets.

When forecasting return correlation, we again typically assume that the future will equal the past. The basis for our forecast of return correlation is, therefore, the historical correlation between assets, observed over the longest time period for which reliable data is available.

Determining the Fund's Current Allocation

The amount of the Fund currently allocated to each asset class was determined by using information in the Fund's 1993 Annual Report, with supplemental information provided by William L. Means, the Fund's Chief Investment Officer. Market values of all investments came from the Annual Report, while Mr. Means provided clarification regarding the amount currently invested in equities of domestic companies with capitalizations larger than \$1 billion (large capitalization equities), the amount currently invested in equities of companies with capitalizations of \$1 billion or less (mid and small capitalization equities), and the amount currently invested in domestic government and corporate bonds with maturities ranging from one to seven years (intermediate-term),



and more than seven years (long-term). The Fund's current allocation, and its expected return and standard deviation is given on page 5.

Determining the Fund's Three-Year Target Allocation

The Permanent Fund's investment manual provided information regarding the three-year target allocation, although some guidelines were too broad for our purposes. For example, the manual lists a 10 percent target allocation for international equities, but gives no country-specific allocations. In this case, we assumed the Fund would increase its international equity exposure to 10 percent, while maintaining the current proportion invested among sectors. Also, the target allocation constrains the amount invested in non-domestic fixed income assets to 10 percent or less, but provides no specific number. We assumed the amount invested in international debt would decrease in proportion to the total decrease in the amount allocated to all fixed income assets. The Fund's three-year target allocation, and its expected return and risk, is listed on the following page.

Current and Three-Year Target Portfolios

Asset Class	Current Allocation (%)	3-Year Target Allocation (%)
U.S. Large Capitalization Stocks	21.17	24.00
U.S. Mid/Small Capitalization Stocks	0.65	6.00
Canadian Stocks	0.03	0.04
European Stocks	2.54	4.28
Pacific Region Stocks	2.94	4.97
Emerging Market Stocks	0.42	0.72
Real Estate	6.69	10.00
Cash	4.64	0.00
Intermediate Govt/Corp Bonds	30.86	25.32
Long-Term Govt/Corp Bonds	25.27	20.74
Mortgage-Backed Securities	3.94	3.24
Non-U.S. Government Bonds	0.85	0.69
Expected Return (%)	8.53	9.93
Standard Deviation (%)	7.57	9.91



II. Asset Allocation Recommendations

The next step in our analysis was to improve the Fund's current and target portfolios by increasing their expected return while keeping expected risk at a constant level.

Allocation with Risk of the Current Portfolio

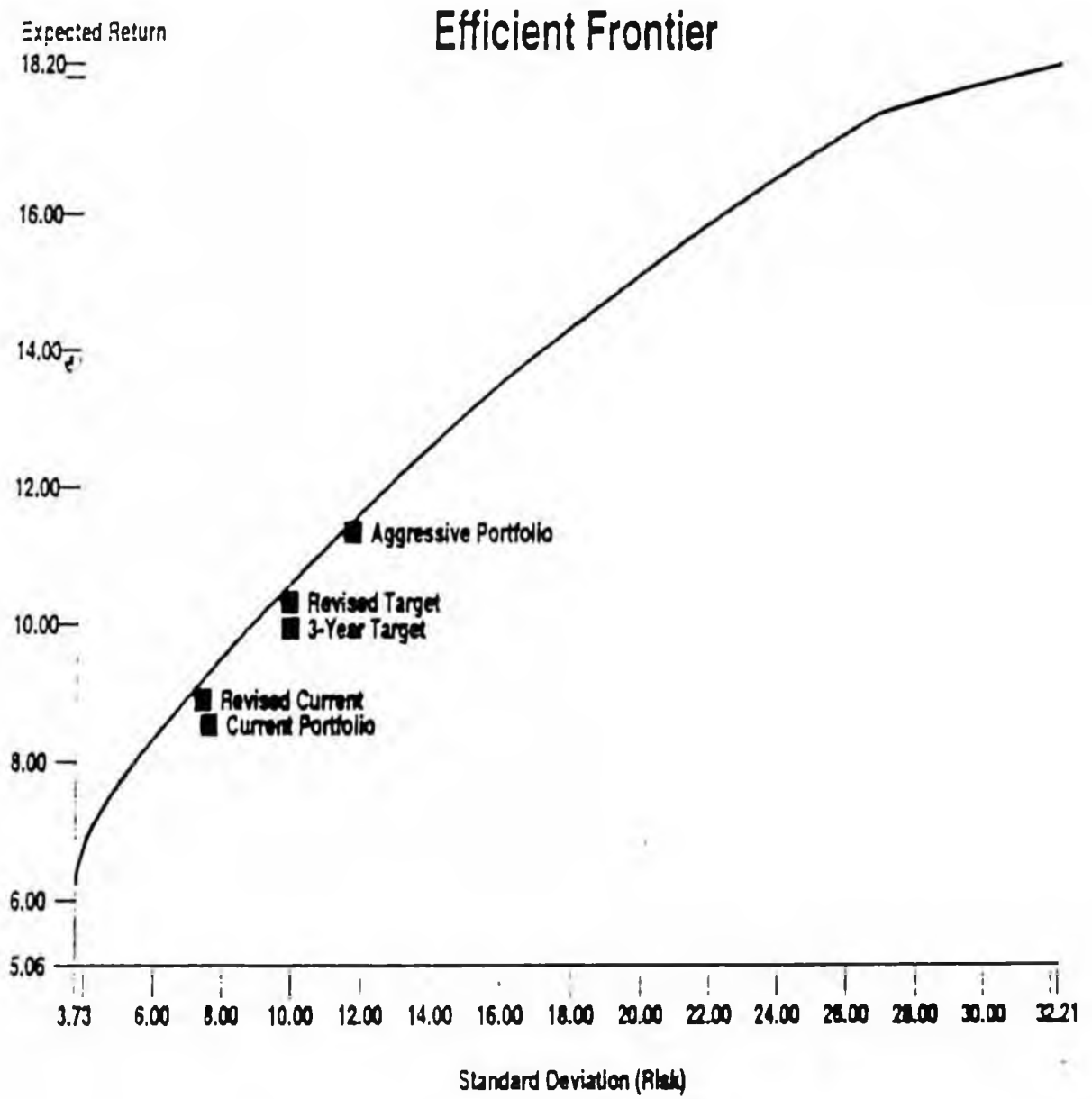
As shown in the graph on page 7, the Fund's current portfolio does not provide the maximum amount of expected return for the amount of risk taken. For example, the portfolio labeled "revised current" provides a higher expected return and slightly less risk than the current portfolio. (The graph is titled "Efficient Frontier" because the line in the graph represents those portfolios which are the most efficient in providing return to the investor; i.e., those portfolios provide the maximum return for a given level of risk.) The allocations for both the current and revised portfolios, as well as their expected returns and standard deviations, are shown on page 8.

The current portfolio need not be drastically changed in order to achieve a higher expected return. In fact, the percent of the portfolio invested in equities (approximately 35 percent, including real estate) and in fixed income assets (approximately 65 percent), is the same in both the current and revised portfolios. Rather, the composition of the equity and fixed income portions need only change. By shifting part of the equity portion from large capitalization stocks to mid and small capitalization and international stocks, and part of the fixed income portion from cash and long-term bonds to intermediate-term bonds and mortgage-backed securities, the Fund can achieve a higher expected return while taking less risk.

Although these changes represent shifts from safer assets to more risky ones, the overall risk of the portfolio actually decreases. This is because domestic mid and small stocks, mortgage-backed securities, and international stocks have low correlations with many of the other portfolio assets.

Allocation with Risk of the Target Portfolio

The graph on page 7 shows that the Fund's target portfolio also does not provide the highest possible expected return for the amount of risk taken. Although both the allocations of the target and revised target portfolios are equally divided between equity and fixed income assets, the revised target portfolio has a significantly higher expected return and less risk. The composition of both portfolios, along with their expected returns and standard deviations, is given on page 8.



**Current and Recommended
Portfolio Allocations**

Asset Classes	Allocations				
	Current Portfolio (%)	Revised Current (%)	3-Year Target (%)	Revised Target (%)	Aggressive Portfolio (%)
U.S. Large Cap Stocks	21.17	11.00	24.00	16.00	18.00
U.S. Mid/Small Cap Stocks	0.65	4.00	6.00	8.00	10.00
Canadian Stocks	0.03	0.00	0.04	0.00	0.00
European Stocks	2.54	3.50	4.28	6.00	7.50
Pacific Region Stocks	2.94	4.00	4.97	7.00	10.50
Emerging Market Stocks	0.42	2.50	0.72	3.00	4.00
Real Estate	6.69	10.00	10.00	10.00	10.00
Cash	4.64	1.00	0.00	1.00	1.00
Intermediate-Term Govt/Corp Bonds	30.86	40.00	25.32	30.00	18.00
Long-Term Govt/Corp Bonds	25.27	12.00	20.74	5.00	6.00
Mortgage-Backed Securities	3.94	12.00	3.24	14.00	15.00
Non-U.S. Govt Bonds	0.85	0.00	0.69	0.00	0.00
Expected Return	8.53	8.89	9.93	10.31	11.33
Standard Deviation	7.57	7.40	9.91	9.89	11.69

The superior tradeoff between risk and return of the revised target portfolio can be accomplished by shifting a larger portion of Fund assets into domestic mid and small capitalization stocks, international stocks, mortgage securities, and real estate. Again, these riskier assets have low correlations with many other portfolio assets, and therefore provide enhanced diversification benefits.

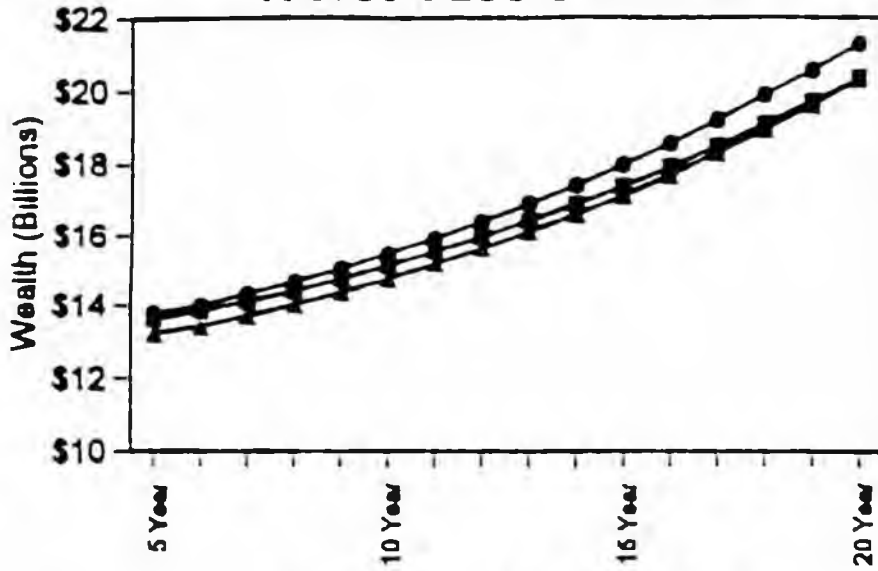
Allocation of a More Aggressive Portfolio

Although we have analyzed and suggested improvements to both the current and target portfolios, we have not yet commented on whether either portfolio is appropriate for the Fund. Ideally, a portfolio provides enough return to meet the goals of the investor while maintaining a level of risk that is comfortable for the investor. By setting a three-year target portfolio that has an increased allocation to equity assets, the Board has indicated that it is comfortable with a more aggressive investment philosophy. In our opinion, such an aggressive investing strategy is appropriate and necessary for achieving the Fund's statutory goals of maximizing total return and providing the maximum amount of disposable income to the citizens of Alaska. Consequently, we believe the Fund should consider the benefits of investing in the "aggressive portfolio," also shown in the graph on page 7.

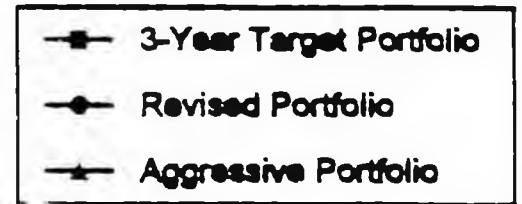
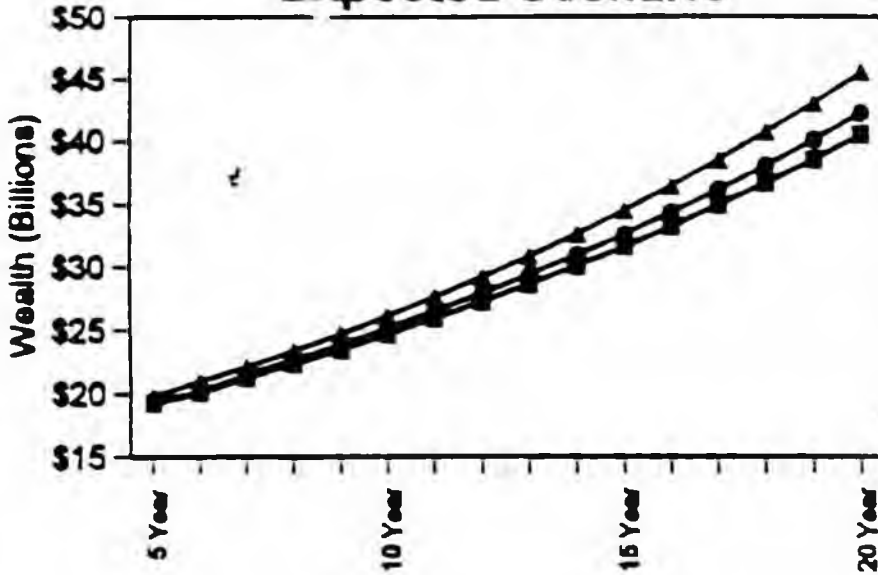
In recent years, the Fund has enjoyed relatively high returns, particularly on its fixed income investments. These high returns were due, in part, to rather unique market conditions, such as a dramatic decline in U.S. interest rates. These market conditions, however, are not expected to continue in the future, as evidenced by the returns expected on the current and target Fund portfolios. The potentially lower returns earned by both these portfolios are important factors to consider, because such low returns will inevitably lead to lower dividend payments to Alaskans. Our recommended aggressive portfolio, however, with its significant allocations to international equities and mortgage-backed securities, has an expected return in the range of the Fund's recent returns. The allocation of this aggressive portfolio, along with its expected return and standard deviation, is provided on page 8.

The graphs on the following page can help to compare the expected performance of each portfolio. The graphs show expected wealth values under the target, revised target, and aggressive portfolios for five-, ten-, and twenty-year investment horizons. Although the Board may consider the aggressive portfolio too risky, the graph shows that the majority of this portfolio's volatility is due to its broad range of possible high, *positive* returns, not negative ones. For all investment time horizons, the aggressive portfolio has a higher expected wealth value under the best- and expected-case scenarios. Only under the worst-case scenario does the aggressive portfolio underperform the target portfolio, while the revised target portfolio performs better than the target portfolio in *all* cases.

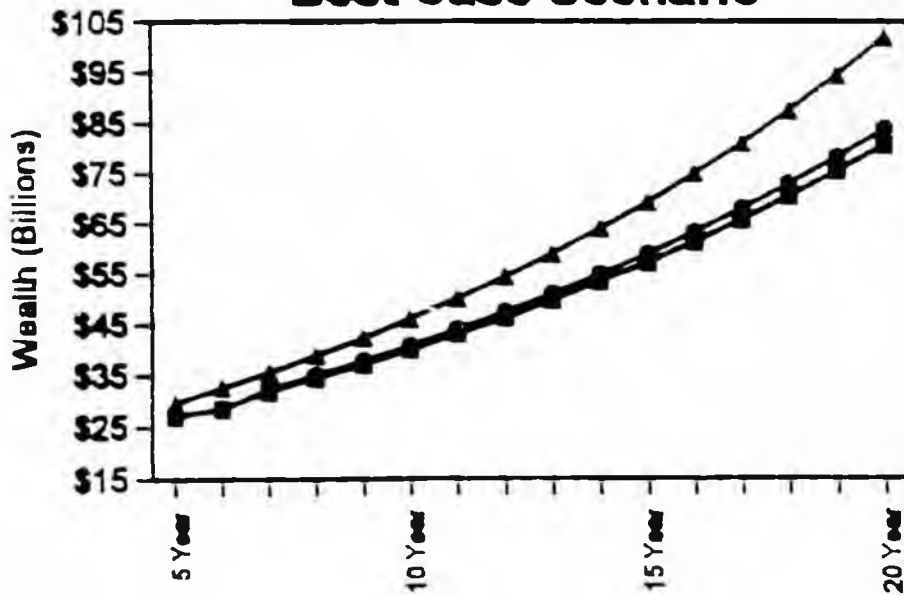
Worst Case Scenario



Expected Scenario



Best Case Scenario





Testing Our Recommended Portfolios

To ensure the validity of our recommended portfolios, we tested those portfolios and the Fund's current and target portfolios for *stability*. A stable portfolio is one that performs well under a variety of possible future market conditions; i.e., the portfolio provides adequate return for the amount of risk taken under conditions that differ from our forecasts. We tested the portfolios using "worst-case" scenarios where the return of one or more assets is lower than expected and the risk is higher than expected. The following scenarios were used, both individually and in combination, to test our recommended portfolios:

- U.S. equity risk premium decreases to 5 percent
- Mid and small capitalization equity return decreases to 15 percent
- Europe equity return decreases to 10 percent
- Europe equity standard deviation increases to 26 percent
- Pacific equity return decreases to 10 percent
- Pacific equity standard deviation increases to 34 percent
- Emerging market equity return decreases to 10 percent
- Return between long-term and intermediate-term bonds increases to 1 percent
- Intermediate-term bond standard deviation increases to 6 percent
- Mortgage-backed securities return decreases to 6 percent
- Mortgage-backed securities standard deviation increases to 11 percent
- Real estate standard deviation increases to 25 percent
- Correlation between U.S. stocks and U.S. bonds increases 30 percent
- Correlation between U.S. stocks and non-U.S. stocks increases 30 percent

Under these scenarios, our recommended portfolios provided higher returns with less risk than either the Fund's current or target portfolios. For example, the improved target portfolio had 10 basis points more return and less risk than the current target portfolio when tested under the assumption that all international markets had the lower returns and higher risks outlined above. This indicates that the revised portfolios will perform better over the long run, despite possible extreme underperformance of some markets.



III. Implementation Issues

Whichever portfolio the Board chooses, several issues must be addressed by the Board to ensure maximum Fund performance. The single most important issue is the degree of adherence to the chosen allocation. Research has suggested that the asset allocation decision accounts for over 90 percent of the variability of returns on a portfolio, and is the single largest determinant of portfolio performance.¹ Consequently, individual security selection and active security management, the two factors commonly assumed to contribute the most to the return of a portfolio, actually account for only a small amount of portfolio return variability. Therefore, adherence to the chosen allocation is *crucial* to the future performance of any investment portfolio, including the Permanent Fund. Accordingly, the Board must decide whether the current investment strategy of the Fund accommodates a strict adherence to the chosen allocation. We address this issue separately for equity and fixed income assets in the following two sections.

Equity Assets

As of April 1993, the Board decided to use active managers only for domestic mid/small capitalization stocks and all international equities. Since our recommended portfolios are based on passive benchmarks, we believe that the long-term performance we forecast can be achieved through the use of passive managers, although it is certainly possible for active managers to meet or exceed that performance. For this reason, we believe the Board's decision to retain active managers is appropriate, *as long as each manager is given only that portion of Fund assets that is recommended in the chosen allocation, and is required to invest those assets in the specific, recommended asset class.*

This stipulation is in direct contrast to the Board's new global investment strategy as outlined in the Fund's 1993 Annual Report. The new strategy allows active international equity managers to decide when and where to invest Fund assets, essentially *shifting* the asset allocation decision from the Board to the manager. As mentioned earlier, asset allocation, not security selection or active market timing, is the largest determinant of portfolio performance. Under the planned strategy, the Fund's equity allocation will shift continuously, violating the most crucial aspect of strategic asset allocation: maintaining a stable asset mix which was chosen based on long-term forecasts and needs of the fund. For this reason, we suggest a slightly modified strategy where the Board hires managers that have a specific style of investing. For example, under this modified strategy, the European equity allocation would be managed by a manager who specializes in European equities. This type of management strategy would allow the Board to retain control over the equity allocation of the Fund.

¹ Gary P. Brinson, Brian D. Singer, and Gilbert L. Beebower, "Determinants of portfolio performance II: An update," *Financial Analysts Journal*, May-June 1991.


The Fund's domestic equity managers also have similar control over the asset allocation decision. Currently, the performance of each domestic equity manager is evaluated by using a benchmark portfolio that consists of 80 percent large capitalization equities and 20 percent mid and small capitalization equities. The equity managers, however, are not specifically required to invest 80 percent of their Fund allocation in large capitalization stocks and 20 percent in mid and small capitalization stocks. A manager could alternate between large cap and mid and small cap stocks, and still *average* an 80 percent large cap and 20 percent mid and small cap investment. This manager could potentially be 100 percent invested in large cap stocks when the return in the mid and small cap market is high, and vice-versa. Again, this causes the overall equity allocation of the Fund to change continuously, and shifts control of the asset allocation decision to individual managers. Because the asset allocation decision is so important to the overall performance of the Fund, we feel the Board should set specific domestic equity allocations, and select managers who specialize in each asset class. This will ensure the maximum expected return for the Fund's equity investments.

Fixed Income Assets

Currently, the Fund's fixed income assets are passively managed in-house by the Fund's Chief Investment Officer, and are generally treated as a single asset class. Our analysis, however, treats the fixed income category as five distinct asset classes, because each contributes unique benefits to the overall portfolio. Treasury bills, for example, provide more liquidity than the other assets, and are, consequently, the least risky. Also, mortgage-backed securities perform differently from government or corporate bonds. For this reason, each fixed income asset class must be considered separately in the asset allocation decision.

Currently, the Board treats all fixed income assets as a single asset class and provides only a broad allocation directive. This essentially shifts the asset allocation decision to the fixed income manager. While the current allocation across fixed income assets may be appropriate when viewed in isolation, that same allocation may be inappropriate when viewed in the context of the overall portfolio. The Board has a comprehensive perspective on the Fund and, as such, should determine the Fund allocation to each asset class. For this reason, we suggest that the Board set specific target allocations for fixed income asset classes. In this way, the Board maintains control over the Fund's asset allocation and ensures maximum overall Fund performance.

Prior to beginning our study, several Board members and senators voiced concern over the Fund having only one manager for the entire fixed income portfolio. We feel that a single, capable manager, such as the current manager, can manage a large, passive fixed income portfolio with few problems, as long as that portfolio has only a small allocation to mortgage-backed securities. However, if a larger proportion of funds was invested in



mortgage-backed securities (as is our recommendation), it may be required to hire additional staff. This is because mortgage-backed securities are more complex to analyze, and the holders of mortgage securities continually receive principal and interest payments which must be accurately recorded. All our recommended portfolios contain substantial allocations to mortgage-backed securities. Consequently, we suggest that the Board hire an outside manager to manage the mortgage portfolio, or, at the very least, hire additional support staff.

Conclusion

Although the Permanent Fund has an excellent performance history, the Fund faces new and uncertain investment challenges in the coming years. The Board, realizing the importance of asset allocation to overall Fund performance, has created a target allocation to meet those challenges. However, as our analysis reveals, the Board can implement a better allocation for the Fund, one that has higher expected return and less risk than the Fund's target portfolio. Also, the Board can implement a new investing policy, one emphasizing an adherence to the chosen allocation. By doing so, the Board will help ensure the maximum expected performance of the Fund over the long-term investment horizon, thereby providing the highest possible income to the State's citizens and fulfilling its obligation to those citizens.



Appendix A: Benchmarks Used in Asset Allocation Study

<u>Asset Class</u>	<u>Benchmark Description</u>
U.S. Large Capitalization Equity	S&P 500: A market capitalization-weighted index of 500 of the largest stocks of companies domiciled in the United States.
U.S. Mid/Small Capitalization Equity	Russell 2000 Index: A market capitalization-weighted index of the stocks of the bottom two thirds of the largest 3,000 publicly traded companies domiciled in the United States.
Canada Equity	Morgan Stanley Capital International Canada Total Return Index: A market capitalization-weighted index of 81 large Canadian stocks.
Europe Equity	Morgan Stanley Capital International Europe Total Return Index: A market capitalization-weighted index of large stocks from Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Spain, Sweden, Switzerland, and the United Kingdom.
Pacific Equity	Morgan Stanley Capital International Pacific Total Return Index: A market capitalization-weighted index of large stocks from Australia, Hong Kong, Japan, Malaysia, New Zealand, and Singapore.
Emerging Markets Equity	IFC Emerging Market Composite Index: A broad-based, market capitalization-weighted index of stocks listed in countries with a per capita GDP below an annually-disclosed figure. Currently, 20 countries are represented in the Composite index.
Cash	U.S. 90-Day Treasury Bills: Published by Salomon Brothers in <i>International Bond and Money Market Performance</i> .



IT Govt/Corp Bonds

Lehman Brothers Intermediate-Term Government/Corporate Bond Total Return Index: A portfolio of U.S. government issues (>\$100 million par value) and investment grade corporate debt (>\$50 million par value) with an average maturity of 4.42 years as of November 29, 1993.

LT Govt/Corp Bonds

Lehman Brothers Government/Corporate Bond Total Return Index: A portfolio of U.S. government issues (>\$100 million par value) and investment grade corporate debt (>\$50 million par value) with an average maturity of 10.81 years as of November 29, 1993.

Mortgage-Backed Securities

Lehman Brothers Mortgage-Backed Securities Total Return Index: An index of all fixed-rate securities backed by mortgage pools of the Government National Mortgage Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC), and the Federal National Mortgage Association (FNMA). The index has an average maturity of 5.39 years.

Non-U.S. Bonds

Salomon Brothers Non-U.S. 1+ Bond Index: A market capitalization-weighted index of bonds from Australia, Canada, Germany, Japan, Netherlands, Switzerland, and the United Kingdom with one year or more to maturity. The average maturity of bonds in the index is 6.95 years.

Real Estate

Wilshire Real Estate Securities Total Return Index: A market capitalization-weighted index of approximately 85 real estate investment trust and real estate operating companies.



Appendix B: Forecasts Used in Asset Allocation Study

Forecasts of Expected Return and Standard Deviation

Asset Class	Expected Return	Standard Deviation
U.S. Large Cap Stocks	13.56	20.61
U.S. Mid/Small Cap Stocks	18.03	32.95
Canada Stocks	13.73	24.64
Europe Stocks	13.98	22.69
Pacific Stocks	15.11	28.24
Emerging Market Stocks	21.38	47.00
Real Estate	9.90	13.63
Cash	4.61	2.73
IT Govt/Corp Bonds	5.89	4.10
LT Govt/Corp Bonds	6.37	7.22
Mortgage-Backed Securities	7.45	9.28
Non-U.S. Govt Bonds	6.01	14.75

GOVERNOR TONY KNOWLES
LIEUTENANT GOVERNOR FRAN ULMER

Executive Summary

KNOWLES/ULMER

POLICY

TRANSITION

TEAMS'

REPORT

JANUARY 1995

Fiscal Policy

The Knowles/Ulmer Administration asked the Fiscal Policy team to build on the ideas from other public forums to develop guidelines for a responsible fiscal plan to guide the state into the 21st century, and to make recommendations on how to achieve the broad public support necessary for their implementation.

RECOMMENDATIONS

- Continue to articulate a "vision" of the state's financial future—the administration's views on the appropriate role of government and the values and criteria that should guide our public policy decisions—and recognize the threat the fiscal gap poses to ourselves and our children.
 - Make a commitment to develop a plan to bring annually recurring revenues into balance with state spending.
 - Integrate the cabinet into the plan and process, i.e., the commissioners should all be speaking in concert and actively involved in the plan's development.
 - Convey the message that sound fiscal management equals good government and good government means good politics.
 - The team emphatically endorses the Knowles/Ulmer campaign pledge to cap total state spending (except for education funding) at the FY 95 level.
 - Continue with an unwavering policy of budget sustainability and develop an annual report card to inform the public about the success of the administration's actions to protect Alaska's fiscal future.

- Give average citizens a direct voice in shaping the future and invite the public to help develop a shared vision for Alaska and the role of government in their lives.
 - Develop a strategy for inviting public input into fiscal decisions and collect baseline information on public attitudes regarding the fiscal gap.
 - Implement a strategy for educating the public on Alaska's fiscal situation and our choices for the future. Effective forums might include: newspaper inserts, town meetings, market research, industry groups, social service groups and local government bodies.
 - Ask the legislature to participate in every step of the outreach process.
 - Make government more open to the public through better use of communication systems, including electronic media (video conference, internet, Alaska Online, etc.).
 - As part of a long-term strategy, the administration should budget for public participation in reexamining the respective roles of state and local governments, setting goals and benchmarks for Alaska, and deciding the role of the Permanent Fund in the state's fiscal future.

- Create an annually updated five-year fiscal plan.
 - Work with and inform the legislature in a timely manner of any changes the administration wishes to make in the FY 96 budget, and announce that a fiscal plan will be in place by the time the FY 97 budget is proposed.
 - Develop a five-year plan and a comprehensive reporting framework that encompasses all aspects of state spending and revenues, including "off-budget items" such as Permanent Fund earnings, Permanent Fund dividends, cash reserves, public corporations, etc. Include deferred maintenance and the operating and maintenance costs of capital projects in the plan.

- Resolve legal questions surrounding the use of the Constitutional Budget Reserve funds, the setting of specific revenue and expenditure targets (including Permanent Fund dividends), development of a debt policy (including school debt reimbursement), an overall reserves policy employing triggers for instituting an income tax, and a cash-flow management plan.
 - Implement the five-year plan and keep the public informed of Alaska's fiscal situation and progress toward reaching fiscal stability. Although no consensus was reached, one approach recommended was to set up a budget commission or blue ribbon task force to act as a conduit between the executive branch, legislature and the public to develop a long-term fiscal strategy for Alaska.
 - Capitalize cash reserves to the greatest extent possible.
 - Pass legislation to automatically inflation-proof the Permanent Fund by distributing only real earnings for dividends.
 - Explore means of controlling personnel costs.
 - Examine various public services for potential privatization.
 - Evaluate all entitlement programs on an ability-to-pay basis.
- Form partnerships for economic development and intergovernmental alliances.
 - Emphasize partnerships between the executive and legislative branches, state and local governments, and the public and private sectors.
 - Create a spirit of cooperation between the state of Alaska and the federal government.
 - Eliminate unfunded mandates on local governments.
 - Reexamine the state's petroleum tax and royalty regime with the intention of maintaining Alaska's competitiveness.
 - Improve federal relations and understanding of Alaska issues, particularly with respect to oil and gas development, and adopt a "Visit Alaska" program to allow members of Congress to see the state in order to make more informed decisions.
 - Maintain the economic viability of resource development by ensuring that efforts aimed at increasing revenues from resource industries are made via an income tax on jobs rather than through increased business taxes. (The team noted that non-petroleum resource development actually ends up costing the state money in comparison to revenues generated.)
 - Make serious efforts at regulatory reform to reduce government red tape.
 - Organize programs to streamline the delivery of state government services.
 - Make state government as cost-efficient as possible by adopting a customer-oriented approach to public service delivery.
 - Develop and begin to implement meaningful, real-world performance measures of the effectiveness of government programs.
 - In order to provide incentives to agencies, commissioners should be allowed to use part or all of their cost savings for investments that will increase future productivity.
 - An employee recognition and cash reward system should be developed and funded for employee ideas that save money.
 - Join in a partnership with local governments to thoroughly evaluate the delivery of services to the public. Ensure that public services are delivered at the most appropriate level of government to meet the needs of the citizenry in the most cost-effective manner possible, even if government roles need redefinition.

Alaska State Senate

SENATOR STEVE RIEGER
District I

Senate Finance Committee
Chair, Senate Transportation Committee

Legislative Budget and Audit Committee
Administrative Regulation Review Committee
Legislative Council

During Session:
State Capitol, Room 516
Juneau, Alaska 99801
(907) 465-1879

716 West 4th Avenue, Suite 530
Anchorage, Alaska 99501
(907) 258-8188

TO: Senator Rick Halford
Co-Chair, Senate Finance Committee

FROM: Senator Steve Rieger *A*

DATE: March 9, 1995

RE: SB 51 - "An Act Relating to the Income of the Permanent Fund"

I respectfully request that you calendar the above referenced bill in the Senate Finance Committee at your earliest convenience. I am attaching a bill packet for distribution to member's files.

Thank you for your consideration of this matter.

*3/27/95 packet
placed in
Sen. Rieger's
file
per Steve
(per Steve)*

Alaska State Senate

SENATOR STEVE RIEGER
District 1

Senate Finance Committee
Chair, Senate Transportation Committee

Legislative Budget and Audit Committee
Administrative Regulation Review Committee
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During Session:
State Capitol, Room 516
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716 West 4th Avenue, Suite 530
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SENATE BILL 51

-AN ACT RELATING TO THE INCOME OF THE PERMANENT FUND-

- SPONSOR STATEMENT
- PERMANENT FUND TRUSTEES' POSITION PAPER, 2/25/95
- PERMANENT FUND PROJECTIONS, January, 1995
- ALASKA POPULATION PROJECTIONS, March 1992
- IBBOTSON REPORT- Asset Allocation Study of the Alaska
Permanent Fund Report dated January, 1994
- "Real Dollars Now Means Real Dividends Later" by Tim Bradner
Anchorage Daily News, January 8, 1995
- EXECUTIVE SUMMARY - Knowles/Ulmer Policy Transition Teams'
Report, dated January, 1995

Alaska State Senate

SENATOR STEVE RIEGER
District 1

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PERMANENT FUND PROJECTIONS:

The attached projections from the Alaska Permanent Fund Corporation show the effect of different earnings assumptions on the size of the Permanent Fund, as well as the amount of each year's earnings and transfers to the dividend fund, through the year 2000.

The first forecasts provided by the Permanent fund Corporation are based on recent investment performance and long-standing assumptions which the Corporation has used regarding nominal earnings and inflation.

At my request, the Permanent Fund Corporation also did additional runs, which reflect the higher earnings assumptions suggested in the Ibbotson Associates' report (enclosed). The Ibbotson report was commissioned by the Legislative Budget and Audit Committee and completed January 1994. This report recommends a target portfolio which is higher-yielding than its present portfolio because of a greater amount of assets invested in higher-yielding securities. This return was estimated by Ibbotson to be 10.31%. The attached projections include assumptions of 10.31% nominal earnings and 6% inflation; and assumptions of 10.31% nominal earnings and 4% inflation. Finally, the projections are stated in nominal dollars and inflation-adjusted dollars.



Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1999

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
8	0		54		54	
9	54		24		139	
10	139		344		483	
11	483	300	385		1,768	
12	1,769	300	400		2,969	
13	2,969	400	421	231	4,021	
14	4,021	300	388	151	4,838	
15	4,838	300	368	235	5,741	
16	5,741		323	218	6,281	
17	6,281	1,264 **	170	148	7,864	
18	7,864		418	303	8,585	
19	8,585		228	360	9,173	
20	9,173		267	454	9,894	
21	9,894		435	559	10,888	
22	10,888		338	477	11,703	
23	11,703	5 ***	315	382	12,385	
24	12,385	6 ***	210	372	12,973	
25	12,973	5	212	344	13,534	
26	13,534	2	198	515	14,253	
27	14,253	7	194	542	14,996	
28	14,996	7	185	570	15,757	
29	15,757	8	168	598	16,532	
30	16,532	6	160	1,002	17,699	
31	17,699	6	145	1,071	18,921	
32	18,921	7	130	1,143	20,201	
33	20,201	7	117	1,218	21,546	
34	21,545	8	105	1,298	22,958	
35	22,958	9	94	1,383	24,444	
36	24,444	10	87	1,472	26,012	
37	26,012	11	81	1,566	27,669	
38	27,669	12	76	1,665	29,421	
39	29,421	13	70	1,770	31,273	
40	31,273	14	67	1,880	33,234	

Cumulative Totals Projected
For FY 1995 - 2010: 2,932 18,892

USE OF FUND INCOME

FY	Net Income	Distributions			Reserves		FY End Balance	FY
		Dividends	Per Capita Dividends	Inflation-Proofing	General Fund	Add (Delete)		
8	2							78
9	8							79
10	32	12						80
11	150	28				59	59	81
12	368	71	\$1,000.00			185	244	82
13	471	108	\$388.15	231	110	110	364	83
14	530	178	\$331.28	151		288	567	84
15	658	217	\$484.00	235		208	769	85
16	1,021	303	\$556.28	218		501	1,264 **	86
17	1,088	391	\$708.18	148		528	528	87
18	789	424	\$828.83	303		82	591	88
19	868	488	\$872.16	380	4	44	635	89
20	918	487	\$882.63	454	4	(36)	688	90
21	1,030	488	\$831.34	559	4	(24)	591	91
22	1,038	488	\$831.34	477	5	84	646	92
23	1,228	532	\$948.48	382	5	328	985	93
24	1,088	588	\$882.88	372	11	181	1,117	94
25	950	588	\$842.88	344	14	258	1,385	95
26	1,252	588	\$888.00	515		181	1,297	96
27	1,325	608	\$878.00	542		188	1,486	97
28	1,402	627	\$888.00	570		188	1,664	98
29	1,483	688	\$1,027.00	598		211	1,876	99
30	1,748	738	\$1,134.88	1,002		(11)	1,865	0
31	1,888	812	\$1,282.88	1,071		(34)	1,851	1
32	1,988	878	\$1,278.00	1,143		(82)	1,769	2
33	2,081	948	\$1,381.00	1,218		(94)	1,674	3
34	2,198	1,023	\$1,428.88	1,298		(132)	1,542	4
35	2,318	1,082	\$1,482.00	1,383		(186)	1,388	5
36	2,448	1,143	\$1,537.00	1,472		(188)	1,208	6
37	2,578	1,288	\$1,582.88	1,568		(288)	1,022	7
38	2,713	1,271	\$1,688.88	1,668		(284)	788	8
39	2,857	1,338	\$1,708.88	1,770		(284)	584	9
40	3,007	1,410	\$1,770.00	1,880		(297)	287	10
25	950	588	\$842.88	344	14	258	1,385	95
26	1,252	588	\$888.00	515		181	1,297	96
27	1,325	608	\$878.00	542		188	1,486	97
28	1,402	627	\$888.00	570		188	1,664	98
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29	1,483	688	\$1,027.00	598		211	1,876	99
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40	3,007	1,410	\$1,770.00	1,880		(297)	287	10
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27	1,325	608	\$878.00	542		188	1,486	97
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29	1,483	688	\$1,027.00	598		211	1,876	99
30	1,748	738	\$1,134.88	1,002		(11)	1,865	0
31	1,888	812	\$1,282.88	1,071		(34)	1,851	1
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25	950	588	\$842.88	344	14	258	1,385	95
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31	1,888	812	\$1,282.88	1,071		(34)	1,851	1
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40	3,007	1,410	\$1,770.00	1,880		(297)	287	10
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27	1,325	608	\$878.00	542		188	1,486	97
28	1,402	627	\$888.00	570		188	1,664	98
29	1,483	688	\$1,027.00	598		211	1,876	99
30	1,748	738	\$1,134.88	1,002		(11)	1,865	0
31	1,888	812	\$1,282.88	1,071		(34)	1,851	1
32	1,988	878	\$1,278.00	1,143		(82)	1,769	2
33	2,081	948	\$1,381.00	1,218		(94)	1,674	3
34	2,198	1,023	\$1,428.88	1,298		(132)	1,542	4
35	2,318	1,082	\$1,482.00	1,383		(186)	1,388	5
36	2,448	1,143	\$1,537.00	1,472		(188)	1,208	6
37	2,578	1,288	\$1,582.88	1,568		(288)	1,022	7
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40	3,007	1,410	\$1,770.00	1,880		(297)	287	10
25	950	588	\$842.88	344	14	258	1,385	95
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29	1,483	688	\$1,027.00	598		211	1,876	99
30	1,748	738	\$1,134.88	1,002		(11)	1,865	0
31	1,888	812	\$1,282.88	1,071		(34)	1,851	1
32	1,988	878	\$1,278.00	1,143		(82)	1,769	2
33	2,081	948	\$1,381.00	1,218		(94)	1,674	3
34	2,198	1,023	\$1,428.88	1,298		(132)	1,542	4
35	2,318	1,082	\$1,482.00	1,383</				



Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
91			54		54	
92	54		34		139	
93	139		344		483	
94	483	300	385		1,769	
95	1,769	300	400		2,969	
96	2,969	400	421	231	4,021	
97	4,021	300	368	151	4,838	
98	4,838	300	368	235	5,741	
99	5,741		323	218	5,281	
00	5,281	1,264**	170	148	7,364	
01	7,364		418	303	8,585	
02	8,585		228	360	9,173	
03	9,173		267	454	9,894	
04	9,894		435	559	10,888	
05	9,894		435	559	10,888	
06	11,703		315	362	12,385	
07	12,385		210	372	12,973	
95†	12,973	5	212	344	13,534	
96	13,345	5	204	497	13,738	
97	13,241	5	184	479	13,931	
98	13,428	5	174	485	14,110	
99	13,600	7	160	492	14,269	
00	13,460	5	138	488	14,411	
01	13,595	5	123	769	14,534	
02	13,711	5	105	778	14,629	
03	13,810	5	89	781	14,729	
04	13,895	5	78	786	14,808	
05	13,968	5	54	790	14,872	
06	14,031	5	54	794	14,931	
07	14,086	5	47	797	14,983	
08	14,135	5	41	807	15,030	
09	14,179	5	37	802	15,072	
10	14,218	5	32	808	15,110	

Cumulative Totals Projected:
For FY 1995-2010: 1,738 10,683

USE OF FUND INCOME

Net Income	Distributions			General Fund	Reserves	
	Dividends	Per Capita Dividends	Inflation-Proofing		Add (Delete)	FY End Balance
2					1	
3					7	
4					12	
5	150	29			29	59
6	268	71	\$1,000.00		71	244
7	471	108	\$388.15	231	110	354
8	530	175	\$331.29	151		507
9	558	217	\$404.00	235		763
00	1,021	303	\$588.28	216		1,264
01	1,069	391	\$708.19	148		1,529
02	739	424	\$328.93	303		1,591
03	368	460	\$873.18	360		1,535
04	316	487	\$822.83	454		1,506
05	1,030	489	\$931.34	559		1,581
06	1,030	489	\$915.34	559		1,581
07	1,226	532	\$949.48	362		1,965
08	1,098	558	\$883.90	372	11	1,117
95†	950	558	\$942.00	344	14	1,146
96	1,206	559	\$921.00	497		1,250
97	1,231	564	\$918.00	479		1,362
98	1,256	561	\$888.00	485		1,490
99	1,280	575	\$888.00	492		1,619
00	1,422	610	\$923.00	486		1,519
01	1,425	624	\$923.00	769		1,406
02	1,425	637	\$924.00	776		1,282
03	1,423	649	\$924.00	781		1,144
04	1,418	660	\$921.00	786		995
05	1,411	658	\$902.00	790		844
06	1,403	656	\$882.00	794		693
07	1,395	653	\$883.00	797		543
08	1,386	649	\$843.00	800		392
09	1,377	645	\$823.00	802		243
10	1,367	641	\$805.00	805		94
95†	21,374	9,899	\$10,277	10,883	14	

* Department of Revenue Fall 1994 Low-Cost Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994.

STATUS QUO IN REAL 1995 DOLLARS

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 95-99:	5.49%	2.61%	3.68%
FY 98-99:	3.11%	3.75%	4.36%
FY 00-2010:	3.00%	6.00%	3.00%

Constant/Real dollars

In times of any inflation, the value of the dollar erodes over time. Adjusting future nominal amounts to constant 1995 dollars removes the effects of inflation from the future projections.



Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
78	0		34		34	
79	54		34		139	
80	139		344		483	
81	483	500	385		1,769	
82	1,769	300	400		2,969	
83	2,969	400	421	231	4,021	
84	4,021	300	366	151	4,838	
85	4,838	300	368	235	5,741	
86	5,741		323	216	6,281	
87	6,281	1,264**	170	148	7,864	
88	7,864		418	303	8,585	
89	8,585		228	360	9,173	
90	9,173		257	454	9,884	
91	9,884		425	559	10,868	
92	10,868		338	477	11,703	
93	11,703	5***	315	362	12,385	
94	12,385	5***	210	372	12,973	
95	12,973	5	212	344	13,534	
96	13,534	5	198	515	14,252	
97	14,252	7	194	542	14,995	
98	14,995	7	185	568	15,758	
99	15,758	3	169	597	16,530	
00	16,530	5	160	1,001	17,696	
01	17,696	5	145	1,071	18,919	
02	18,919	7	130	1,143	20,200	
03	20,200	7	117	1,219	21,544	
04	21,544	8	105	1,299	22,958	
05	22,958	9	94	1,383	24,442	
06	24,442	10	87	1,472	26,010	
07	26,010	11	81	1,568	27,667	
08	27,667	12	78	1,665	29,419	
09	29,419	13	70	1,768	31,277	
10	31,277	14	57	1,880	33,231	

Cumulative Totals Projected:
For FY 1995-2010: 2,023 18,034

USE OF FUND INCOME

Net Income	Distributions			Reserves		FY
	Inflation-Proofing	Per Capita Dividends	General Fund	Add (Delete)	FY End Balance	
2						78
3						79
12						80
28						81
71						82
108	231					83
175	151					84
217	235					85
303	216					86
391	148					87
424	303					88
480	380					89
487	454					90
489	559					91
488	477					92
532	362					93
558	372					94
521	344					95
490	515					96
462	542					97
424	568					98
441	597					99
427	1,001					00
443	1,071					01
461	1,143					02
483	1,219					03
508	1,299					04
538	1,383					05
608	1,472					06
688	1,568					07
727	1,665					08
733	1,768					09
884	1,880					10

36,589 18,034 8,873 812,293 16

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 95-	6.49%	2.51%	3.88%
FY 96-99****	8.11%	3.75%	4.36%
FY 2000-10:	9.00%	5.00%	3.00%

* Department of Revenue Fall 1994 Low-Cost Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994.



Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
83			54		54	
84	54		34		139	
85	139		344		483	
86	483	300	385		1,769	
87	1,769	300	400		2,969	
88	2,969	400	421	231	4,021	
89	4,021	300	388	151	4,838	
90	4,838	300	368	235	5,741	
91	5,741		223	216	6,281	
92	6,281	1,254	170	148	7,864	
93	7,864		418	303	8,585	
94	8,585		228	360	9,173	
95	9,173		267	454	9,894	
96	9,894		435	559	10,888	
97	9,894		435	559	10,888	
98	11,703	5	315	362	12,385	
99	12,385	5	210	372	12,973	
00	12,973	5	212	344	13,534	
01	13,045	5	204	498	13,737	
02	13,241	5	184	478	13,931	
03	13,427	5	174	485	14,108	
04	13,599	7	160	481	14,287	
05	13,459	5	138	488	14,410	
06	13,594	5	123	789	14,533	
07	13,710	5	108	778	14,638	
08	13,809	5	88	781	14,728	
09	13,894	5	78	788	14,808	
10	13,967	5	64	790	14,871	
11	14,030	5	54	794	14,930	
12	14,085	5	47	797	14,982	
13	14,134	5	41	800	15,028	
14	14,178	5	37	802	15,070	
15	14,217	6	32	804	15,109	

Cumulative Totals Projected:
For FY 1995 - 2010: 1,738 10,681

USE OF FUND INCOME

Net Income	Distributions			Reserves		FY End Balance
	Dividends	Per Capita Dividends	Inflation-Proofing	General Fund	Add (Delete)	
2						54
3						139
12						483
28						1,769
71						2,969
108		\$1,000.00				4,021
175		\$331.29				4,838
217		\$404.00				5,741
303		\$554.28				6,281
391		\$708.19				7,864
424		\$828.93				8,585
480		\$973.16				9,173
487		\$982.83				9,894
488		\$931.14				10,888
488		\$915.84				10,888
532		\$948.48				12,385
558		\$983.90				12,973
521		\$877.00				13,534
472		\$771.00				13,737
429		\$678.00				13,931
390		\$582.00				14,108
381		\$570.00				14,287
348		\$508.00				14,410
340		\$484.00				14,533
334		\$478.00				14,638
330		\$481.00				14,728
327		\$438.00				14,808
338		\$448.00				14,871
348		\$483.00				14,930
380		\$481.00				14,982
371		\$468.00				15,028
382		\$478.00				15,070
393		\$483.00				15,109

23,825 5,052 3,816 10,881 14

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 88:	5.49%	2.51%	3.98%
FY 88 - 89:	3.11%	3.75%	4.36%
FY 00 - 2010:	3.00%	5.00%	3.00%

Constant/Real dollars

In times of any inflation, the value of the dollar erodes over time. Adjusting future nominal amounts to constant 1995 dollars removes the effects of inflation from the future projections.

- * Department of Revenue Fall 1994 Low-Case Revenue Forecast.
- ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
- *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
- **** Based on capital market assumptions adopted by the Trustees in March 1994.

SB 51 IN REAL 1995 DOLLARS



2A

Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appro- priations	Dedicated State Revenues*	Inflation- Proofing	FY End Balance	Inflation- Proofing Shortfall
78	0		54		54	
79	54		34		139	
80	139		344		483	
81	483	900	385		1,769	
82	1,769	500	400		2,969	
83	2,969	400	421	231	4,021	
84	4,021	300	368	151	4,838	
85	4,838	300	368	235	5,741	
86	5,741		323	216	6,281	
87	6,281	1,254	170	148	7,864	
88	7,864		418	303	8,585	
89	8,585		228	380	9,173	
90	9,173		287	454	9,894	
91	9,894		435	559	10,888	
92	10,888		338	477	11,703	
93	11,703	5	315	382	12,385	
94	12,385	5	210	372	12,973	
95	12,973	5	212	344	13,534	
96	13,534	5	198	324	14,561	
97	14,561	7	194	308	15,848	
98	15,848	7	185	290	16,790	
99	16,790	8	169	1,018	17,986	
00	17,985	9	160	1,089	19,243	
01	19,243	10	145	1,163	20,560	
02	20,560	11	130	1,241	21,843	
03	21,943	12	117	1,324	23,386	
04	23,396	13	108	1,410	24,925	
05	24,925	15	94	1,501	26,535	
06	26,535	16	87	1,587	28,238	
07	28,238	18	81	1,680	30,033	
08	30,033	20	78	1,807	31,838	
09	31,938	22	70	1,920	33,947	
10	33,947	24	67	2,041	36,079	

Cumulative Totals Projected:
For FY 1995-2010: 2,023 20,838

USE OF FUND INCOME

FY	Net Income	Distributions			Reserves		FY
		Inflation- Proofing	Per Capita Dividends	General Fund	Add (Delete)	FY End Balance	
78	2				1		78
79	3				7		79
80	32		12		12		80
81	150		28		28	59	81
82	368		71	\$1,000.00	71	185	82
83	471	231	108	\$388.15	110	110	83
84	530	151	175	\$331.29		203	84
85	658	235	217	\$404.00		208	85
86	1,021	218	303	\$558.28		501	86
87	1,069	148	391	\$708.19		329	87
88	789	303	424	\$828.93		52	88
89	868	380	480	\$873.18	4	44	89
90	918	454	487	\$962.83	4	(30)	90
91	1,030	559	488	\$831.34	4	(24)	91
92	1,038	477	488	\$819.84	5	64	92
93	1,228	382	532	\$948.46	5	320	93
94	1,088	372	558	\$813.90	11	151	94
95	950	344	521	\$677.00	14	65	95
96	1,814	324	486	\$308.00		288	96
97	1,737	388	475	\$753.00		390	97
98	1,917	950	448	\$530.00		512	98
99	2,087	1,018	480	\$725.00		591	99
00	2,291	1,089	508	\$748.00		687	00
01	2,502	1,163	583	\$818.00		788	01
02	2,728	1,241	628	\$883.00		848	02
03	2,971	1,324	897	\$978.00		938	03
04	3,231	1,410	773	\$1,088.00		1,034	04
05	3,510	1,501	958	\$1,180.00		1,137	05
06	3,808	1,587	948	\$1,282.00		1,248	06
07	4,130	1,680	1,044	\$1,371.00		1,388	07
08	4,475	1,807	1,148	\$1,488.00		1,488	08
09	4,845	1,920	1,263	\$1,608.00		1,840	09
10	5,243	2,041	1,388	\$1,740.00		1,783	10

48,088 20,813 12,226 \$1,878 14

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 95-	5.49%	2.61%	3.88%
FY 96-99-	10.31%	6.00%	4.31%
FY 2000-10-	10.31%	6.00%	4.31%

* Department of Revenue Fall 1994 Low-Cost Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994.
 SENATE BILL NO. 51, BUT ASSUMES 10.31% FUTURE RATE OF RETURN
 AND 6% RATE OF INFLATION.



2-12

Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
'91			54		54	
'91	54		34		139	
'01	139		344		483	
'11	483	300	385		1,769	
'21	1,769	500	400		2,969	
'31	2,969	400	421	231	4,021	
'41	4,021	300	368	151	4,838	
'51	4,838	200	368	235	5,741	
'61	5,741		323	216	5,281	
'71	5,281	1,254	170	148	7,864	
'81	7,864		418	303	8,585	
'91	8,585		228	360	9,173	
'01	9,173		267	454	9,894	
'11	9,894		435	559	10,888	
'21	9,894		435	559	10,888	
'31	11,703	5	315	362	12,385	
'41	12,385	5	210	372	12,973	
'51	12,973	5	212	344	13,534	
'61	12,768	5	200	777	13,737	
'71	12,959	5	178	733	13,928	
'81	13,138	5	183	743	14,087	
'91	13,299	5	147	752	14,246	
'01	13,439	7	128	780	14,379	
'11	13,565	7	113	787	14,484	
'21	13,674	7	98	774	14,580	
'31	13,767	3	82	779	14,679	
'41	13,848	3	70	783	14,753	
'51	13,918	3	58	787	14,817	
'61	13,978	3	50	791	14,874	
'71	14,032	3	43	794	14,928	
'81	14,081	3	38	787	14,973	
'91	14,125	10	34	798	15,019	
'01	14,165	10	29	801	15,084	

Cumulative Totals Projected:
For FY 1995-2010: 1,838 11,983

USE OF FUND INCOME

Net Income	Distributions			Reserves		FY
	Per Capita Dividends	Inflation-Proofing	General Fund	Add (Delete)	FY End Balance	
2						'91
3						'91
32	12					'01
150	28					'11
368	71	\$1,000.00				'21
471	108	\$388.15	231			'31
530	175	\$331.28	151			'41
558	217	\$404.00	235			'51
1,021	303	\$358.28	216			'61
1,069	391	\$708.19	148			'71
789	424	\$828.83	303			'81
368	480	\$172.18	380			'91
916	487	\$962.83	454			'01
1,030	488	\$931.34	559			'11
1,030	488	\$915.84	559			'21
1,228	532	\$948.48	362			'31
1,098	558	\$983.90	372			'41
950	521	\$872.00	344			'51
1,522	487	\$782.00	777			'61
1,584	422	\$878.00	733			'71
1,610	378	\$578.00	743			'81
1,661	381	\$574.00	752			'91
1,712	378	\$588.00	780			'01
1,784	397	\$575.00	787			'11
1,814	417	\$584.00	774			'21
1,864	437	\$812.00	779			'31
1,912	458	\$830.00	783			'41
1,960	478	\$848.00	787			'51
2,008	488	\$888.00	791			'61
2,062	518	\$881.00	794			'71
2,088	538	\$887.00	797			'81
2,143	558	\$711.00	799			'91
2,188	578	\$728.00	801			'01

28,820 7,426 \$10,580 11,983 14

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 95:	5.49%	2.51%	3.88%
FY 98-99:	10.31%	5.00%	4.31%
FY 00-2010:	10.31%	5.00%	4.31%

Constant/Real dollars

In times of any inflation, the value of the dollar erodes over time. Adjusting future nominal amounts to constant 1995 dollars removes the effects of inflation from the future projections.

* Department of Revenue Fall 1994 Low-Cost Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994.
 SENATE BILL NO. 51, BUT ASSUMES 10.31% FUTURE RATE OF RETURN AND 6% RATE OF INFLATION; IN REAL 1995 \$\$.



2 B

Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

as of January 31, 1995

GROWTH OF FUND PRINCIPAL						USE OF FUND INCOME								
FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall	Distributions			Reserves		FY		
							Net Income	Inflation-Proofing	Per Capita Dividends	General Fund	Add (Delete)		FY End Balance	
81	0		34		34		2			1			81	
91	34		34		139		3			7			79	
01	139		344		433		12			12			301	
11	483	500	385		1,769		150	28		28	59	59	311	
21	1,769	300	400		2,969		368	71	\$1,000.00	71	185	244	321	
31	2,969	400	421	231	4,021		471	231	108	\$388.15	110	110	354	331
41	4,021	300	368	151	4,838		530	151	175	\$331.29	203	557	341	
51	4,838	300	368	215	5,741		558	215	217	\$404.00	208	763	351	
61	5,741		323	216	6,281		1,021	216	303	\$556.26	501	1,264	361	
71	6,281	1,264	170	148	7,864		1,069	148	391	\$708.19	529	529	371	
81	7,864		418	303	8,585		789	303	424	\$826.93	62	591	381	
91	3,585		228	360	9,173		668	360	460	\$873.16	4	44	535	391
01	3,173		257	454	3,894		918	454	487	\$952.63	4	(30)	605	301
11	3,894		435	559	10,988		1,030	559	489	\$931.34	4	(24)	581	311
21	10,888		338	477	11,703		1,036	477	488	\$915.84	5	54	645	321
31	11,703	5	315	362	12,385		1,228	362	532	\$948.48	5	320	965	331
41	12,385	5	210	372	12,973		1,098	372	556	\$983.90	11	151	1,117	341
51	12,973	5	212	344	13,534		950	344	521	\$877.00	14	65	1,182	351
61	13,534	9	198	548	14,290		1,814	549	524	\$858.00	532	1,714	96	361
71	14,290	10	194	579	15,073		1,754	579	535	\$858.00	529	2,343	97	371
81	15,073	11	185	610	15,879		1,907	610	543	\$848.00	743	3,086	98	381
91	15,879	12	199	642	16,702		2,075	642	613	\$840.00	308	3,896	99	391
01	16,702	13	160	675	17,550		2,253	675	678	\$1,020.00	887	4,782	0	401
11	17,550	15	145	708	18,417		2,441	708	747	\$1,102.00	971	5,753	1	411
21	18,417	16	130	742	19,305		2,640	742	822	\$1,190.00	1,060	6,813	2	421
31	19,305	18	117	777	20,217		2,852	777	903	\$1,282.00	1,155	7,968	3	431
41	20,217	20	108	813	21,155		3,077	813	989	\$1,378.00	1,258	9,224	4	441
51	21,155	22	94	850	22,121		3,315	850	1,081	\$1,479.00	1,363	10,567	5	451
61	22,121	24	87	888	23,120		3,568	888	1,178	\$1,588.00	1,479	12,066	6	461
71	23,120	26	81	928	24,155		3,839	928	1,283	\$1,698.00	1,502	13,668	7	471
81	24,155	29	78	988	25,229		4,128	988	1,385	\$1,818.00	1,734	15,401	8	481
91	25,229	32	70	1,012	26,342		4,432	1,012	1,514	\$1,938.00	1,875	17,278	9	491
01	26,342	35	67	1,058	27,501		4,758	1,058	1,641	\$2,072.00	2,025	19,301	10	501
Cumulative Totals Projected:							45,803	12,143	14,967	\$20,542	14			

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
1995:	5.49%	2.51%	3.88%
1996 - 99: ****	10.31%	4.00%	6.31%
2000 - 10:	10.31%	4.00%	6.31%

* Department of Revenue Fall 1994 Low-Case Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994
SENATE BILL NO. 51, BUT ASSUMES 10.31% FUTURE RATE OF RETURN AND 4% RATE OF INFLATION.



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Alaska Permanent Fund Corporation

FINANCIAL PROJECTIONS (in millions)

As of January 31, 1995

GROWTH OF FUND PRINCIPAL

FY	FY Begin Balance	Appropriations	Dedicated State Revenues*	Inflation-Proofing	FY End Balance	Inflation-Proofing Shortfall
93			54		54	
94	54		54		109	
95	109		244		353	
96	353	300	285		938	
97	938	300	400		2,969	
98	2,969	400	421	231	4,021	
99	4,021	300	368	151	4,838	
00	4,838	300	368	235	5,741	
01	5,741		323	216	6,281	
02	6,281	1,254	170	148	7,864	
03	7,864		418	203	8,583	
04	8,583		228	260	9,173	
05	9,173		257	454	9,884	
06	9,884		435	559	10,888	
07	9,884		435	559	10,888	
08	11,703		315	362	12,385	
09	12,385		210	372	12,973	
10	12,973	5	212	344	13,534	
11	13,013	9	203	328	13,740	
12	13,211	9	183	508	13,938	
13	13,400	10	173	515	14,117	
14	13,574	10	158	522	14,277	
15	13,728	11	139	528	14,425	
16	13,870	11	127	533	14,558	
17	13,995	12	110	538	14,670	
18	14,106	13	96	542	14,773	
19	14,204	14	83	548	14,863	
20	14,292	15	71	549	14,944	
21	14,369	15	51	552	15,018	
22	14,441	16	54	555	15,087	
23	14,507	17	48	557	15,152	
24	14,569	18	44	560	15,212	
25	14,627	20	39	562	15,270	

USE OF FUND INCOME

FY	Net Income	Distributions			Reserves		FY
		Dividends	Per Capita Dividends	Inflation-Proofing	General Fund	Add (Delete) Balance	
93	2					1	93
94	3					7	94
95	32	12				12	95
96	150	28				28	96
97	268	71	\$1,000.00			71	97
98	471	108	\$388.15	231	110	110	98
99	530	173	\$331.29	151		223	99
00	558	217	\$404.00	235		228	00
01	1,021	303	\$358.28	216		501	01
02	1,089	391	\$708.19	148		529	02
03	789	424	\$428.93	303		52	03
04	968	480	\$873.18	360	4	44	04
05	916	487	\$852.83	454	4	(30)	05
06	1,030	488	\$531.34	559	4	(24)	06
07	1,030	489	\$915.84	559	4	(24)	07
08	1,226	532	\$948.48	382	5	320	08
09	1,098	558	\$983.80	372	11	151	09
10	950	521	\$877.00	344	14	65	10
11	1,352	503	\$828.00	528		512	11
12	1,522	496	\$791.00	508		582	12
13	1,698	483	\$754.00	515		661	13
14	1,774	524	\$804.00	522		681	14
15	1,851	557	\$838.00	528		729	15
16	1,929	581	\$871.00	533		768	16
17	2,008	625	\$904.00	538		808	17
18	2,084	680	\$877.00	542		844	18
19	2,162	686	\$888.00	548		882	19
20	2,240	730	\$988.00	549		921	20
21	2,318	783	\$1,030.00	552		980	21
22	2,398	801	\$1,081.00	558		1,000	22
23	2,478	838	\$1,081.00	557		1,041	23
24	2,560	874	\$1,120.00	560		1,083	24
25	2,642	911	\$1,151.00	582		1,125	25
10-25	12,281	10,573	\$15,022	8,438	14		10-25

Cumulative Totals Projected:
For FY 1995 - 2010: 1,798 8,438

REALIZED RATE OF RETURN ASSUMPTIONS:

	Nominal	Inflation	Real
FY 95:	5.49%	2.51%	3.38%
FY 96 - 99:	10.31%	4.00%	5.31%
FY 00 - 2010:	10.31%	4.00%	5.31%

Constant/Real dollars

In times of high inflation, the value of the dollar erodes over time. Adjusting future nominal amounts to constant 1995 dollars removes the effects of inflation from the future projections.

* Department of Revenue Fall 1994 Low-Case Revenue Forecast.
 ** Earnings reserve appropriated to Fund principal by the Legislature July 1, 1987.
 *** Transferred to principal from earnings reserve account per AS 37.13.145(d).
 **** Based on capital market assumptions adopted by the Trustees in March 1994.
 SENATE BILL NO. 51, BUT ASSUMES 10.31% FUTURE RATE OF RETURN AND 4% RATE OF INFLATION; IN REAL 1995 \$\$.

SENATE COMMITTEE REPORT
First Committee of Referral

JMR DATE: 1/25/95

FURTHER: Finance

Date of 5-Day Notice: 2-9-95
 (in accordance with Uniform Rule 23)

DATE TURNED INTO OFFICE: 3-2-95

State Affairs Committee considered SENATE BILL NO. 51

~~"An Act relating to income of the permanent fund; and providing for an effective date."~~

and recommends:

Φ ER

- be replaced with _____ CS _____
- adopt previous _____ CS _____
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to the _____ Committee

Senate Bill:
 same title
 new title
 House Bill:
 technical change
 new: SCR# _____

SIGNING DO PASS	DP	OTHER RECOMMENDATIONS	NR	DNP	AM
		<i>Loren A. Leman</i>	✓		
		<i>(1) David J. Jolley</i>	✓		
		<i>Robert J. Demarest</i>	✓		
		<i>Richard E. Hood</i>	✓		
CHAIR:		<i>Best Thomas</i>	✓		

NEW FISCAL NOTE(S):

Department	Date	Zero	Fiscal
REVENUE	3/13	✓	

PREVIOUS FISCAL NOTE(S):*

Department	Date	Zero	Fiscal

APPROPRIATION -- no fiscal note

*include fiscal notes accompanying Governor's bill