STATE OF NEW JERSEY
DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT

Annual Report

For Fiscal and Calendar Year 2007

A report of the Division of Investment, Department of the Treasury, State of New Jersey for the fiscal year ended June 30, 2007 and calendar year 2007. A separate fiscal year report is also prepared for the State of New Jersey Cash Management Fund, available upon request from the Division at (609) 984-4187.

This annual report can be accessed on our website: www.state.nj.us/treasury/doinvest

State of New Jersey
Department of Treasury
Division of Investment
William G. Clark, Director
Mailing Address: 50 W. State Street, P.O. Box 290, Trenton, NJ 08625-0290
Offices: 50 W. State St., 9th Floor, Trenton, NJ 08608
General Telephone: (609) 292-5106

Graphics and Layout by Linda Thompson

Table of Contents

Photo courtesy of John Ignatowitz

New Jersey Division of Investment

2008 Winner of the

Wall Street Hall of Fame Award, National Association of Securities Professionals

And the

Large Public Plan of the Year Award, Money Management Letter

To the Honorable Governor, Legislators and State Treasurer and Citizens of New Jersey:

This Annual Report provides detailed information on the legal structure and oversight of the investment management of the State's Pension Fund, along with information on investment activity and performance for the fiscal and calendar year 2007.

The State of New Jersey maintains seven pension funds (collectively referred to in this report as the "Pension Fund") that provide retirement benefits to various public sector employees. The Pension Fund is intended to provide retirement benefits to more than 700,000 active and retired employees. This is a responsibility that we take very seriously.

While the State Investment Council and the Division of Investment are separate entities, they work together in order to manage these Pension Fund assets. Quite simply, the State Investment Council sets the investment policy for the portfolio, and the Division of Investment implements that policy. This letter discusses the recent changes made in the Council's investment policy and the investment results for the fiscal year 2007. Finally, we offer comments on changes in the investment environment occurring after fiscal year 2007 and how these changes have, and likely will, impact the portfolio.

"New Jersey was one of the first public pension funds to invest in U.S. common stocks. While critics of this approach viewed this shift as 'too risky,' this change positioned New Jersey as one of the top-performing funds."

<u>**Changes to Investment Policy**</u>

In the early 1980s, New Jersey was one of the first public pension funds to invest a significant portion of its portfolio in U.S. common stocks. While critics of this approach viewed this shift as "too risky," this change positioned New Jersey as one of the top-performing pension funds in the country for many years. In 1991, the Council took another innovative, yet controversial step – authorizing investment in international stocks and bonds. In doing so, the Council sought to achieve two important objectives: to capitalize on the potential for strong economic growth outside of the United States, and to diversify the portfolio (i.e., reduce the risk level) by adding a new asset class that would not necessarily move in tandem with U.S. equities.

Helped by a long-term bull market (which was spurred by a multi-year decline in inflation and interest rates, among other things) the Division's strategy led to strong investment returns for many years. In fact, from 1995 to 1999, New Jersey's pension plan returned an average of 27.96 percent per year, ranking it among the top of all public pension funds during that period.

However, after leading in strong investment returns and reducing fund risk by diversifying its portfolio with new asset classes, New Jersey opted to stay the course and hold its asset allocation constant, rather than move into newer asset classes, such as private equity and real estate. With the bursting of the "internet bubble" in late 2000-2001, the S&P 500 lost 12.8 percent and16.5 percent for the period from July 1, 2000-June 30, 2001 and July 1, 2001-June 30, 2002, respectively. During these two fiscal years, New Jersey's portfolio was down 9.0 percent and 10.4 percent, respectively, resulting in net investment loses during those years of $8 billion and $6 billion.

While it is not always advisable to compare ourselves with other public funds, there can be no argument that other funds, most of which continued to diversify into other asset classes, have significantly out-performed New Jersey on a risk-adjusted basis over five-, 10- and 15-year periods – and that performance was attributable to superior asset allocation policies. While New Jersey had solid relative performance in each of its major portfolios during that period, New Jersey's performance was in the bottom quartile relative to other public funds according to a 2007 national Public Fund Universe Report by R. V. Kuhns & Associates.

"Other public funds…which continued to diversify into other asset classes...outperformed New Jersey…the Council's conclusion was that the plan's asset allocation needed to be adjusted."

Starting in 2003, the State Investment Council began to re-evaluate the plan's asset allocation, undertaking the plan's first asset/liability study in nearly 25 years. Following multiple studies by independent consultants, the Council's conclusion was that the plan's asset allocation needed to be adjusted, and starting in the fiscal year ending on June 30, 2006, the Council made several adjustments to the portfolio's asset allocation. The major changes adopted include the following:

- A significant reduction in the allocation to domestic equities to reduce risk, while slightly increasing the allocation to international equities, particularly equities domiciled in so-called emerging markets countries, which as a group is expected to experience stronger economic growth than domestic markets.

- Initiating investments in private equity, the only new asset class in the portfolio expected to out-perform public equities over the long-term. The target allocation for private equity on an invested basis is 5 percent by 2010-2012.

- Initiating investments in real estate, with a target allocation of 4 percent by 2010-2012.

- Initiating investments in hedge funds as a means to generate positive returns that have a low correlation to public equities. The current target for the hedge fund portfolio, which is diversified by investment strategy, is 6 percent of assets.

- Initiating an inflation-sensitive portfolio as a means to hedge the Pension Fund against any potential increase in inflation in the U.S. As you may know, inflation is a major risk in a pension fund like New Jersey's where benefits are initially set as a percent of an employee's final average salary (which is indirectly influenced by inflation), and benefit payments are adjusted upwards by a percentage of the Consumer Price Index (CPI). The portfolio's desired allocation to inflation sensitive assets includes a 4 percent allocation to commodities and other real return assets (e.g., timber, infrastructure) and a 3 percent allocation to U. S. Treasury Inflation Protected Securities (TIPS).

- In recognition of the fact that the plan's liabilities are long-term in nature, we've sought to extend the duration (i.e., the average maturity) of the fund's fixed income portfolio from roughly five to more than 10 years.

Based on theoretical expected returns for each asset class in the portfolio, these changes are not designed to necessarily result in significantly higher returns for the portfolio. Rather, we expect to generate *comparable to slightly higher* returns than the former portfolio, but with a significantly lower level of risk (i.e., volatility of returns).

"We expect (these changes) to generate comparable to slightly higher returns than the former portfolio, but with a significantly lower level of risk."

Investment Results for Fiscal Year 2007

We are pleased to report that the portfolio's performance for the fiscal year ended June 30, 2007 was 17.1 percent, which exceeded our portfolio benchmark of 15.6 percent. More importantly, the Investment Division's performance in each of the four major portfolios – domestic equity, domestic fixed income, international equity and money markets – all exceeded their respective benchmarks for the fiscal year.

We briefly touch on the results and activity in each portfolio below. For more detailed information about each portfolio, please review the information and financial statements that follow this letter in the Annual Report.

***Domestic Equity*:** Performance for this portfolio (Common Pension Fund A) was 21.0% for the fiscal year, versus 20.2% for the S&P 1500 Composite Index, the benchmark for this portfolio. The main factors contributing to our out-performance were superior stock selection within the technology sector and underexposure to commercial banks and thrifts in the portfolio.

For the fiscal year, we had net sales of nearly $10.8 billion throughout the portfolio. These funds were used to make investments in other areas of the portfolio (primarily alternative investments) and to make benefit payments to retirees from the various pension plans.

As of June 30, 2007, the domestic equity portfolio had a market value of $31.5 billion, representing 38.3% of the overall portfolio. While the portfolio is broadly diversified across all economic sectors, the portfolio composition incorporates several major deviations from the overall market. In particular, the portfolio was underexposed to the financial services (discussed below) and consumer discretionary sectors, while having a higher exposure than the overall market to the energy and technology sectors.

***Domestic Fixed Income*:** This portfolio underwent a major transition, with its overall duration being extended from roughly five to nearly eight years during the fiscal year. Portfolio performance for the fiscal year was 5.2 percent, versus 4.4 percent for the Division's benchmark for the year (which was a blend of the Lehman Government/Credit Index and the Lehman Long Government/Credit Index).

"The portfolio's performance for the fiscal year ended June 30, 2007 was 17.1 percent, which exceeded our portfolio benchmark of 15.6 percent."

The market value of the portfolio as of June 30, 2007 was $20.9 billion. While the portfolio is well diversified, we made a conscious decision to be underexposed to corporate bonds, particularly those with credit ratings of BBB/Baa (the lowest ratings within the "investment grade" corporate bond market). In lieu of holding corporate bonds, the portfolio was overexposed to U.S. Treasury securities and mortgage-backed securities guaranteed by either the U.S. Government (i.e., GNMAs) or one of the government-sponsored enterprises (GSEs, meaning either the Federal National Mortgage Administration or the Federal Home Loan Mortgage Corporation). Please note that the portfolio had no ownership of securities backed by sub-prime mortgages.

***International Equity*:** The portfolio returned 28.5 percent for the fiscal year, versus 27.3 percent for the MSCI-EAFE index adjusted for those issues that are not eligible for purchase under the State's Sudan divestment law. The much stronger returns for international equities were partially attributable to a decline in the U.S. dollar relative to other foreign currencies (particularly the Euro).

Net purchases for the fiscal year were $758 million, consisting primarily of stocks in the consumer staples sector. As of June 30, 2007, the portfolio was overexposed to stocks in the media, luxury goods, machinery and infrastructure industries. The portfolio was underexposed to stocks in the commercial banking, metals/mining, telecommunications/utilities industries.

***Money Market*:** The State of New Jersey's Cash Management Fund returned 5.47 percent for the year, versus 5.06 percent for 90-day U.S. Treasury bills (the benchmark for the Fund).

As of June 30, 2007, the portfolio had a yield of 5.2 percent, with an average maturity of 62 days. The portfolio consists predominantly of bank certificates of deposit and U.S. Treasury bills.

***Alternative Investments*:** While performance statistics for an alternative investment portfolio in its early stages of development are not terribly valuable given their limited history, we note that the net returns (after fees) for the three major asset classes within the alternatives portfolio were as follows: 13.7 percent for private equity, 16.5 percent for real estate and 13.2 percent for hedge funds.

For private equity, the Division announced commitments of $4.8 billion through June 30, 2007 to 47 different partnerships. The actual amount invested in the program through June 30, 2007 was $1.1 billion. While the portfolio is well-diversified by investment strategy, we have attempted to de-emphasize the large U.S. buyout funds and to concentrate on debt-oriented strategies and international buyout funds.

"Net returns (after fees) for the three major asset classes within the alternatives portfolio were 13.7 percent for private equity, 16.5 percent for real estate and 13.2 percent for hedge funds."

Within real estate, we announced commitments of approximately $2.6 billion to 33 different partnerships as of June 30, 2007. The actual amount invested through fiscal year-end was $900 million. While the portfolio is also well-diversified by strategy, we have de-emphasized core real estate (given concerns about excessive market valuation) and instead have sought opportunities in opportunistic strategies in the U.S. and international real estate.

For the hedge fund portfolio, we announced commitments of $2.8 billion to 24 different funds, with actual investments of $2.3 billion as of June 30, 2007. While the portfolio initially concentrated on investing in fund of funds strategies (a fund managed by an investment advisor that invests in a number of underlying hedge funds), over the past year the Division has sought to make direct investments in a number of top-performing funds.

Discussion Of Subsequent Developments in the Financial and Equity Markets

For some time, the Council and Division had been concerned that the financial markets were mis-pricing risk across a wide range of financial assets. This concern was made evident by the historically low-risk premia embedded in the market values for structured financial products, corporate bonds, certain equity securities (particularly those in the financial services sector), and emerging market equities and debt.

The cause of this mis-pricing is still being debated in financial circles. Many experts believe that unsustainably low short-term interest rates in the U.S. created an environment where investors had incentive to reach for higher returns in a variety of higher-risk securities. The large U.S. current account deficit, coupled with the high savings rates of many of our trading partners, has resulted in large and growing accumulations of wealth held by foreign governments and private institutions. This large growth in liquidity no doubt contributed to a general re-pricing of certain asset classes as well.

As the demand for debt instruments offering higher yields grew, the U.S. financial services sector responded by growing new bases of borrowers and creating new types of financial instruments. The largest debt creation came in the U.S. mortgage market, where new products were designed to make home ownership possible for a new class of borrowers – those with inferior credit histories and/or speculators in real estate. The other major type of debt was in the form of "leveraged loans," or loans to private equity funds to finance leveraged buyouts of various businesses around the world. Since most of this debt was in the form of variable-rate loans with interest rates tied to short-term interest rates, borrowers were able to finance abnormally large levels of debt. In the housing market, the assumption was that when rates on mortgages reset to higher levels, the borrowers could refinance based on further home price appreciation.

"Because of our concerns about (structured financial products…especially in the mortgage area)… we took prudent steps to minimize our exposure to the potential unwinding."

New types of structured financial products allowed the financial services sector to package this debt into securities that could be sold to investors around the globe. Especially in the mortgage arena, securities were created en masse with credit ratings that were not (in hindsight) reflective of the true creditworthiness of the underlying collateral. Because the banks, brokers and other entities that originated these loans had no intention of keeping the debt on their balance sheets, there was inadequate attention paid to credit standards and/or risk management principles associated with these new forms of debt. This was an accident waiting to happen, and it did.

Because of our concerns about these trends, we took prudent steps to minimize our exposure to the potential unwinding of these excesses. The portfolio did not have any exposure to the various securities and debt held by many other pension funds that have re-priced and experienced significant market value losses in recent months: CDOs, CLOs, sub-prime mortgages, leveraged loans, asset-backed commercial paper. We also were significantly underexposed to stocks in the financial services sector, particularly those of commercial banks and thrifts that were most tied to the growth in the sub-prime mortgage market. Finally, our fixed income portfolio was significantly under-exposed to corporate bonds in general. The Division believed that spread levels (i.e., the incremental yield over U.S. Treasuries of comparable maturities) had become too narrow.

As of the date of this letter, worldwide investment losses that have been announced by financial services companies are approaching $300 billion. We suspect that ultimate losses will be significantly higher. In order to maintain their franchises, many financial services firms have raised additional capital from investors. The major investors in these issues have been sovereign wealth funds, but our pension fund has also participated in several of these transactions where terms were attractive. In addition to raising capital, these financial services firms have sought to improve their financial strength by curtailing new lending, even to creditworthy borrowers that have historically had little difficulty receiving credit. This has caused economic growth to slow, raising the likelihood of a recession.

In fact, the difficulties faced by financial institutions, along with rising energy prices and other factors slowing economic growth, have resulted in a weak equity market in fiscal year 2008, with expected returns for this fiscal year projected to be much weaker than in fiscal year 2007.

"The difficulties faced by financial institutions, along with rising energy prices and other factors slowing economic growth, have resulted in a weak equity market in fiscal year 2008."

What does all this mean for our performance and investment strategy going forward?

While we will remain cautious about the potential for additional systemic risk, we believe the unwinding of this credit bubble presents excellent investment opportunities for us. As mentioned above, we expect to continue evaluating opportunities to participate in the recapitalization of the global financial services sector. Given our size and continued underexposure to the financial services sector, we are well positioned to take advantage of the favorable investment terms offered by various recapitalization opportunities.

In addition, the curtailment of new lending by various financial institutions opens up opportunities for new capital to realize attractive risk-adjusted returns by picking up the slack. Given the size of our portfolio, and our ability to forego liquidity given the long-term nature of our pension liabilities, we expect to seek out multiple opportunities to lend and invest that were traditionally absorbed by the financial services sector. To date, we have committed capital to invest in leveraged loans and distressed mortgage-backed securities on extremely attractive terms, and are actively considering opportunities to also invest in newly originated commercial mortgages and other financing opportunities. On a broader level, we will seek to leverage our potential access to direct investment opportunities on a financially attractive basis.

While it will likely take many years to assess the impact of recent events on the financial services sector, we strongly believe that the sector will continue to shrink in importance in relation to the overall economy, and that will create new opportunities for us to realize attractive returns and to further diversify the portfolio into asset classes that were previously unavailable to us.

Our investment plan for FY2008 includes several new long-term initiatives that we believe represent excellent investment opportunities for us. First, we intend to commit funds over time to "sustainable investments," with a potential focus on alternative energy opportunities. There are several general partners in the marketplace this year with excellent track records in this area. Given the political initiatives to reduce greenhouse gas emissions and the effectiveness of new technologies in this area, we believe that commitments to alternative energy projects offer the potential for exceptional risk adjusted returns.

Second, we will consider strategies that allow us to obtain equity stakes in general partners across all components of the alternative investments portfolio. The size of New Jersey's investment capital and the reputation benefits associated with an investment by New Jersey make us an attractive partner for some managers looking to grow (regardless of their size).

"Our investment plan for FY2008 includes several new long-term initiatives that we believe represent excellent investment opportunities for us."

Finally, we will seek opportunities to invest directly with other institutional investors as a means to influence product design and terms offered by general partners within the alternatives space. We will seek to identify opportunities where we can work with other public funds, endowments, foundations and sovereign wealth funds to structure investment programs within our various asset classes.

Sincerely,

Orin S. Kramer

William G. Clark

Orin S. Kramer
Chair
State Investment Council

William G. Clark
Director
Division of Investment

June 1, 2008

The State Investment Council

The State Investment Council was created by the New Jersey Legislature in 1950 to formulate policies governing the investment of funds by the Director of the Division of Investment, and to consult with the Director with respect to the work of the Division.

The Council meets monthly to discuss major investment policy issues and to review Pension Fund performance. Other investment programs and returns are reviewed annually or as needed.

The 13-member Council represents various constituent groups in the state. Seven members are appointed by the Governor for staggered five-year terms, and are drawn traditionally from the corporate investment community. Six of the seven are appointed with the advice and consent of the Senate, and the seventh is nominated jointly by the President of the Senate and Speaker of the Assembly.

Four employee representatives are elected to the Council by their respective pension boards for three-year terms. Two new employee representative seats created in 2007 are to be filled by appointment of the Governor from candidates nominated by the New Jersey State AFL-CIO and the New Jersey Education Association (NJEA) for three-year terms.

The Council has formed six committees organized around broad investment subjects relevant to Council decision-making: Executive/ Audit, Communications and Public Employee Relations, Corporate Governance and Diversity, Economically Targeted Investment, Incentive Compensation and Investment Policy.

Council meetings are open to the public. Agendas, meeting times and locations can be viewed at the Division of Investment website:
www.state.nj.us/rtreasury/doinvest

Council Members

Orin S. Kramer, Chair
General Partner
Boston Provident, L.P.

Jonathan Berg, Vice Chair
Representing
Public Employees' Retirement System

Erika Irish Brown
Senior Vice President
Lehman Brothers, Inc.

Maj. Marshall C. Brown
Representing
State Police Retirement System

W. Montgomery Cerf
Managing Director
Lehman Brothers, Inc.

Jose R. Claxton
Director
Latigo Partners, L.P.

James Clemente
Representing
Teachers' Pension and Annuity Fund

Susan Ann Crotty
Managing Director
Tremont Capital Management

Mark Kandrac
Representing
Police & Firemen's Pension Fund Board

James C. Kellogg
President
J.C. Kellogg Foundation

Douglas A. Love, PhD
Chief Investment Officer
Ryan Labs, Inc.

Vacant
Representing
New Jersey State AFL-CIO

Vacant
Representing
The New Jersey Education Association

As of June 1, 2008

The New Jersey Division of Investment

The Division of Investment is responsible for the investment management of more than 180 accounts, including the seven pension funds that comprise the New Jersey Pension Fund, the State of New Jersey Cash Management Fund and the Supplemental Annuity Collective Trust (a 403b plan). On June 30, 2007, the total net assets under management were $97.4 billion.

The Division of Investment, under the supervision of the State Investment Council, is the 10th largest public fund manager in the United States and the 15th largest among both corporate and public pension fund managers.*

Pension funds constituted $82.5 billion as of June 30, 2007, supporting the retirement plans of more than 700,000 active and retired employees in seven public pension systems: the Consolidated Police & Firemen's Pension Fund, the Judicial Retirement System, the Police & Firemen's Retirement System, the Prison Officers Pension Fund, the Public Employees' Retirement System, the State Police Retirement System and the Teachers' Pension & Annuity Fund (collectively referred to in this report as the "Pension Fund").

Assets are managed in 180 investment accounts, with the largest funds being the Pension Fund, the State of New Jersey Cash Management Fund, and the Supplemental Annuity Collective Trust (a 403b plan). The Division also manages a portion of the NJBEST Fund (a 529 college savings plan) and several funds under the New Jersey State Employees Deferred Compensation Program (a 457 plan).

The Division is staffed by some 65 professionals working in domestic and international equities, fixed income securities and alternative investments. The Division ranks 5th among all U.S. pension funds, both public and corporate, in assets managed internally.* The Division ranks 6th among all U.S. funds with assets in active international securities.*

The Pension Fund also earns fees from lending its domestic and foreign equities, and domestic fixed income securities, to brokers and financial institutions. In fiscal year 2007, the net income from fees on all securities loaned by the Pension Fund was $35.8 million.

Statutory Authority
The **Division of Investment** was created in 1950 by the New Jersey Legislature (P.L. 1950, c.270) to centralize all functions relating to the purchase, sale or exchange of securities for the State's diverse funds under experienced and professional management.

The statute vests investment authority in the Director of the Division, who is appointed by the State Treasurer from candidates nominated by the State Investment Council.

The statute also establishes a **State Investment Council** to formulate investment procedures and policies to be followed by the Director. New policies when adopted by the Council after public comment are filed with the Office of Administrative Law and reported in the *New Jersey Register.*

** Measured by assets as of 9/30/07. Reported by Pensions and Investments, January 21, 2008.*

Investment Parameters
All investments by the Director must conform to the heightened "prudent person" standard set by the New Jersey Legislature (P.L. 1997 c.26). This standard requires the Director "to manage and invest the portfolio solely in the interests of the beneficiaries of the portfolio and for the exclusive purpose of providing financial benefits to the beneficiaries of the portfolio."

Eligible investments are governed by the "whole plan" or "whole portfolio" principle, which permits a broad spectrum of investments to ensure diversity, minimize risk and improve returns on the investments as a whole.

Asset Allocations
Asset allocation policies for the Pension Fund are adopted and revised by the Council from time to time. Targets for fiscal year 2007 were as follows:

Total Equities Target: 55.7 percent. Includes domestic equities, 30.7 percent; international equities in developed markets, 22.5 percent; and international equities in emerging markets, 2.5 percent.

Total Fixed Income Target: 31 percent. Includes U.S. fixed income, 25 percent; U.S. high yield, 3 percent; and Treasury Inflation-Protected Securities (TIPS), 3 percent.

Alternative Investment Target: 10.3 percent. Includes private equity, real estate and hedge funds, as well as commodities and other real assets.

Cash Target: 3 percent.

Benchmarks for asset performance include the Standard & Poor's Composite 1500 Index for domestic equities; the Morgan Stanley Capital International-Europe, Australia and Far East Index (MSCI EAFE ex-Prohibited securities) for international equities; a blend of the Lehman U.S. Government/Credit and Lehman Long Government/Credit indices for domestic fixed-income; the HFRI Fund of Funds Composite Index for hedge funds and the National Council of Real Estate Investment Fiduciaries Property Index, NPI, plus 100 basis points for real estate; and 90-day Treasury Bill performance for cash.

Social Investment
The Council has determined that social and financial considerations are not mutually exclusive. The Council and the Division are open to any investment program which would benefit socially desirable purposes, particularly investment within the State of New Jersey, provided such investments meet fiduciary standards.

Net Assets under Management

	Net Assets June 30, 2007
Pension Fund	**$82.5 billion**
These basic retirement funds contain pension assets contributed by participants and by state and local employers for currently working and/or retired participants in seven statewide retirement plans. *(Total does not add due to rounding)*:	
Teachers' Pension & Annuity Fund	$34.0 billion
Public Employees' Retirement System	$26.3 billion
Police & Firemen's Retirement System	$19.7 billion
State Police Retirement System	$2.0 billion
Judicial Retirement System	$371 million
Consolidated Police & Firemen's Pension Fund	$14 million
Prison Officers' Pension Fund	$14 million
State of New Jersey Cash Management Fund*	**$19.9 billion**
This fund contains the cash balances of state government funds and "other-than-state" government entities (counties, municipalities, school districts and the agencies or authorities created by any of these).	
Supplemental Annuity Collective Trust	***$184.3 million***
This fund contains voluntary investments by employees for retirement income separate from, and in addition to, their basic pension plan.	
Trustees for the Support of Public Schools Fund	**$118.2 million**
This fund contains investments provided by bond investors and annual appropriation for the maintenance and support of the state's public schools.	

NJBEST Fund
The Division also manages some of the contributions of New Jersey residents for the state's tax-advantaged 529 college savings program. On June 30, 2007, this fund had a net asset value of $353.3 million.

Deferred Compensation Program
The Division also manages some of the assets contributed by employees into the New Jersey State Employees Deferred Compensation Program. Prudential Retirement, a business of New Jersey-based Prudential Financial, serves as the third-party administrator for this plan. Funds managed by the Division include contributions to the Bond (Fixed Income) Fund, Equity Fund, Money Market (Cash Management) Fund and Small Capitalization Equity Fund. On June 30, 2007, these funds had a combined market value of $1 billion.

Pension Funds Not Under Management
The Division manages some, but not all, of the pension funds for NJTRANSIT employees. It does not manage about $1 billion in pension funds invested by NJTRANSIT and the New Jersey Turnpike Authority, nor much smaller funds for employee health care at NJTRANSIT.

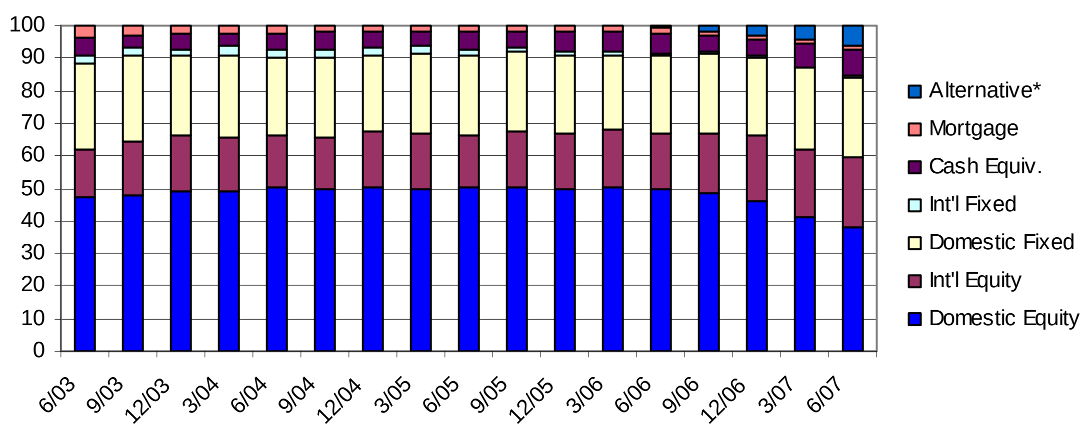
**The total for the Cash Management Fund includes $6.9 billion held for (and included in the totals for) the Pension Fund, the Supplemental Annuity Collective Trust, trustees for the Support of Public Schools Fund, the NJBEST Fund and Deferred Compensation Program.*

FINANCIAL SECTION

Financial Highlights for Fiscal Year 2007

- Net assets of the Pension Fund increased by $9.4 billion, or 12.9 percent, over the previous fiscal year. The Pension Fund out-performed its market benchmarks for fiscal year 2007, generating an additional $500 million in value for the fund compared to benchmark returns.
- The rate of return on investments was 17.1 percent, an increase from the 9.8 percent rate of return in the prior fiscal year. This marks the fund's highest return in nine years.
- The Cash Management Fund had no exposure to investments backed by sub-prime mortgages, enabling the Pension Fund to avoid the turmoil that affected some other money market funds.
- The Pension Fund continued to move away from investments solely in public equity and fixed income securities into a variety of new asset classes, building its alternative investment portfolio by funding nearly $4 billion in commitments during the fiscal year and establishing new relationships with 17 private equity funds, 19 real estate funds and 17 new hedge funds. Alternative investments returned 12.4 percent for the fiscal year.
- The Fund paid $5.5 billion in monthly retirement benefits to 236,787 retirees and beneficiaries during fiscal 2007. This compares to $5.2 billion paid to 227,816 retirees and beneficiaries during the 2006 fiscal year.
- The Fund received member and employer contributions of $1.51 billion and $2.24 billion, respectively, during fiscal 2007, compared with member and employer contributions of $1.45 billion and $1.93 billion, respectively, for fiscal 2006.

STATE OF NEW JERSEY COMPOSITE
ASSET ALLOCATION HISTORY



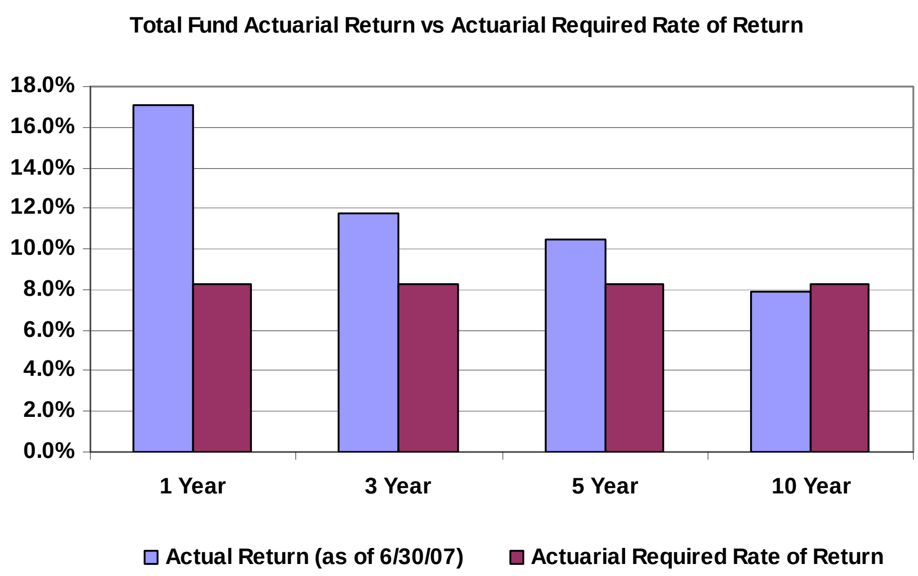
Alternative Investment Program started 9/05

10-Year Financials Summary

Market Values and Total Rates of Return

for Pension Fund for Fiscal Years ending June 30

	$ Billion	Return
2007	82.5	17.1%
2006	73.1	9.8%
2005	69.8	8.7%
2004	67.8	14.1%
2003	62.6	3.3%
5-year annualized return (thru 6/30/07)		10.5%
2002	63.3	(9.0)%
2001	72.2	(10.4)%
2000	82.6	12.0%
1999	76.2	16.0%
1998	67.3	22.7%
10-year annualized return thru 6/30/07		7.9%



Summary of Results for Fiscal Year 2007

Pension Fund Performance Summary

Net assets June 30, 2007: $82.5 billion
Net assets June 30, 2006: $73.1 billion

Benchmark (Indexed returns in each asset class): 15.6 percent
Actual rate of return: 17.1 percent

Net asset growth: $9.4 billion, or 12.9 percent

Management of New Jersey's Pension Fund earned a 17.1 percent rate of return for fiscal year 2007, exceeding both the Pension Fund's overall benchmark and the 8.25 percent assumed rate of return used by actuaries when calculating the Fund's future obligations. Individually, the Fund's four major asset classes – domestic equity, domestic fixed income, international equity and short-term money market securities in the Cash Management Fund – also exceeded their respective benchmarks for the fiscal year, as detailed below.

The strong returns were achieved even as the Division took steps to reduce risk by diversifying the pension portfolio, including the continued strengthening of an alternative investments program (see "Alternative Investments," below). As of June 30, 2007, the asset allocation of the Pension Fund was 38.3 percent in domestic equity, 23.9 percent in domestic fixed income, 20.9 percent in international equity, 8.2 percent in short-term money market securities, 6.1 percent in alternative investments and 2.0 percent in other classes.

Total Pension Fund assets were boosted by a $1.1 billion contribution from the State of New Jersey on June 29, 2007.

Net Pension Fund withdrawals were $2.7 billion during the 2007 fiscal year (net of employer and employee contributions), primarily for benefits paid out to retirees and other beneficiaries. These payments were more than offset by net investment income of $13.0 billion, consisting of interest and dividend income of $2.3 billion, net appreciation of $9.8 billion in the fair value of the underlying portfolio, and net securities lending income of $35.8 million.

How Pension Assets Are Managed

New Jersey's Pension Fund draws its income from the contributions of active employees, contributions from the state as authorized annually by the legislature, the contributions of county and local government employers, and income from the appreciation of Fund assets managed by the Division. Pension assets are managed by Division professionals in five different investment portfolios:

Domestic Equity Portfolio (Common Pension Fund A)
Domestic Fixed Income Portfolio (Common Pension Fund B)
International Equity Portfolio (Common Pension Fund D)
Alternative Investments Portfolio (Common Pension Fund E)
Cash Management Fund

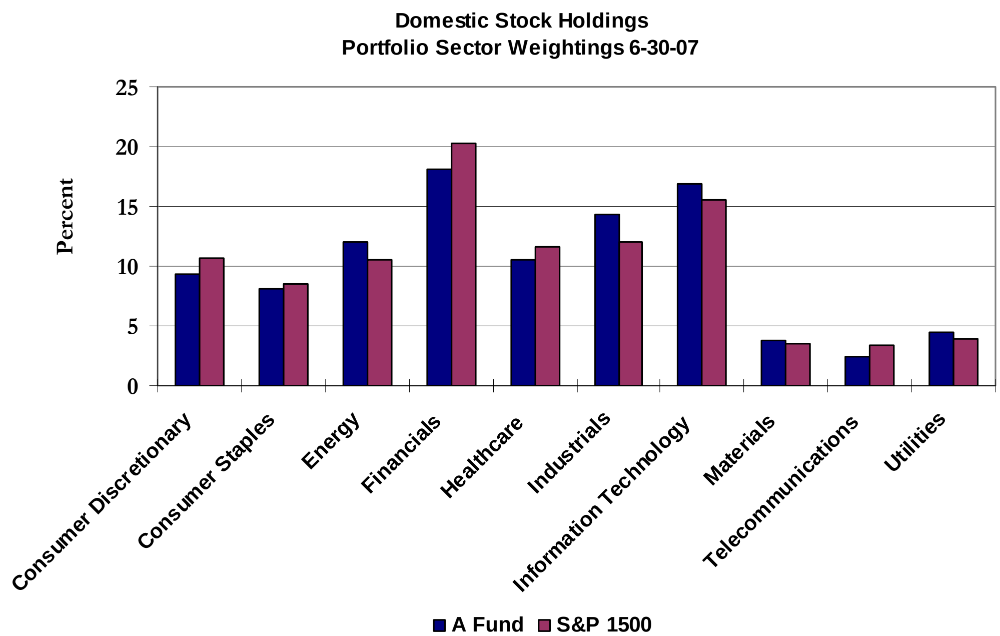
Domestic Equity
Annual Return Benchmark: 20.2 percent
(S&P 1500 Composite Index)
Actual return on investment: 21.0 percent

The Domestic Equity Portfolio out-performed the overall equity market in fiscal year 2007, as measured by the Standard & Poor's 1500 Composite Index.

The major factors contributing to the Division's out-performance were its stock selection within the technology sector and the relative lack of exposure to commercial banks and other financial services equities with connections to the residential mortgage market during the fiscal year.

The Domestic Equity Portfolio is broadly diversified by economic sector. While exposure to most sectors and industries is comparable to that of the overall market benchmark, the portfolio ended the fiscal year "overweight" (meaning a level of investment that exceeds that in the overall market benchmark, in percentage terms) in the industrial, energy and information technology sectors, and "underweight" (meaning a level of investment that is lower than that in the overall market benchmark, in percentage terms) in the financial, consumer discretionary and health care sectors.

The percentage of the Pension Fund invested in domestic equities declined over the fiscal year from 49.5 percent to 38.3 percent, consistent with the long-term strategy of the Council, as well as other major public pension funds, to reduce holdings in U.S. stock in order to fund other types of investments. Total domestic equity investments at the end of fiscal year 2007 were $31.5 billion.



Domestic Fixed Income

Annual Return Benchmark: 4.4 percent
(Blend of the Lehman U.S. Government/Credit and Lehman Long Government/Credit Indices)
Actual return on investment: 5.2 percent

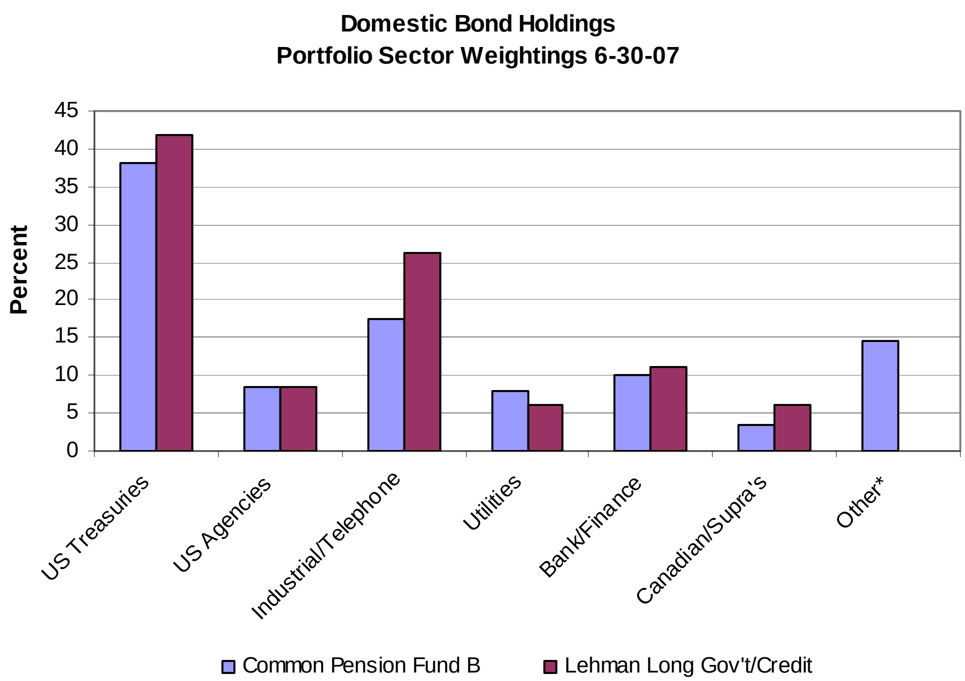
The Pension Fund's Domestic Fixed Income portfolio significantly out-performed its benchmark for fiscal year 2007. Several factors contributed to this out-performance, most significantly the Division's decisions to reduce holdings of corporate bonds and to avoid subprime mortgage-backed securities.

Also contributing to the portfolio's out-performance was the credit quality of corporate bonds in the portfolio, which remains superior to the securities in the indices that comprise the market benchmark.

The Division extended the duration of the portfolio from five years to nearly eight (7.84) years during fiscal 2007, to better match the anticipated benefit payments of the various pension plans.

The percentage of the portfolio invested in domestic fixed income securities (including federally guaranteed mortgage-backed securities) held steady at 23.9 percent as compared to the previous fiscal year.

The portfolio is overweight in U.S. Treasury securities versus the index on a duration-adjusted basis, with the major underweight being U.S. Agency securities.



* *US Agency Mortgage Backed Securities*

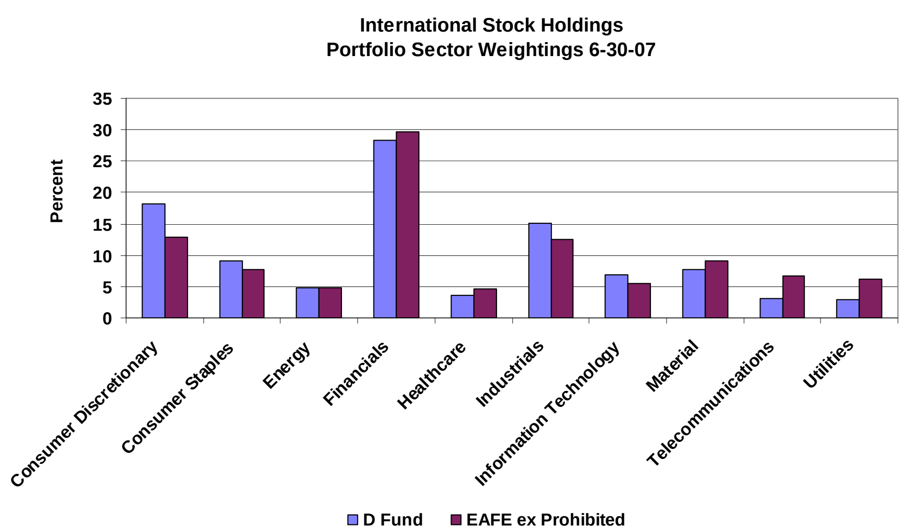
International Equity

Annual Return Benchmark: 27.3 percent
(MSCI-EAFE Index ex-prohibited securities)
Actual return on investment: 28.5 percent

Despite volatile and challenging markets, the International Equity portfolio earned a 28.5 percent return for the fiscal year, and out-performed the general market as measured by the Morgan Stanley Capital International-Europe, Australia and Far East Index (minus those index companies with ties to Sudan, in which the Division is prohibited from investing. See “State and Federal Legislation Update” in this report).

The percentage of the portfolio invested internationally in both equities and fixed-income securities rose in fiscal year 2007, ending at 20.9 percent. Within the international portfolio, international equities rose from $13.0 billion to $17.2 billion. In the Fund overall, international fixed income investment dropped from $1.2 billion to about $1 billion.

The International Portfolio is underweight in Japanese equities, in a belief that Japanese equity performance will be negatively impacted by an anticipated slowdown in global economic growth.



Alternative Investments

Hedge Funds -- Annual Return Benchmark: 14.3 percent
(HFRI Fund of Funds Composite Index)
Actual net return on investment: 13.2 percent

Private Equity – (No benchmark)
Actual net return on investment: 13.7 percent

Real Estate -- Annual Return Benchmark: 18.3 percent
(National Council of Real Estate Investment Fiduciaries Property Index, NPI, plus 100 basis points)
Actual net return on investment: 16.5 percent

The Alternative Investment portfolio, introduced in 2005 to reduce pension fund risk by diversifying fund investments beyond traditional stocks and bonds, also boosted the Fund's overall performance for fiscal year 2007.

At the close of the fiscal year, the portfolio had $10.2 billion in approved commitments, of which $6 billion had been invested. Of the total commitments, $4.8 billion was in private equity (including domestic and international buyout funds, venture capital, distressed and mezzanine debt funds); $2.6 billion was in real estate; and $2.8 billion was in hedge funds, both direct and fund of funds.

The State Investment Council also authorized a commitment of four percent of the portfolio in June 2007 dedicated to commodities and other inflation-sensitive assets. A total of $502 million was invested in commodity-linked notes as of June 30, 2007, with total returns on the matured one-year notes of 25.22 percent (for two notes maturing January 31, 2008) and 36.97 percent (for two notes maturing February 28, 2008). The Division also invested in two commodities funds in Fiscal Year 2008.

Cash Management Fund

Annual Return Benchmark: 5.06 percent
(90-Day U.S. Treasury Bills)
Actual Return on Investment: 5.47 percent

Despite the increased risks associated with securities backed by sub-prime mortgages, the Cash Management Fund's historically conservative position with regard to asset-backed commercial paper, coupled with an early divestment of its limited holdings, allowed the fund to deliver strong returns for the year.

The average daily compounded rate of return for State participants was 5.47 percent, compared with 4.31 percent the prior fiscal year. The average daily compounded rate for "Other-Than-State" participants (counties, municipalities, school districts and the agencies or authorities created by any of these) was 5.35 versus 4.20 for the previous fiscal year. The higher rates of return of the latest fiscal year followed the pattern of rising short-term interest rates in the United States.

Historically the Cash Management Fund has had limited exposure to asset-backed commercial paper (debt issued by stand-alone entities that can potentially invest in a variety of securities, including those collateralized by subprime mortgages). The Division has also utilized strict criteria for eligible investments, and capped its exposure to any one issuer. Nevertheless, the Division became increasingly concerned about potential exposure to asset-backed commercial paper in the spring of 2007, and began a series of steps to eliminate the Cash Management

Fund's exposure to these securities with no negative impact to performance. As of September 2007, the Cash Management Fund has no exposure to asset-backed commercial paper.

More than 180 state funds and more than 1,180 other-than-state entities invested in the fund in fiscal year 2007. The average maturity of the portfolio at fiscal year end was 62 days.

Costs of Management

Costs for managing all funds: 7.8 cents per $100 under management

The Division of Investment maintains one of the lowest costs of all public pension funds, largely because it ranks near the top nationally among all public and corporate pension funds in the percentage of funds managed internally. The Division ranks fifth nationally among all funds in the size of assets managed internally.

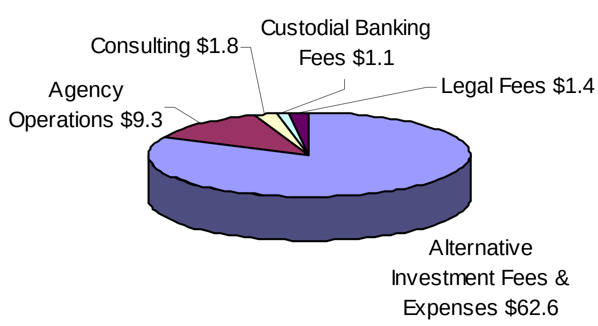
As part of its investment plans for fiscal years 2007 and 2008, the Division in 2007 began a process of engaging external managers to invest portions of the Pension Fund in certain types of investments (e.g., small cap and small-mid cap domestic equity, high-yield fixed income, and emerging market international equity), where the Division lacked the resources and expertise to invest directly. The first investments were made by these external managers in December 2007, and will be included in the fiscal year 2008 report.

The Division also invests in a number of alternative investment funds. The decision to invest in each alternative investment fund is made internally; each fund's individual investment decisions are made by its own investment management. The alternative investment funds charge the Pension Fund management fees and expenses in connection with their respective investments.

The Division spent $76.2 million in fiscal year 2007 for management of $97.4 billion in total assets. Operating expenses for staff compensation, overhead and equipment were $9.3 million, and represent about 12 percent of total costs. Remaining expenses include fees for alternative investment management, consulting services, custodial banking and legal services, as shown in the chart below.

Note: Alternative investment fees and expenses are directly linked to positive returns realized by the investment manager.

Total Management Costs (millions)
For fiscal year ended June 30, 2007



Total Management Costs (millions)
For fiscal year ended June 30, 2007

Alternative Investment Fees & Expenses	$62.6
Agency Operations	9.3
Consulting	1.8
Custodial Banking Fees#	1.1
Legal Fees^	1.4
Total all costs*	**$76.2 million**
Total assets under management	**$97.4 billion**
Costs as a percentage of assets under management	**0.078%**
Cost per each $100 under management	**7.8 cents**

 # Excludes banking fees satisfied by compensating (minimum) balances

^ As paid to outside attorneys. Legal services provided by the New Jersey Attorney General's Office are included within Agency Operations costs.

** Excludes brokerage commissions totaling $34.8 million for fiscal 2007 on domestic and foreign equities in all funds managed by the Division, because these commissions are accounted for as part of the cost (for purchase) or proceeds (for sales) for each respective transaction. The brokerage commission total of $34.8 million includes $4.8 million in "soft dollar" commissions used to procure systems and services critical to the Division's trading and research.*

Summary of Results for Calendar Year 2007

Pension Fund Performance *(Unaudited)*

Total Market Value of Pension Fund on December 31, 2007: $81.3 billion
Overall Annualized Return as of December 31, 2007: 9.21 percent

In addition to out-performing its fiscal-year benchmarks, the Pension Fund out-performed its calendar-year benchmarks in each major asset class.

The Domestic Equity portfolio returned 7.69 percent, versus a benchmark return of 5.47 percent. This strong result is attributable to an underweight exposure to financials and stock selection within the industrial and technology sectors.

The Domestic Fixed Income portfolio returned 8.41 percent versus 6.92 percent for a blend of the Lehman U.S. Government/Credit and Lehman Long Government/Credit Indices, the benchmark for this portfolio. Even though the portfolio remains short in duration versus the index (which hurt performance in a period of declining interest rates), this was more than offset by an underweight exposure to corporate bonds, particularly in the financial sector.

Within the International Equity portfolio, investments returned 11.53 percent, versus 11.49 percent for the Division's custom benchmark (MSCI EAFE ex-prohibited securities). Despite lagging the index earlier in the year, this portfolio had an excellent fourth-quarter performance (particularly in December), driven by an underweight position in Japanese stocks. This portfolio also included $200 million during calendar year 2007 assigned for investment in emerging markets.

	Market Values		Calendar Year 2007
	12/31/06	**12/31/07**	**Returns**
Common Fund A - Domestic Equity *S&P 1500*	$35,756,265,402	$28,850,821,506	7.69% *5.47%*
Common Fund B - Domestic Fixed Income *Blend of Lehman US Government/Credit and Lehman Long Government Credit*	$18,371,059,258	$22,511,191,765	8.41% *6.92%*
Common Fund D - International Equity *MSCI EAFE ex-prohibited (Division's custom benchmark)*	$16,129,761,039	$46,320,112,187	11.53% *11.49%*

OPERATIONS SECTION
Investment and Corporate Governance

Investment Policy and Strategy
The Investment Plan adopted by the Council for fiscal year 2007 resulted in several significant changes in the allocation and management of plan assets.

The Council, assisted by Division staff throughout 2006, undertook an extensive analysis that attempted to quantify the risk/return profile of potential asset allocations. The result was a new set of asset allocation targets starting in fiscal year 2007 designed to reduce overall risk to the Pension Fund, including inflationary risks, and to better match Fund performance to actuarial obligations. To further ensure these goals, the number of asset classes was broadened to incorporate alternative investments and a greater number of traditional asset classes.

Asset class targets for fiscal year 2007 are as follows. (It should be noted that "targets" as approved by the Council refers to central tendencies within a range, rather than hard target amounts):

Total Equities Target: 55.7 percent. Includes domestic equities, 30.7 percent; international equities in developed markets, 22.5 percent, and in emerging markets, 2.5 percent.

Total Fixed Income Target: 31 percent. Includes U.S. fixed income, 25 percent; U.S. high yield, 3 percent; and Treasury Inflation-Protected Securities (TIPS), 3 percent.

Alternative Investment Target: 10.3 percent. Includes private equity, real estate and hedge funds, as well as commodities and other real assets.

Cash Target: 3 percent.

Benchmarks for asset performance in fiscal year include the Standard & Poor's Composite1500 Index for domestic equities; the Morgan Stanley Capital International-Europe, Australia and Far East Index (MSCI EAFE ex-Prohibited securities) for international equities; a blend of the Lehman U.S. Government/Credit and Lehman Long Government/Credit indices for domestic fixed-income; and the 90-day Treasury bill performance for cash.

Additionally, the fiscal year 2007 Investment Plan proposed for the first time that several new and traditional asset classes be managed entirely or in part by external managers, including international equities, high-yield debt and emerging market investments, so that the Fund could avail itself of those most skilled in such investments to complement Division personnel. Although approved by the Council in 2006, implementation of this external management policy did not begin until the fiscal year ending June 2008.

Council Regulations and Business
In addition to the investment guidelines established by law, the State Investment Council sets specific investment policies by regulation to keep Council policies current with economic and fiscal trends, in accordance with its fiduciary responsibility and the authority provided under P.L. 1950, c.270.

All proposed regulations and amendments are filed with the Office of Administrative Law for publication in *The New Jersey Register*. Following a 60-day public comment period, proposals and all comments are brought to the Council for action or adoption. All regulations of the State Investment Council are published in the New Jersey Administrative Code (N.J.A.C. 17:16).

In fiscal year 2007, the Council:

- **Re-adopted with amendments all SIC regulations** (N.J.A.C. 17:16) after extensive review, as mandated by law every five years. Amendments included in the re-adoption: adding the flexibility to opportunistically purchase high-yield securities; flexibility to invest in interest-rate swaps; flexibility to increase the maximum futures exposure from 10 percent of the portfolio up to 50 percent after formal consultation with the Council's Executive Committee; and granting the ability to use index options and to remove the 10 percent limitation on option securities. Changes adopted to the Alternative Investments Program included: increasing the maximum commitment to any one fund to 10 percent of the asset class allocation, reverting to 5 percent when the commitments reach $5 billion*;* increasing the limit on investment in private equity, real estate, real assets and hedge fund strategies to 7 percent of the Pension Fund assets.

- **Approved the engagement of external managers** (N.J.A.C. 17:16-2) for management of several new and traditional asset classes either entirely or in part, including small- and mid-cap equities, high-yield debt and emerging market investments. Implementation of this external management policy began in 2008.

- **Amended the Division's broker firm eligibility policy** to allow the Division greater flexibility in accessing smaller brokerage firms able to provide valuable research.

- **Modified the caps on international developed and emerging markets, and the limitation on total plan assets that can be invested in high-yield debt,** to give the Division increased flexibility to exceed Investment Plan targets when it believes the market offers attractive or potential returns. Additional minor amendments were also approved by the Council to bring regulations in line with the current year Investment Plan. Note: All approved amendments took effect in August 2007. (N.J.A.C. 17:16-12, 14, 15, 16, 19, 20, 31, 33, 44, 46, 47, 58, 62, 67, 69, 71, 90 and 100)

The Council also reviewed outside professional analysis on the following investment policy issues:

- **Market value of pension plan assets against anticipated liabilities.** A study by Ryan Labs, Inc. presented in March 2007 addressed Council concerns about pension liabilities from an investment, rather than the customary accounting or actuarial, perspective. The study estimated the Pension Fund has a market value shortfall of more than the state-estimated actuarial shortfall when comparing the present value of benefits payments against the market value of pension assets as of September 30, 2006. The study illustrated why the Division has begun to extend the duration of fixed-income assets in the portfolio, and why it is examining other long-term, cash flow-producing assets, such as infrastructure.

- **The value of infrastructure as a potential pension plan asset class.** An analysis presented to the Council in May 2007 by Strategic Investment Solutions noted that the need for longer-duration cash flows is being considered by pension funds worldwide, with infrastructure investing (primarily energy, transportation and water investments) pursued by the governments of Australia and Canada among others. The 2007 Investment Plan considered infrastructure investment part of the inflation-sensitive asset class allocated a total 7 percent in the fiscal year portfolio. According to Strategic Investment Solutions, the role of infrastructure investments for the New Jersey fund would be primarily to hedge inflation risk, increase the fund's diversification, enhance returns and provide for stable, long-term cash flows.

The Council underwent the following organizational changes in fiscal year 2007: (Note: additional structural changes to the Council were made in July 2007, and will be reported in the upcoming annual report for fiscal year 2008.)

- The re-election of five members to Council seats by their respective pension boards, for one-year terms: Suzanna M.F. Buriani-DeSantis, Public Employees Retirement System; George A. Castro, Consolidated Police & Firemen's Pension Fund; James Clemente, Teachers' Pension and Annuity Fund; Vincent Foti, Police and Firemen's Retirement System; and John K. Sayers, State Police Retirement System.

- The re-election of Orin Kramer as Council Chair, and the election of Vincent Foti as vice chair.

- The resignations of public members Cheryl A. Mills, James. M. Farrell, Esq., and Anthony Terracciano.

Corporate Governance

The Council and the Division worked proactively during fiscal year 2007 to protect and advance the Pension Fund's shareholder interests in the corporations in which it is invested. Specifically, the Division:

- **Voted its domestic proxies in support of greater corporate board accountability.** The Division voted 1,266 proxies of U.S. companies in fiscal year 2007; this compares with 1,315 proxies and 1,255 proxies voted in fiscal years 2006 and 2005, respectively. The Division voted with management on all issues in 765 proxies. It voted against management on 639 individual proposals in the remaining 501 proxies. In general, the Division voted against the recommendation of management on issues that reduced board accountability, including proposals for exorbitant stock options and incentive or restricted plans for directors. In general, the Division supported proposals that would increase board accountability, including majority voting in the election of directors, advisory voting on executive compensation, the annual election of directors, the end of supermajority voting and pay tied to performance.

- **Voted its international proxies in support of greater corporate disclosure and improved board accountability.** The Division voted 579 proxies with internationally based companies in fiscal year 2007; this compares with 575 proxies and 505 proxies in fiscal years 2006 and 2005, respectively. The

Division voted with management on all issues in 428 proxies. It voted against management on 219 individual proposals in the remaining 151 proxies. The Division supported shareholder proposals requiring disclose of information on compensation consultants and disclosure of financial statements of bank subsidiaries. The Division voted against management proposals for exorbitant retirement bonuses, stock options, poison pills and director fees.

The Council also held an October 2006 discussion on corporate governance with John C. Coffee Jr., business law professor and Director of the Center on Corporate Governance at Columbia Law School. The discussion covered key policy issues, particularly in the area of executive compensation and corporate exposure to financial risk from environmental issues. Two new proxy voting guidelines were approved by the Council in February 2007: one guideline supporting the right of US shareholders for an advisory vote on executive compensation, and a second guideline supporting corporate initiatives that focused on a proactive approach to climate change.

Legislative Update

Divestiture

The Council and the Division worked with legislative leaders in fiscal year 2007 to reduce the fiscal impacts of a divestiture bill prohibiting state pension fund investment in certain foreign companies doing business in Iran.

Meanwhile, the Division maintains a growing list of companies ineligible for New Jersey investment under a Sudan divestiture law passed in 2005.

In support of the 2005 Sudan divestiture law, the Division sold qualifying holdings in 17 companies by May 2006, well ahead of the three-year deadline required by the act. Sales of these holdings totaled $2.2 billion.

At the end of fiscal 2007, the list of companies ineligible for investment under the state's Sudan law had grown to 30 companies, including Alcatel-Lucent, Ericsson, Nestle and Sony. Some of this list's growth came from the addition of companies located in emerging market counties, as the Division expanded its investments in these countries. The list also grew with the addition of companies not currently in the Fund but newly identified as ineligible for investment because of their equity ties to the government of Sudan or its instrumentalities. Companies that qualified for removal from the ineligible list were fewer in number than those newly qualifying for the list in fiscal 2007.

Divestitures pose three primary fiscal challenges to pension funds: they require the identification and sale of holdings on a timetable that doesn't consider market conditions; they impact risk and return for the entire pension fund; and they permanently reduce the investment universe available to a particular fund.

The Iran divestiture bill, which was signed into law in January 2008, requires the divestiture of an estimated $360 million in Pension Fund holdings by 2011, and further expands the list of companies ineligible for Pension Fund investment. Together, the Sudan and Iran divestiture laws reduce New Jersey's investment universe by almost 10 percent in developed markets and 14 percent in emerging markets, of its respective benchmarks. In addition, the Division's "prohibited" list includes an additional 45 companies which are not included in our international benchmark. The Iran divestiture law will receive full reporting in the fiscal year 2008 annual report.

Environmental Initiatives
The Division and Council took a more active role as institutional investors in fiscal 2007 in understanding and addressing the fiscal risks and opportunities posed by climate change and climate change regulation, in concert with the environmental leadership offered by the Legislature and Governor in drafting and adopting the Regional Greenhouse Gas Initiative, one of the nation's most progressive climate change laws.

Specific actions undertaken by the Division and Council included:

- Joined a growing list of major institutional investors in the Investor Network on Climate Risk (INCR), a $5 trillion network of major investors that promotes better understanding of the financial risks and opportunities posed by climate change.

- Joined a "CEO Call to Action" seeking a mandatory national policy aimed at reducing greenhouse gases, released in April 2007 in Washington, DC.

Strengthening the Operation

Stakeholder Relations
The Council and Division undertook several initiatives in fiscal year 2007 aimed at increasing the transparency of investment policies and practices and strengthening relationships with key stakeholders. Specific initiatives included:

- **Voluntarily adopted personal financial disclosures by all State Investment Council members.** The Council by unanimous vote in February 2007 agreed to file by May 15 each year personal annual financial disclosures required by law of most other State boards and authorities.

- **Increased reporting on Pension Fund performance** by expanding the director's monthly report released publicly at each meeting of the State Investment Council beginning in December 2006, and by adding additional information relating to alternative investments to the Division's website.

- **Offered special briefings.** Council Chair Orin Kramer discussed pension fund shortfall and steps the Council was taking to address these liabilities before the New Jersey League of Municipalities in November 2006. Division Director William G. Clark presented a detailed history of Pension Fund performance and current planning to representatives of the public employee unions in September 2006.

Search for a Global Custodian
The Division partnered with the consulting firm Callan Associates in fiscal 2007 to identify the most cost-effective and efficient ways to consolidate today's multiple custodian services under a single global custodian for all funds except the Cash Management Fund.

A Request for Proposals summarizing the Division's needs for upgraded systems and processes was drafted, and was expected to clear internal state review in the 2008 fiscal year. By consolidating all custody under a single agreement, the Division should be able to negotiate improved economic terms for these services (i.e., lower custody fees);

streamline accounting and other back-office processes through interface with one custody provider; and obtain superior technological and operational support via a larger scope of services.

The Year Ahead

The Investment Plan adopted by the Council for fiscal year 2008 continues the course set by the fiscal year 2007 Investment Plan: Alternative investments will increase at the same pace as previous years, even though the allocation to alternatives will remain less than that of other large public pension funds. The Fiscal Year 2008 plan calls for a somewhat lighter allocation to equities, consistent with the market risks perceived in that class.

The FY 2008 Investment Plan also incorporates three long-term initiatives:

- **Leveraging the Fund's size** where appropriate to seek equity stakes in investment management firms, so that the Fund gains not only returns but shares in the manager's profits as well.

- **Partnering with other pension funds** to increase negotiating power in investments, particularly over fees. The Division will seek such partnerships with other U.S. public funds, foreign funds and endowments. Sectors of special interest are infrastructure and "sustainable investments" including alternative energy.

- **Contracting with a new, global custodian** to upgrade the investment tools and systems available to the Division. A request for proposals is expected to be ready for release in the second quarter of calendar year 2008. The move to a global custodian is expected to modernize and improve the efficiency of Division operations.

Division of Investment Staff and Consultants

William G. Clark, Director
Vacant, Deputy Director
Gilles Michel, Assistant Director

Investment Teams

Domestic Portfolio
Brian Arena, Investment Officer
Vincent Benedetti
Betty Carr
Karin Hollinger
Kathy Jassem
Jeff Lebowitz
Tom Montalto
Michael Sawyer
Bruce Smith

International Portfolio
Gilles Michel, Assistant Director
Kersti Alabert
Brad Bauer
Melanie Lomas
Kevin Onderdonk
Ed Pittman
Danielle Scholl
Vitaly Smirnov

Fixed Income Portfolio
Phil Pagliaro
Tim Patton

Alternative Investments Portfolio
Hedge Funds
Maneck Kotwal, Investment Officer
Jessie Choi
Real Estate
James Falstrault, Investment Officer
Private Equity
Christine Pastore, Investment Officer
Jason MacDonald
Tim Rollender

Trading Desk (Domestic & International)
Mike Wszolek, Trading Officer
Ellie Chiaramonti
Olga Grozio
Vince Pagnotta
John Penza
Angel Rodriguez
Robert Rosati
Rob Schragger
Mary Ann Smith
Donald Sward

Cash Management Fund
Linda Brooks, Sr. Portfolio Manager
Cindy Everett
Venise Frazilus-Exil

Administrative Staff
Susan Burrows Farber, Chief Administrative Officer
Linda Thompson, Assistant to the Director
Amanda Truppa, Chief of Staff (Procurement, Ethics)
Nancy Brancolino
Queeniqueka Parish
Bart Pericoloso

Accounting
Alternatives
Ainsley A. Reynolds, Manager
Ron Hentnik

Domestic
Patricia Schwartz, Supervisor
Jeffrey Grossman
Manick Jhingade
Arlene Patel
Andrea Szul

International
Mary Vassiliou, Manager
Lori Hillman
Patti Hricak
Valerie Oscilowski
Sharon Scully
Kathleen Warchol

Cashier
John Giovannetti, Funds Cashier
Chris Eckel
Rosetta Muccie
Heather Rodriguez
Sharon Thomas
Vivian Velenger

Middle Office
Susan Sarnowski, Manager, Compliance Officer
Linda Gaspari
Jeffrey Taylor

Consultants
General and Private Equity Consultant
Strategic Investment Solutions, Inc.
Hedge Fund Consultant
Cliffwater LLC
Real Estate Consultant
The Townsend Group

As of June 1, 2008

State of New Jersey
Department of Treasury
Division of Investment
William G. Clark, Director
Mailing Address: P.O. Box 290 Trenton, NJ 08625-0290
Offices: 50 W. State St., 9th Floor, Trenton, NJ 08608
General Telephone: (609) 292-5106
Website: www.state.nj.us/treasury/doinvest