

**PFD
BOARD OF
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PRESENT.,**

2/03

SFIN

FILE

Alaska Permanent Fund

Brief history and financial outlook for Fund growth and income

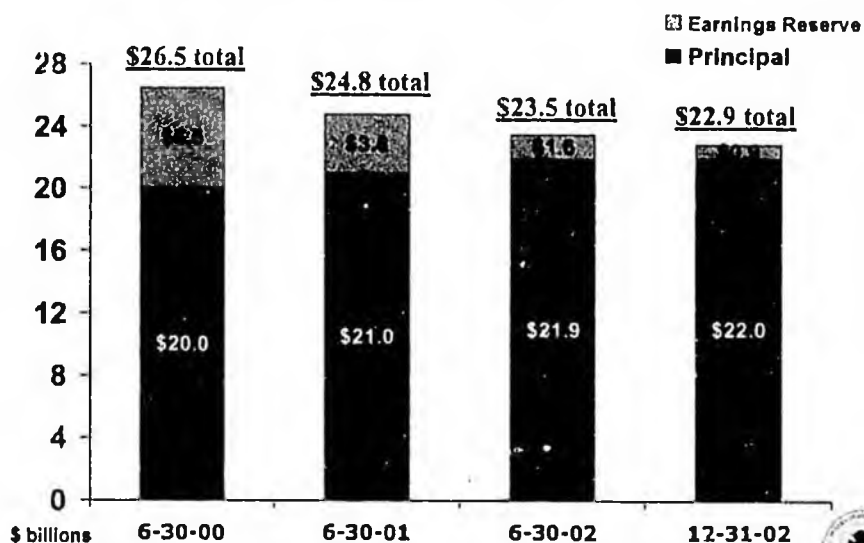
February, 2003

Alaska Permanent Fund Corporation



Permanent Fund market value

30-month change in principal and earnings reserve account



Alaska Permanent Fund Corporation

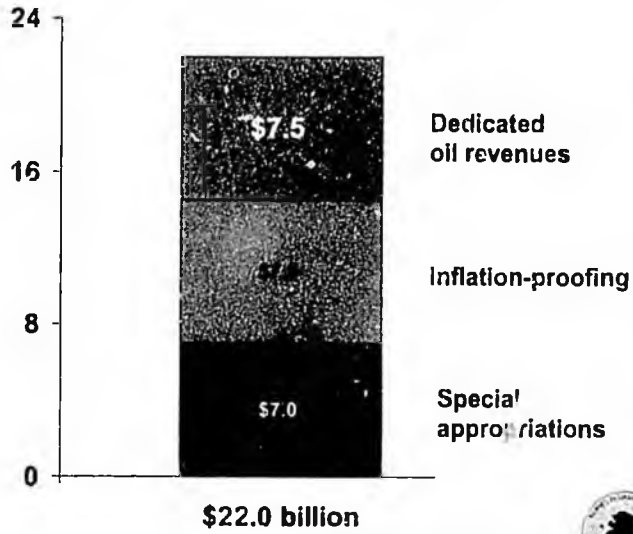


Fund principal

source of contributions as of December 31, 2002

The Alaska Permanent Fund principal is protected by the Alaska Constitution.

The principal is not available for appropriation.



\$22.0 billion

Alaska Permanent Fund Corporation

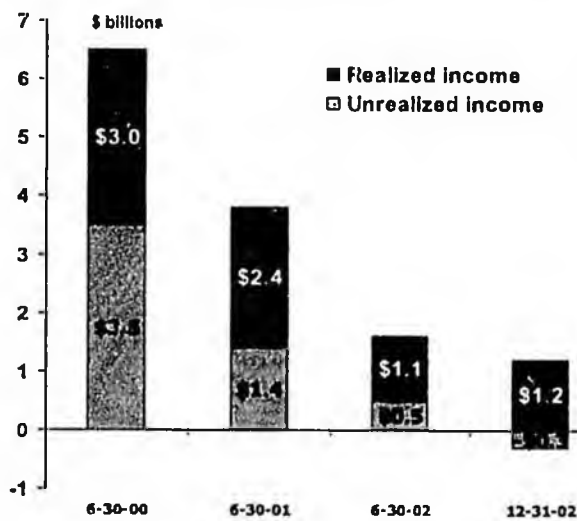


Earnings reserve account

30-month change in realized and unrealized income

As provided by law, all Fund income is deposited in the earnings reserve account.

It is retained there until appropriated by the legislature.



Alaska Permanent Fund Corporation



Earnings reserve reconciliation

What happened to the \$5.6 billion?

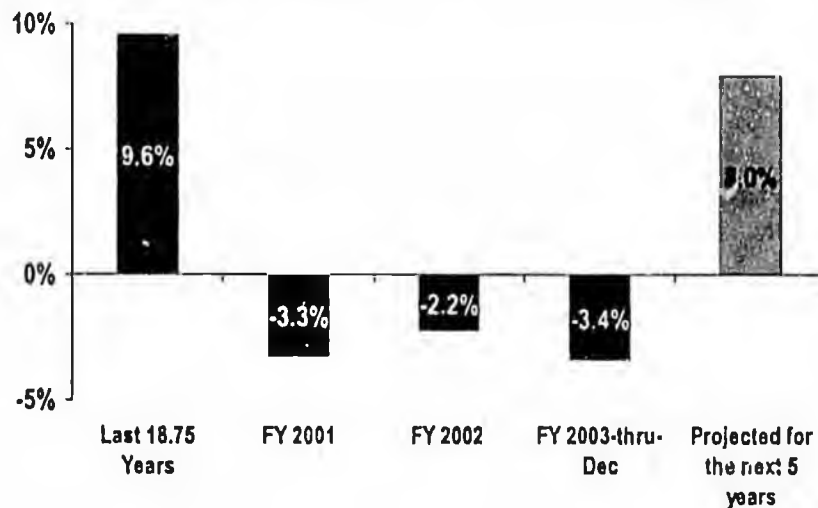
Amount	Description
\$5.6 billion	June 30, 2001 ERA balance
-\$2.4 billion	2 years of net cash flow (interest, dividends and real estate)
-\$1.0 billion	2 years of net realized losses
-\$1.3 billion	2 years of net pension funding transfers to principal
-\$2.0 billion	2 years of paying distributions for PFD's
+\$3.9 billion	2 years change in unrealized gains
= \$.9 billion	December 31, 2002 ERA balance

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Fund's total return

annualized for the past, recent times and the future



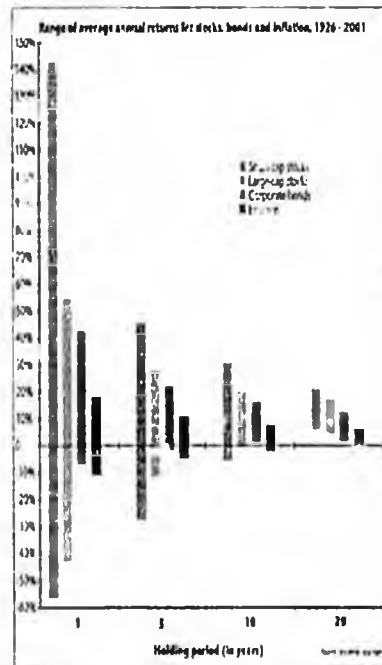
Alaska Permanent Fund Corporation



Fund's asset allocation and control bands

Domestic equities	37% +/- 7%
<u>International equities</u>	<u>16% +/- 5%</u>
Total equities	53% +/- 5%
Domestic bonds	35% +/- 7%
<u>Non-Dollar bonds</u>	<u>2% +/- 2%</u>
Total bonds	37% +/- 5%
Total real estate	10% +/- 2%

Alaska Permanent Fund Corporation



Staying the course

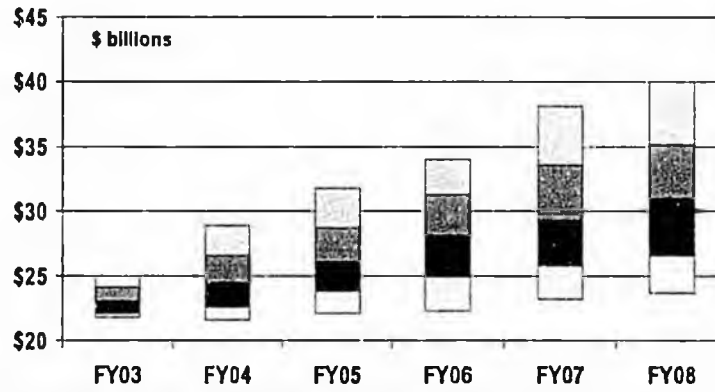
Although there is a 1 in 4 (25%) chance that the Fund will earn a negative return in any single year, there is only a 1 in 20 (5%) chance over a 5-year period and a 1 in 100 (1%) chance over a 10-year period of a negative return.

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Range of market value

FY03 – FY08



	FY03	FY04	FY05	FY06	FY07	FY08
10 th Percentile	\$25.1	\$28.9	\$31.7	\$33.9	\$38.1	\$40.0
25 th Percentile	\$24.2	\$26.6	\$28.6	\$31.3	\$33.6	\$35.1
Median	\$23.1	\$24.5	\$26.0	\$28.1	\$29.3	\$30.9
75 th Percentile	\$22.2	\$22.6	\$23.7	\$24.9	\$25.9	\$26.6
90 th Percentile	\$21.8	\$21.6	\$22.1	\$22.3	\$23.2	\$23.7

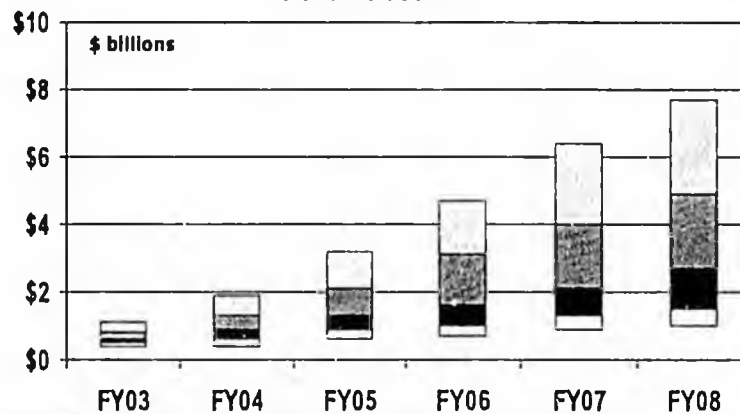
Data as of 12/31/02

Alaska Permanent Fund Corporation



Range of realized earnings reserve

FY03 – FY08



	FY03	FY04	FY05	FY06	FY07	FY08
10 th Percentile	\$1.1	\$1.9	\$3.1	\$4.7	\$6.3	\$7.7
25 th Percentile	\$.8	\$1.3	\$2.0	\$3.1	\$4.0	\$4.9
Median	\$.6	\$.9	\$1.2	\$1.6	\$2.0	\$2.7
75 th Percentile	\$.5	\$.6	\$.8	\$1.1	\$1.3	\$1.5
90 th Percentile	\$.4	\$.4	\$.6	\$.8	\$.9	\$1.0

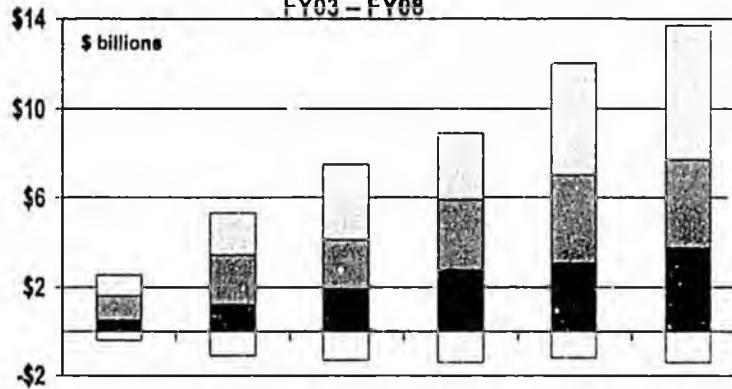
Data as of 12/31/02

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Range of total earnings reserve

FY03 - FY08



	FY03	FY04	FY05	FY06	FY07	FY08
10 th Percentile	\$2.5	\$5.3	\$7.5	\$9.0	\$12.0	\$13.7
25 th Percentile	\$1.6	\$3.4	\$4.1	\$6.0	\$7.0	\$7.7
Median	\$0.5	\$1.2	\$1.9	\$2.8	\$3.1	\$3.7
75 th Percentile	(\$0.2)	(\$0.3)	(\$0.2)	\$0.1	\$0.1	\$0.0
90 th Percentile	(\$0.4)	(\$1.1)	(\$1.3)	(\$1.4)	(\$1.2)	(\$1.4)

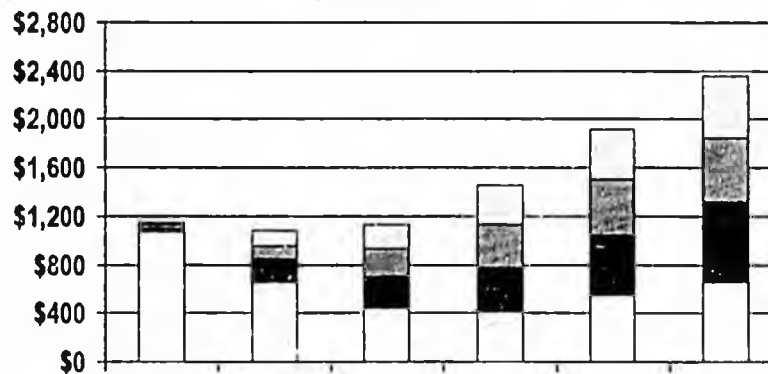
Data as of 12/31/02

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Range of per capita dividends

FY03 - FY08



	FY03	FY04	FY05	FY06	FY07	FY08
10 th Percentile	\$1,150	\$1,080	\$1,130	\$1,450	\$1,910	\$2,360
25 th Percentile	\$1,130	\$950	\$930	\$1,130	\$1,510	\$1,850
Median	\$1,100	\$840	\$700	\$770	\$1,040	\$1,310
75 th Percentile	\$1,070	\$660	\$440	\$420	\$550	\$660
90 th Percentile	\$0	\$0	\$0	\$20	\$0	\$0

Data as of 12/31/02

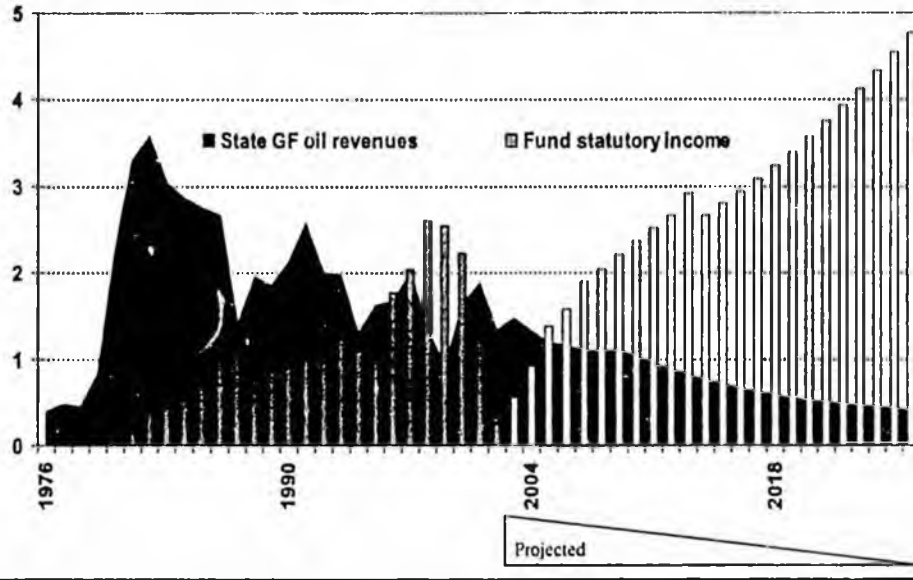
Alaska Permanent Fund Corporation



Focusing on the long term

The relationship of Permanent Fund statutory income vs. General Fund oil revenues

Billions



2003 Capital Market Outlook Legislative Work Session

Michael J. O'Leary CFA
Executive Vice President
Callan Associates Inc.
February 2003



Longest Equity Bear Market Since 1930's

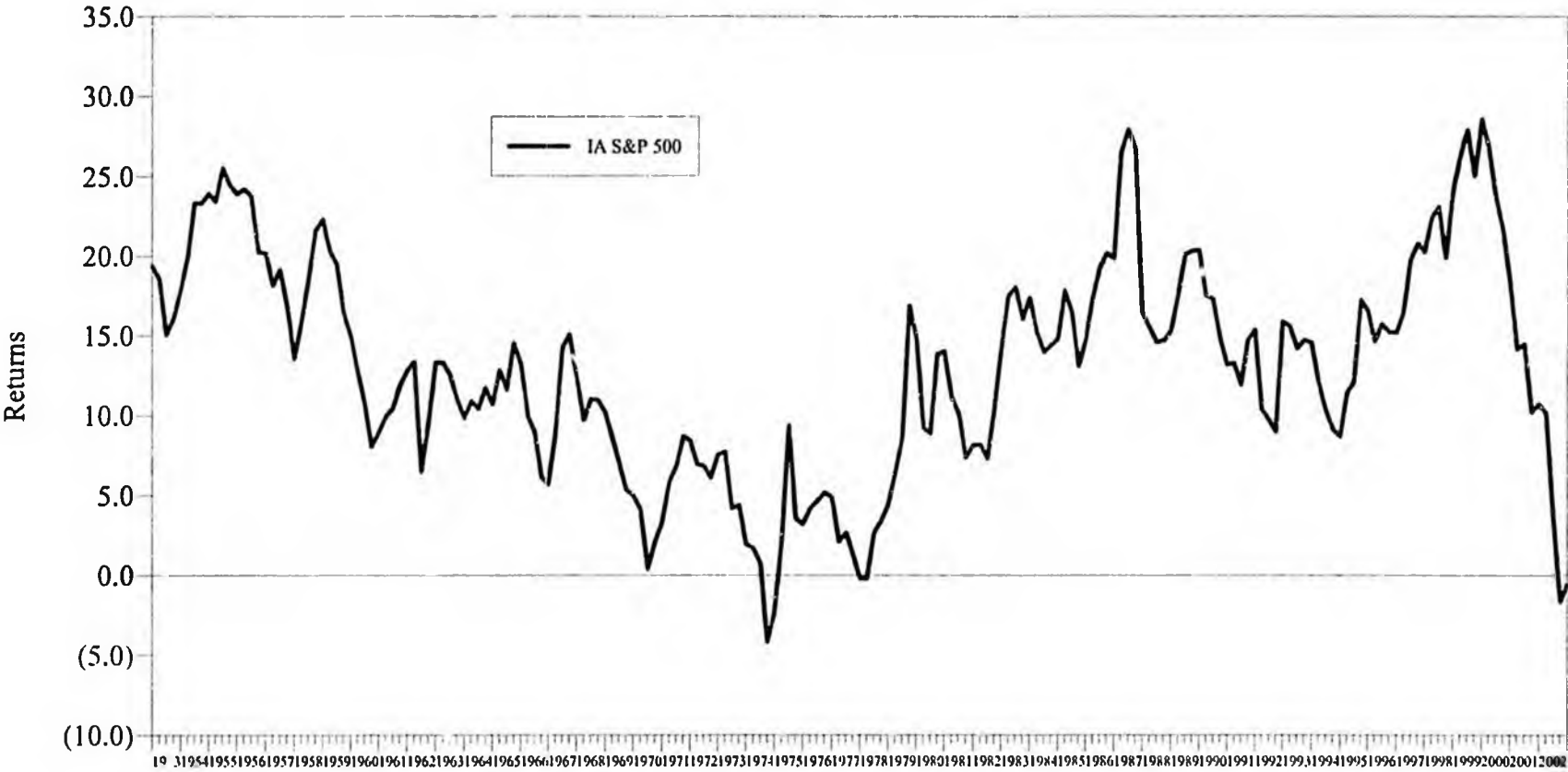
Roles of the 90s Reverse as Bonds Rule

	<u>2000 Returns</u>	<u>2001 Returns</u>	<u>2002 Returns</u>
Russell 3000	-7.46	-11.46	-21.54
S&P Super Composite 1500	-6.98	-10.64	-21.31
Russell 1000	-7.79	-12.45	-21.65
S&P 500	-9.10	-11.88	-22.10
Russell 2000	-3.02	2.49	-20.48
S&P 600 Small Cap	11.80	6.54	-14.63
EAFE (\$US)	-14.17	-21.44	-15.94
LB Aggregate	11.63	8.43	10.25
SB Non-US Bonds	-2.63	-3.54	21.99



Rolling 5 Year Returns for Stocks

Rolling 20 Quarter Returns
for 50 Years Ended December 31, 2002



Cumulative Return Comparison Table

Stocks, Bonds & Cash

Important to Keep Perspective

Return for Periods Ended December 31, 2002

	5 Years	10 Years	20 Years	30 Years	40 Years
Cash	4.49	4.61	5.94	6.96	6.36
Bonds	7.44	6.91	8.74	8.51	7.52
Stock	-0.59	9.34	12.71	10.68	10.49

Growth of a \$ for Periods Ended December 31, 2002

	5 Years	10 Years	20 Years	30 Years	40 Years
Cash	1.25	1.57	3.17	7.53	11.80
Bonds	1.43	1.95	5.35	11.59	18.15
Stock	0.97	2.44	10.94	20.99	54.14



The Current Economic Environment

- The recession is over, but what will the recovery look like?
- Economy is growing, but unemployment is stuck at 6%
- Business investment continues to be weak
- Treasury bonds yields are at their lowest in 40-years, due to:
 - Aggressive Fed action to lower interest rates
 - Investors exiting equity in favor of bonds, driving yields lower
- Credit spreads and equity risk premium are higher than normal
- Disappearing federal surplus and higher state and local deficits
- However:
 - inflation fell from 3% to 1.5%
 - tax cuts and lower interest rates freed up funds for the consumer
 - consumers keep spending, housing and cars sales surged
 - government is also spending to boost the economy
 - confidence is recovering



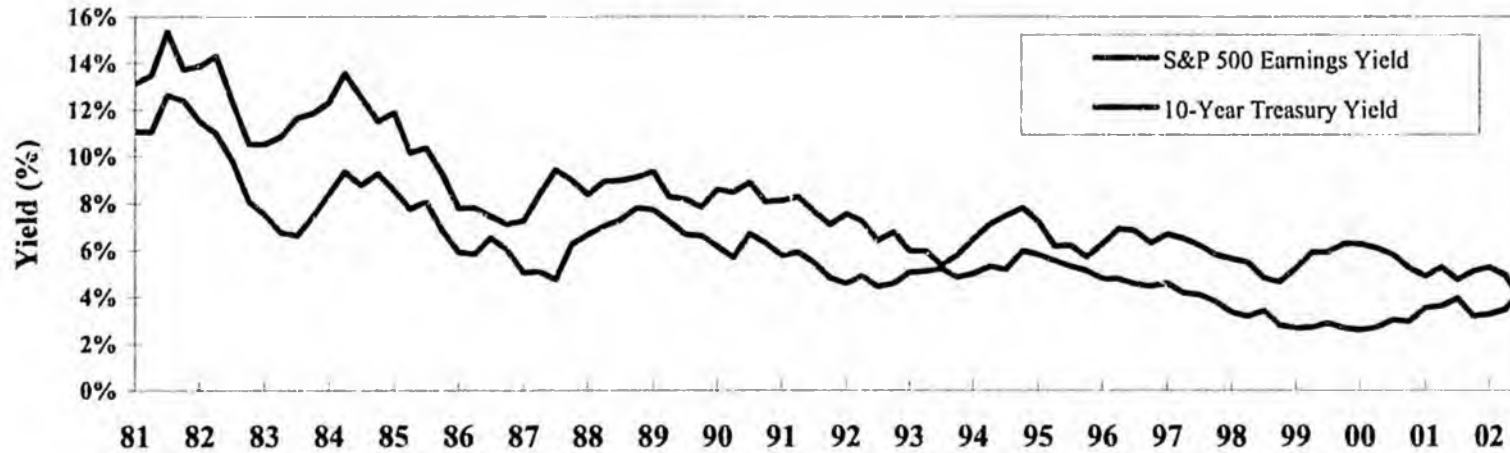
Domestic Fixed Income

Lehman Aggregate Index - Daily Yield to Worst from 1/1/01 to 12/31/02

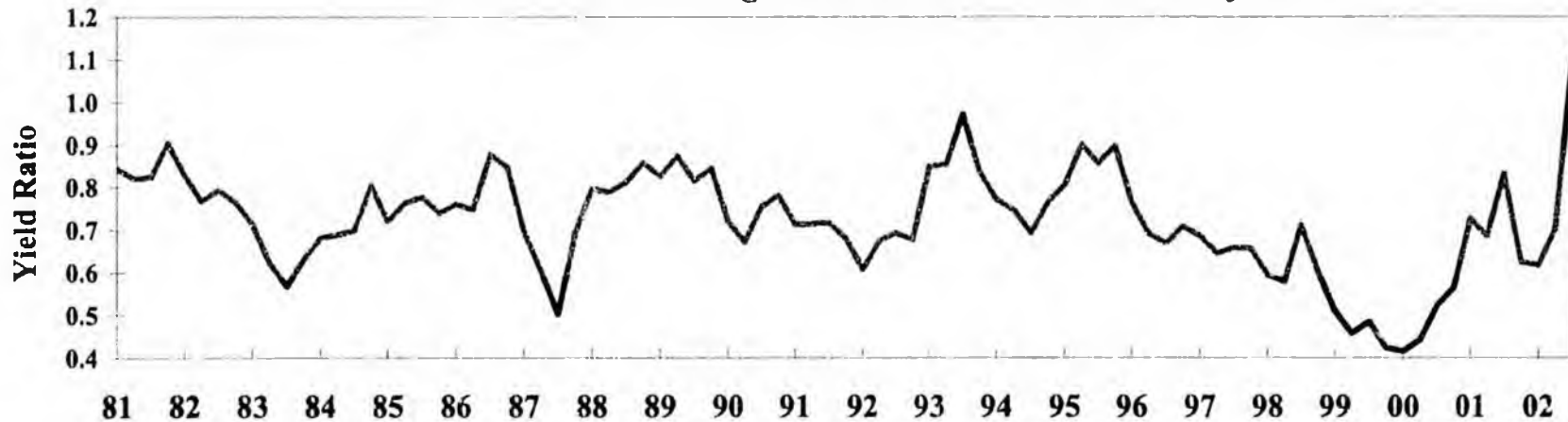


Domestic Equity vs. Bond Yields

S&P 500 Earnings Yield vs. 10-Year Treasury Yield



Ratio of S&P 500 Earnings Yield and 10-Year Treasury Yield

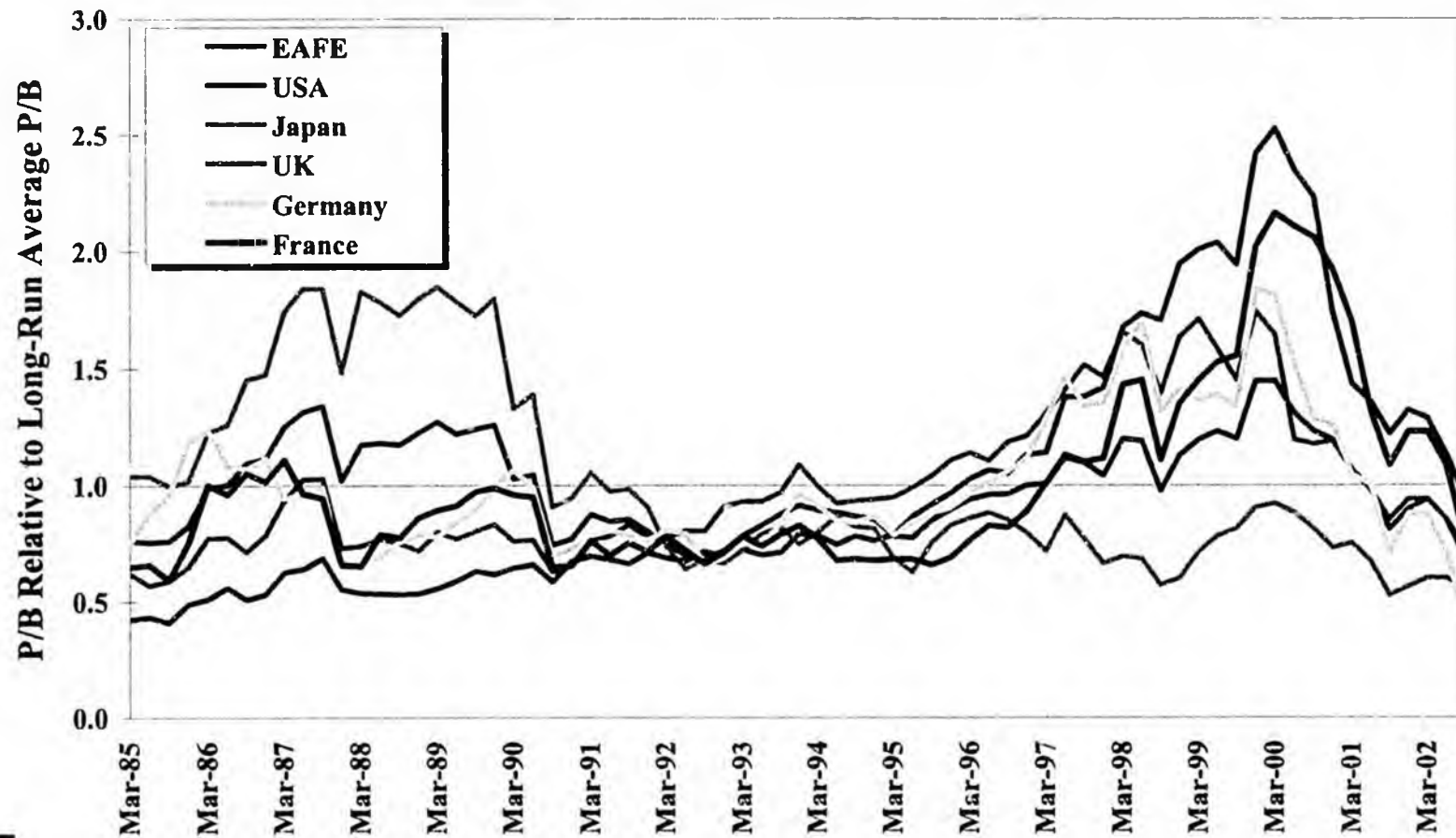


*trailing reported earnings used for S&P 500



U.S. Market Still Expensive Compared to the Rest of the World

Price/Book Value Relative to Long-Run Average
for Major EAFE Countries and USA



2003 Capital Market Projections

- Economic recovery will continue, but slowly.
- Inflation will remain low, but little risk of deflation.
- Consumer spending will slow, in line with disposable income.
- Fiscal stimulus from the Feds will help, but state and local governments will be cutting back.
- Surplus is gone --- higher Treasury yields at the shorter end.
- Feds will ultimately shift to tightening monetary policy.
- Capital spending will follow GDP growth.
- Stock market recovery will be slow.
- Housing market will start to cool.

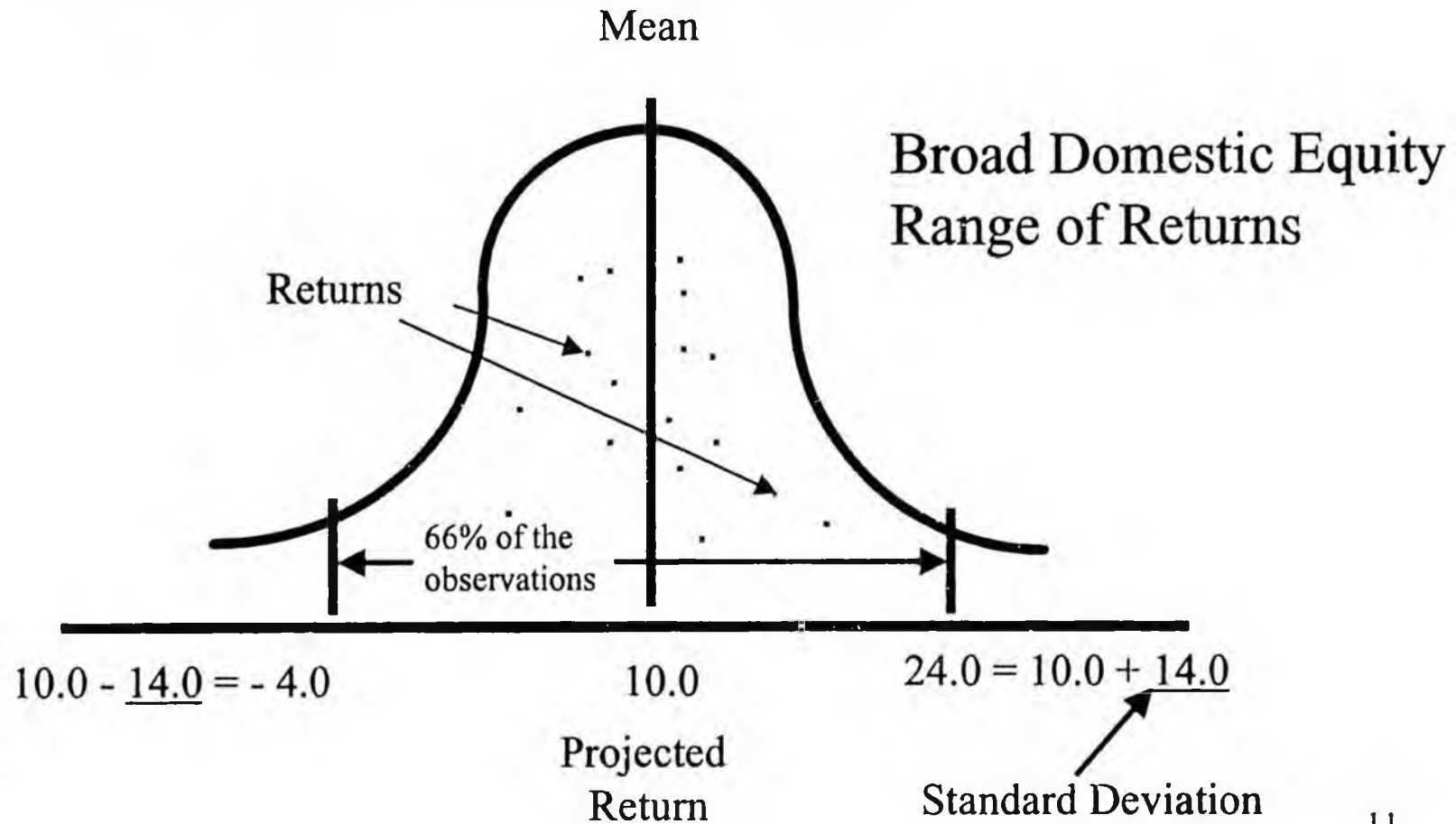
2003 Capital Market Projections

- General decline in expected returns across all asset classes, stemming from lower inflation and lower bond yields.
- Inflation is lowered by 0.3%, but still depicts inflation rising from current low levels.
- Cash returns reflect rising short-term yields, but still low real return of 0.4%
- Bond returns lowered from 5.75% to 4.75% :
 - reflects current yield-to-worst, plus small adjustment
 - build in moderate increase in short rates, relatively stable long rates, narrowing of credit spreads.
- Equity returns built from fundamentals: 3-4% real GDP growth, 2% dividend yield, 0.5%-1% “buyback” yield.
- Real estate lowered from 8% to 7.6%, reflecting lower inflation and further declines in residential and nonresidential valuations.
- Private equity lowered to 12%, primarily due to weaker venture capital sector.



MEASURING RISK

- Standard Deviation - Measures the Variability of Returns from Their Mean



MEASURING RISK

An Illustration

Expected Annual Return = 10.0 %

Standard Deviation of Return = 14.0 %

2 out of 3 years, the return is expected to fall within a range of one standard deviation = -4.0 to 24.0%

95% of the time, the return is expected to fall within a range of two standard deviations = -18.0 to 38.0%



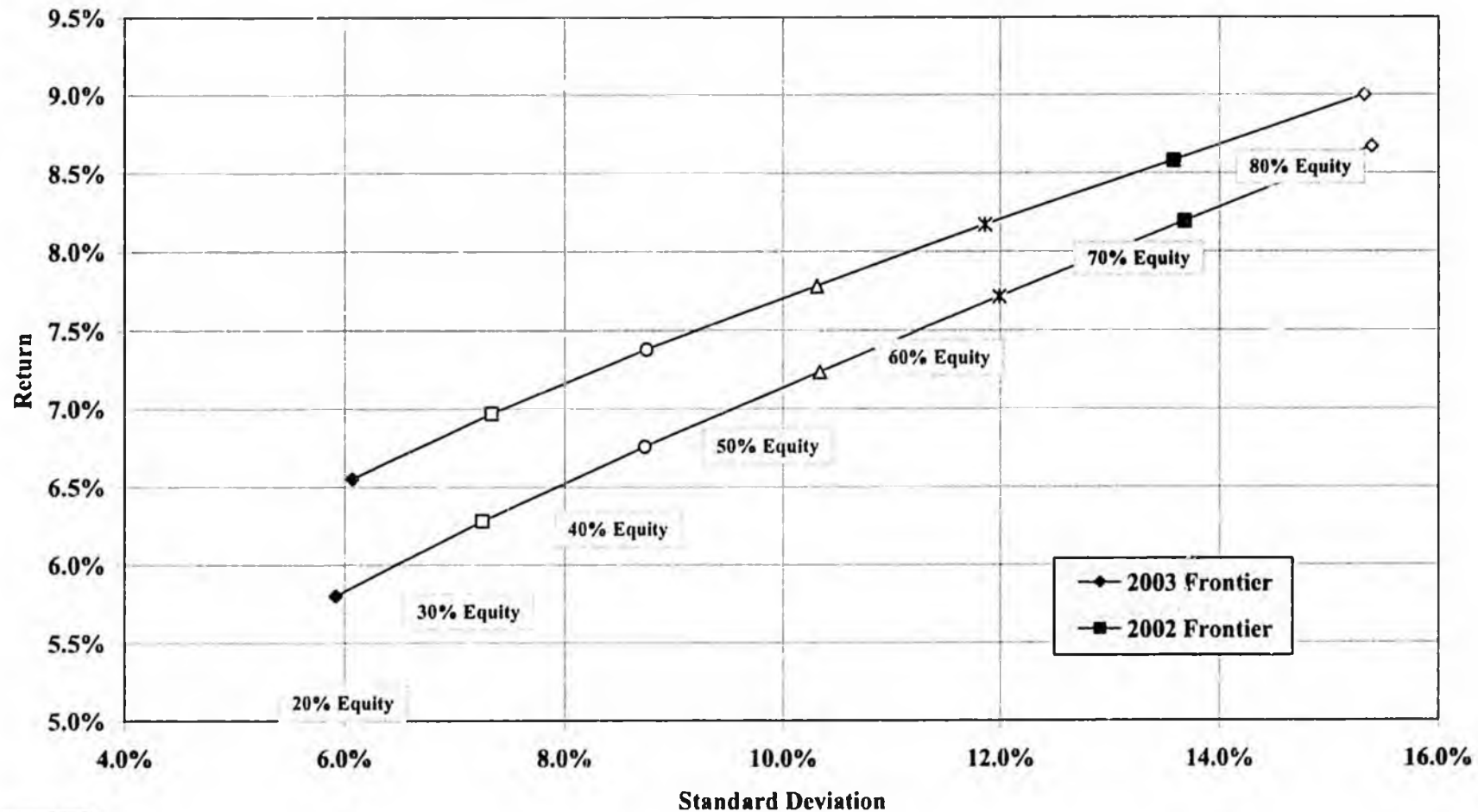
2003 Capital Market Projections

Asset Class	Index	Projected Annual Return	Projected Standard Deviation (Risk)	2003 "Sharpe"	2002 Projections		2002 "Sharpe"
Equities							
Broad Domestic Equity	S&P 1500	9.00%	17.30	0.34682	9.30	17.20	0.33721
Large Cap	S&P 500	8.70%	16.20	0.35185	9.00	16.00	0.34375
Small Cap	S&P 1000	10.30%	25.00	0.29200	10.60	25.00	0.28400
International Equity	EAFE	9.60%	21.50	0.30698	9.90	21.50	0.29767
Fixed Income							
Domestic Fixed	LB Agg	4.75%	4.50	0.38889	5.75	5.00	0.45000
Non US\$ Fixed	SB Non US	4.65%	9.60	0.17188	5.60	9.60	0.21875
Other							
Real Estate	CRES	7.60%	16.50	0.27879	8.00	16.50	0.27273
Alternative Investments	VECO FVCI	12.00%	34.00	0.26471	12.25	35.00	0.25000
Cash Equivalents	T-bill	3.00%	0.70		3.50	0.70	
Inflation	CPI-U	2.60%	1.00		2.90	1.00	



Lowered Expectations - Asset Mixes With Comparable Equity Exposure Offer Less Return

Efficient Frontier (Alternative Investments Excluded)



What Can Go Wrong?

Risks on the Horizon

- Largest risks come from outside the economy:
 - Further terror attacks, or
 - War with Iraq, North Korea, other agents of terrorism
- Risks remain within the US
 - Stagnating economy
 - Collapsing housing market kills consumer enthusiasm for spending
 - Inflation takes off, crushing the bond market

Applying the Projections to the APFC

APFC Target Mix versus Unconstrained Efficient Frontier

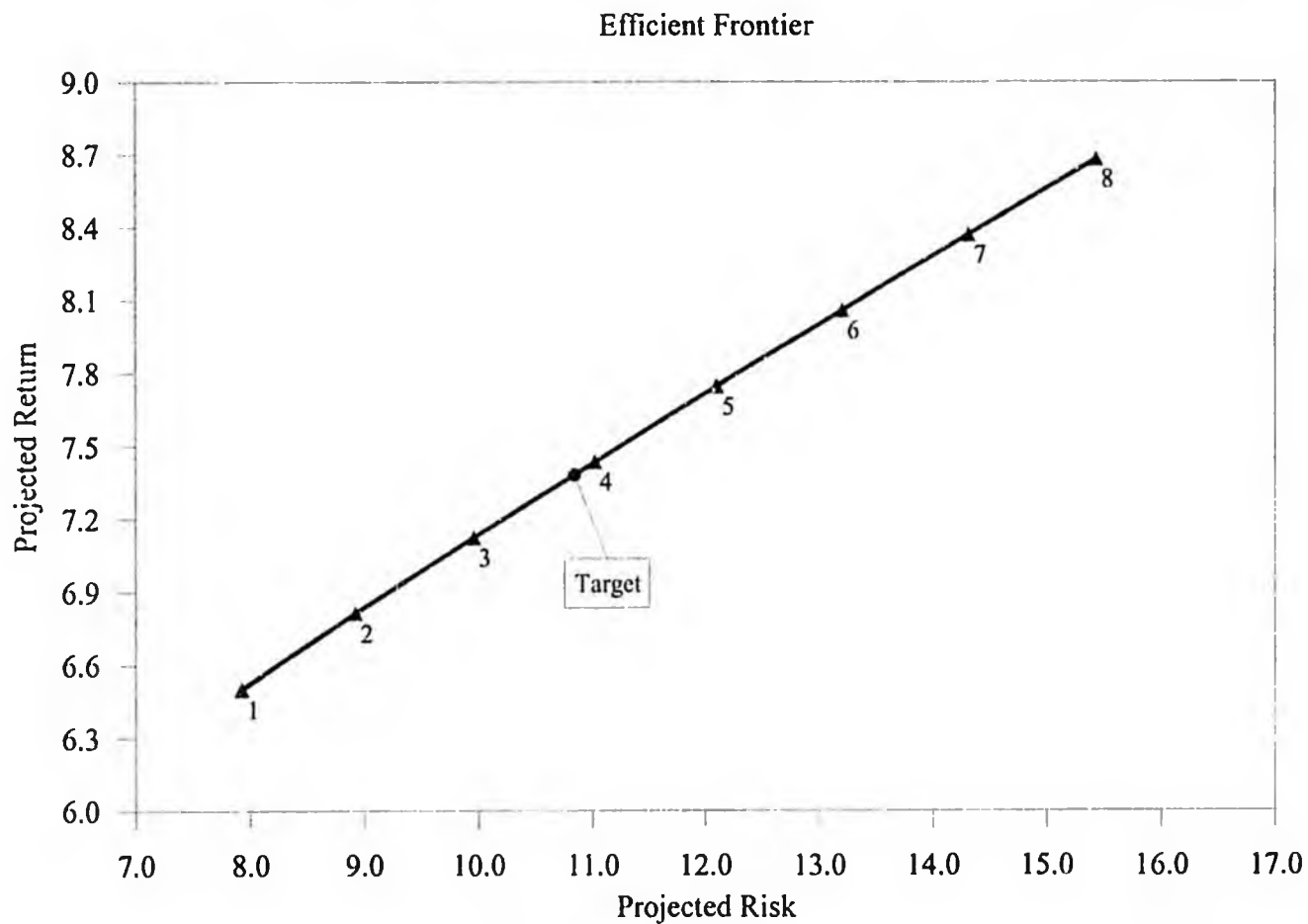
Target is essentially on the efficient frontier near mix 4

Optimal Portfolios

Portfolio Component	Target Mix	Limits		Asset Mix Alternatives							
		Min	Max	1	2	3	4	5	6	7	8
Broad	37%	0%	100%	25%	29%	33%	38%	42%	46%	50%	54%
Int'l Eq	16%	0%	100%	10%	12%	15%	17%	19%	21%	24%	26%
LB Agg	35%	0%	100%	53%	46%	39%	33%	25%	19%	13%	6%
NUS Bond	2%	0%	100%	5%	5%	4%	3%	3%	2%	1%	1%
Real Est	10%	0%	100%	7%	8%	9%	10%	11%	11%	12%	13%
T-Bills	0%	0%	100%	0%	0%	0%	0%	0%	0%	0%	0%
Totals	100%			100%	100%	100%	100%	100%	100%	100%	100%
Median	7.38%			6.50%	6.81%	7.12%	7.43%	7.75%	8.06%	8.37%	8.68%
Std Dev	10.84%			7.92%	8.92%	9.96%	11.02%	12.10%	13.20%	14.31%	15.43%

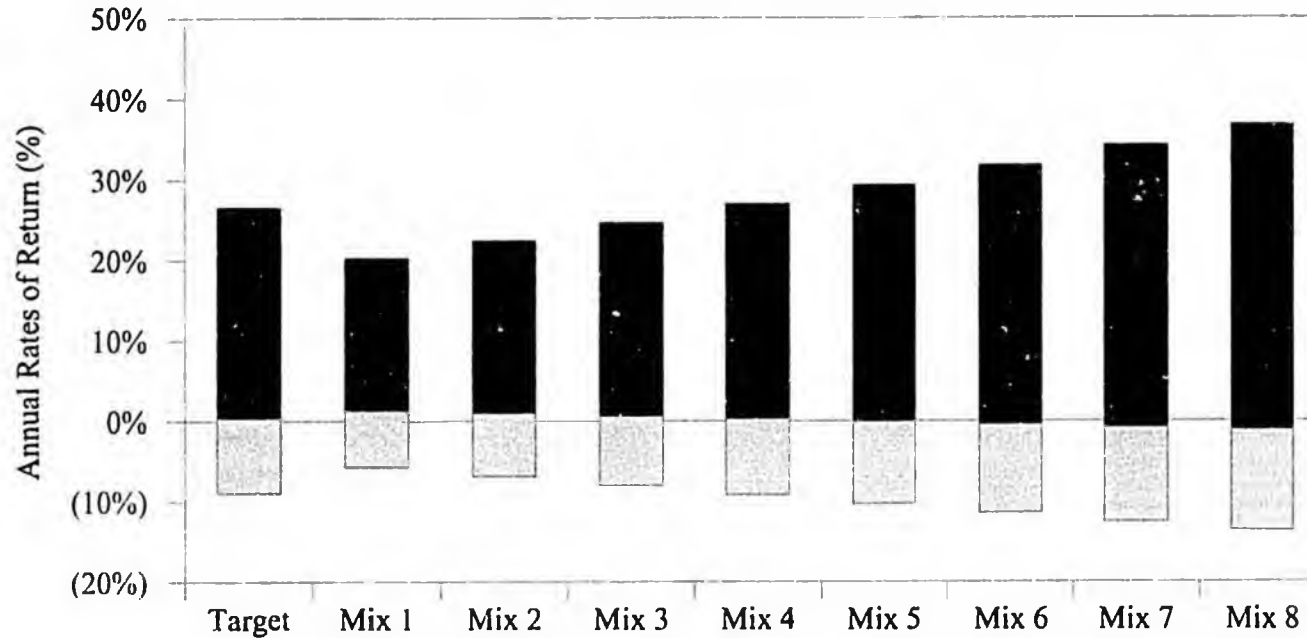


Target Mix Versus Unconstrained Frontier



Range of returns One Year Period

Range of Projected Rates of Return
Projection Period: 1 years

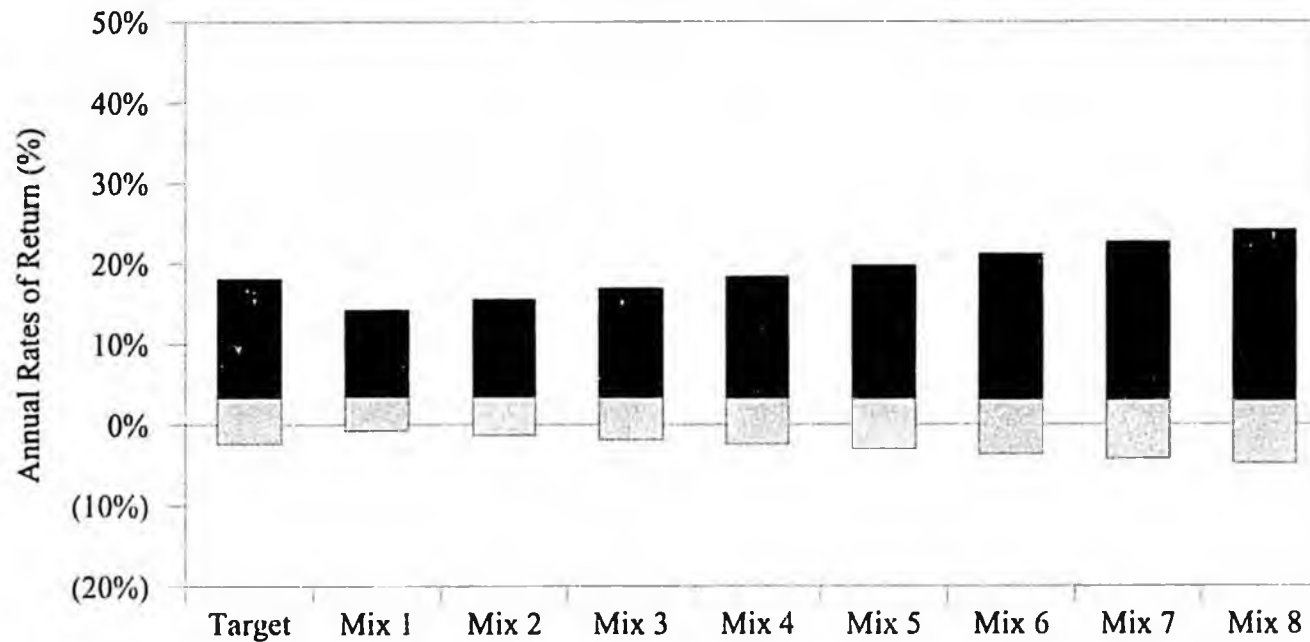


	Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5	Mix 6	Mix 7	Mix 8
5th Percentile	26.62%	20.30%	22.45%	24.70%	27.01%	29.39%	31.82%	34.29%	36.81%
25th Percentile	14.89%	11.96%	12.97%	14.01%	15.07%	16.15%	17.23%	18.33%	19.44%
Median	7.38%	6.50%	6.81%	7.12%	7.43%	7.75%	8.06%	8.37%	8.68%
75th Percentile	0.37%	1.31%	0.99%	0.65%	0.31%	(0.05%)	(0.40%)	(0.76%)	(1.11%)
95th Percentile	(8.93%)	(5.72%)	(6.83%)	(7.97%)	(9.13%)	(10.28%)	(11.42%)	(12.55%)	(13.66%)



Range of returns Three Year Period

Range of Projected Rates of Return
Projection Period: 3 years

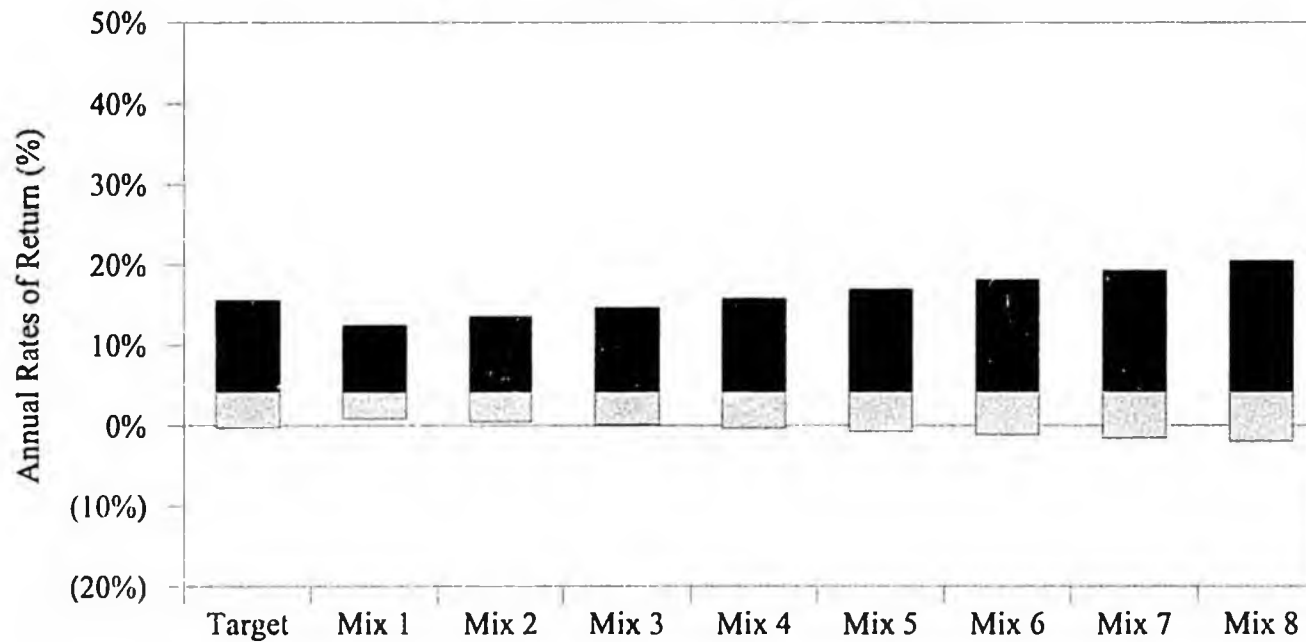


	Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5	Mix 6	Mix 7	Mix 8
5th Percentile	18.10%	14.26%	15.58%	16.94%	18.34%	19.76%	21.20%	22.65%	24.13%
25th Percentile	11.65%	9.62%	10.32%	11.05%	11.78%	12.52%	13.26%	14.01%	14.77%
Median	7.38%	6.50%	6.81%	7.12%	7.43%	7.75%	8.06%	8.37%	8.68%
75th Percentile	3.27%	3.47%	3.41%	3.34%	3.26%	3.18%	3.09%	3.00%	2.92%
95th Percentile	(2.36%)	(0.74%)	(1.29%)	(1.87%)	(2.46%)	(3.06%)	(3.66%)	(4.25%)	(4.84%)



Range of returns Five Year Period

Range of Projected Rates of Return
Projection Period: 5 years

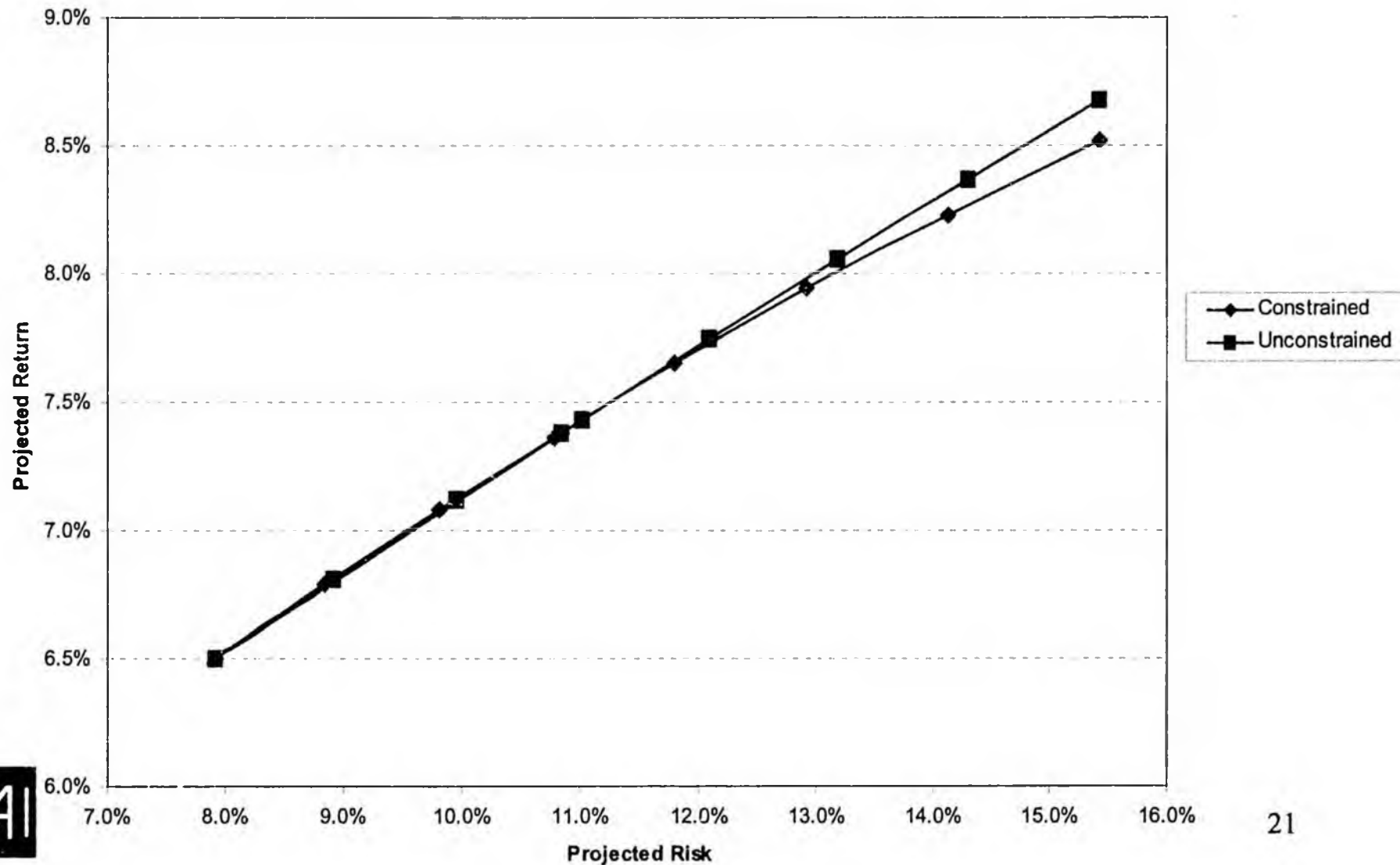


	Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5	Mix 6	Mix 7	Mix 8
5th Percentile	15.59%	12.47%	13.54%	14.65%	15.79%	16.94%	18.10%	19.28%	20.46%
25th Percentile	10.68%	8.91%	9.52%	10.15%	10.78%	11.42%	12.07%	12.72%	13.37%
Median	7.38%	6.50%	6.81%	7.12%	7.43%	7.75%	8.06%	8.37%	8.68%
75th Percentile	4.18%	4.15%	4.17%	4.18%	4.19%	4.19%	4.19%	4.19%	4.19%
95th Percentile	(0.25%)	0.85%	0.48%	0.09%	(0.32%)	(0.72%)	(1.13%)	(1.54%)	(1.95%)



Comparison of constrained vs. unconstrained

Efficient Frontier



Conclusions

- Current policy is consistent with goals of
 - maximizing return subject to statutory limitations on total equity exposure
 - diversifying to achieve maximum return per unit of risk (i.e. the policy is “efficient”)
- Policy does not produce 5% expected real return
 - significant decline in level of interest rates and low embedded real return projection (4.75% minus 2.6% inflation = 2.15% expected real return on bonds)



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ALASKA PERMANENT FUND

Maturity · Balance · Permanence

Brady, Frank and Renkes appointments complete APFC

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QUARTERLY



ANNUAL REPORT



FUND HISTORY



Board of Trustees

A six-person Board of Trustees sets policy for the Alaska Permanent Fund Corporation. The governor appoints four members from the public and two members - including the Commissioner of Revenue - from the cabinet. The public members serve staggered four-year terms. **Click here for a complete listing of all current and former Trustees.**



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Chair

✓ **Clark S. Gruening**
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Robert Stanger Storer
David Teal, R.

Allan Moore
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Directors

Subject: [Fwd: Finance Meeting 2/12/03]

Date: Tue, 11 Feb 2003 15:20:26 -0900

From: Mindy Rowland <Mindy_Rowland@legis.state.ak.us>

Organization: Alaska State Legislature

To: Ryelyn Rader <Ryelyn_Rader@legis.state.ak.us>, Robin Paul <Robin_Paul@legis.state.ak.us>

Subject: Finance Meeting 2/12/03

Date: Tue, 11 Feb 2003 15:16:18 -0900

From: Marty Meyer <Marty_Meyer@Legis.state.ak.us>

Organization: Alaska State Legislature

To: Sheila Peterson <Sheila_Peterson@legis.state.ak.us>, Mindy Rowland <Mindy_Rowland@legis.state.ak.us>

Ladies,

Here's the list of Majority Senators who are not on the Finance Committee which I called to see if they would like to sit at the Finance Table at the 9:00AM meeting on 2/12/03.

- ✓ Sen. Cowdery - yes, sit at table
- ✓ Sen. Dyson - yes, sit at table
- ~~Sen. Ogan - yes, sit at table~~
- ✓ Sen. Taylor - yes, sit at table
- ~~Sen. Therriault - no, will not be there~~
- ✓ Sen. Wagoner - Amy (his aide) ~~said it's very unlikely he will be there~~

Sen Seekins- ???? (Let's plan that he will be there, but if he doesn't show up, we will take his name plate away)

Have I missed anyone?

Thanks
Marty

✓ Sen. French