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# INVESTMENT SECTION

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*Governor*

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 DEPARTMENT OF THE TREASURY  
 DIVISION OF PENSIONS AND BENEFITS  
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ANDREW P. SIDAMON-ERISTOFF  
*State Treasurer*

KIM GUADAGNO  
*Lt. Governor*

FLORENCE J. SHEPPARD  
*Acting Director*

June 30, 2012

**REVIEWS OF MAJOR POLICY ISSUES**

The Division of Investment ("Division"), under the jurisdiction of the State Investment Council (the "Council"), is responsible for the investment management of the assets of 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 and Annuity Fund (collectively referred to as the "Pension Fund").

The Division was created in 1950 by the New Jersey Legislature (P.O. 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 also established the Council to formulate investment procedures and policies to be followed by the Director. The statute vests investment authority in the Director, who is appointed by the State Treasurer from candidates nominated by the Council. New and amended regulations adopted by the Council after public comments are filed with the Office of Administrative Law and reported in the *New Jersey Register*.

The Council is comprised of 16 members, appointed to fixed terms. Nine members are appointed by the Governor for staggered five-year terms, and are drawn traditionally from the corporate investment community. Eight of these nine hold appointments subject to the advice and consent of the Senate, and one appointee is selected by the Governor from nominees submitted jointly by the President of the Senate and Speaker of the Assembly. Two members are appointed by the Governor for five-year terms from nominees submitted by the New Jersey State AFL-CIO, with at least one appointed member being a member of a union representing police officers or firefighters. Two members are appointed by the Governor for three year terms from nominees submitted by the New Jersey Education Association and the State Troopers Fraternal Organization. Three members are designated to the Council for three-year terms by the respective pension system's board of trustees for the Public Employees' Retirement System, the Police & Firemen's Retirement System Board, and the Teachers' Pension and Annuity Fund. State law requires that no Council member shall hold any office, position or employment with any political party, and none can benefit from the transactions of the Division.

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."

To the best of our knowledge, performance is calculated using the time-weighted return based on the modified Dietz method.

Timothy M. Walsh  
 Director, Division of Investment

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# INVESTMENTS

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## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

### STATE INVESTMENT COUNCIL KEY REGULATIONS PERTAINING TO PENSION FUND ASSETS

- Public equity investments are limited to no more than 70 percent of the portfolio, including both domestic and international equities.
- Investments in international securities are limited to 30 percent of the portfolio, including both international equities and fixed income obligations.
- The market value of securities of companies in emerging markets is limited to 1.5 times the percentage derived by (1) dividing the total market capitalization of companies included in the MSCI Emerging Market Index by (2) the total market capitalization of the companies included in the MSCI All-Country World Ex-United States Index of the total market value of the assets held by Common Pension Fund D.
- The currency exposure on international investments may be hedged through currency transactions.
- Unlimited investment is permitted in securities issued by the U.S. Government and designated agencies.
- Investment in domestic and international corporate obligations, and collateralized mortgage obligations are subject to a minimum rating requirement of Baa3 by Moody's, BBB- by Standard & Poor's, and BBB- by Fitch Ratings. Investment in mortgage backed senior debt securities are subject to a minimum rating requirement of A3 by Moody's, A- by Standard & Poor's, and A- by Fitch Ratings. Up to five percent of the pension assets may be invested in these securities not meeting the minimum rating requirements.
- Up to 3 percent of the domestic equity portfolio may consist of debt in lieu of common stock, regardless of the credit rating of the issuing company.
- Investments in international government and agency obligations are limited to direct debt obligations of a sovereign government or its political subdivisions, debt obligations of agencies of a sovereign government which are unconditionally guaranteed as to principal and interest by the sovereign government's full faith and credit, and debt obligations of international agencies that are directly backed by the collective credit of multiple sovereign governments.
- Investments in municipal bonds, commercial paper, repurchase agreements, certificates of deposit, bankers acceptances, etc. are all permitted by specific regulations which specify high credit standards and conservative investment limits.
- Subject to limitations established by the State Investment Council, futures contracts, certain options contracts and exchange-traded funds may be utilized in the management of the portfolios.
- The Council regulations contain limits on (1) the percentage of the portfolio that can be invested in any one security and (2) the percentage of the outstanding amount of any one security that can be owned by the portfolio. These limits help to insure that the portfolio is adequately diversified and that competitive market pricing is obtained.
- Investments in alternative investments are limited to no more than 38% of the portfolio in the aggregate, with individual category limitations for private equity (12%), real estate (9%), real assets (7%), and hedge funds (15%).

### PROXY VOTING

- Proxy voting policy addresses key issues.
- The Division seeks to vote all proxies received, unless shares are out on loan. Under certain circumstances, the Division may restrict shares from being loaned, or recall loaned shares in order to preserve the right to vote on proxy issues.

# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

### INVESTMENT RETURNS

	ANNUALIZED		
	2012	3-YEAR	5-YEAR
<b>TOTAL PORTFOLIOS<sup>(1)</sup></b>	2.52%	11.11%	2.46%
<b>Equity Segment</b>			
<b>Common Pension Fund A (Domestic Equities)</b>	<b>3.58</b>	<b>16.68</b>	<b>1.79</b>
<i>S&amp;P 1500 Index</i>	4.63	16.76	0.46
<b>Common Pension Fund D (International Equities)</b>	<b>(16.53)</b>	<b>3.80</b>	<b>(5.08)</b>
<i>MSCI All World Country Index (ex US)-net</i>	(14.57)	6.97	(4.62)
<b>Fixed Income Segment</b>			
<b>Common Pension Fund B (Domestic Fixed Income)</b>	<b>15.89</b>	<b>12.76</b>	<b>10.77</b>
<i>Barclays Long Government/Credit</i>	24.58	14.41	11.00
<b>Alternative Investments Segment</b>			
<b>Common Pension Fund E</b>	<b>1.63</b>	<b>9.39</b>	<b>0.15</b>
Hedge Funds	(1.33)	6.25	(0.74)
<i>HFRI Fund of Funds Composite</i>	5.40	2.42	(1.84)
Private Equity	4.85	14.42	3.74
<i>Cambridge Private Equity Index<sup>(2)</sup></i>	10.83	18.22	6.97
Real Estate	8.30	6.36	(5.50)
<i>NCREIF Property Index</i>	12.04	8.82	2.51
Real Assets/Commodities	(9.54)	4.40	N/A
<i>DJUBS TR Index</i>	(14.32)	3.49	N/A

N/A — Not Available

Note: Performance is calculated using the time-weighted return based on the modified Dietz method.

<sup>(1)</sup> Excludes performance on Police and Fire Mortgages.

<sup>(2)</sup> Cambridge Private Equity Index is reported on one quarter lag.

# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

### ACTUAL ALLOCATION VS FY 2012 INVESTMENT PLAN TARGET JUNE 30, 2012

	Actual Allocation %	Target %	Difference %	Allocations \$
Absolute Return Hedge Funds	2.12	2.00	0.12	1,483.32
<b>Total Capital Preservation</b>	<b>2.12</b>	<b>2.00</b>	<b>0.12</b>	<b>1,483.32</b>
Cash Equivalents <sup>(1)</sup>	1.71	2.00	(0.29)	1,201.62
US Treasuries	1.80	2.50	(0.70)	1,259.85
<b>Total Liquidity</b>	<b>3.51</b>	<b>4.50</b>	<b>(0.99)</b>	<b>2,461.47</b>
Investment Grade Credit	20.03	20.00	0.03	14,042.13
High Yield Fixed Income	3.56	2.50	1.06	2,496.33
Credit Orient Hedge Funds	2.61	3.00	(0.39)	1,828.42
Debt Related Private Equity	1.05	1.50	(0.45)	737.93
<b>Total Income</b>	<b>27.25</b>	<b>27.00</b>	<b>0.25</b>	<b>19,104.81</b>
Commodities and Other Real Assets	2.82	4.00	(1.18)	1,977.94
TIPS	2.63	3.50	(0.87)	1,841.71
Real Estate	4.67	5.00	(0.33)	3,272.24
<b>Total Real Return</b>	<b>10.12</b>	<b>12.50</b>	<b>(2.38)</b>	<b>7,091.89</b>
US Equity	25.38	23.50	1.88	17,792.29
Non-US Developed Markets Equity	13.80	15.00	(1.20)	9,678.19
Emerging Markets Equity	6.05	5.00	1.05	4,239.35
Equity Oriented Hedge Funds	3.10	5.00	(1.90)	2,172.85
Buyouts/Venture Capital	6.78	5.50	1.28	4,751.04
<b>Total Global Growth</b>	<b>55.11</b>	<b>54.00</b>	<b>1.11</b>	<b>38,633.73</b>
Police and Fire Mortgage Program <sup>(2)</sup>	1.38	0.00	1.38	967.84
Other Cash and Recievables	0.52	0.00	0.52	366.13
<b>Total Pension Fund</b>	<b>100.00</b>	<b>100.00</b>	<b>0.00</b>	<b>70,109.19</b>

<sup>(1)</sup> The cash aggregate comprises the four common fund cash accounts, in addition to the seven plan cash accounts.

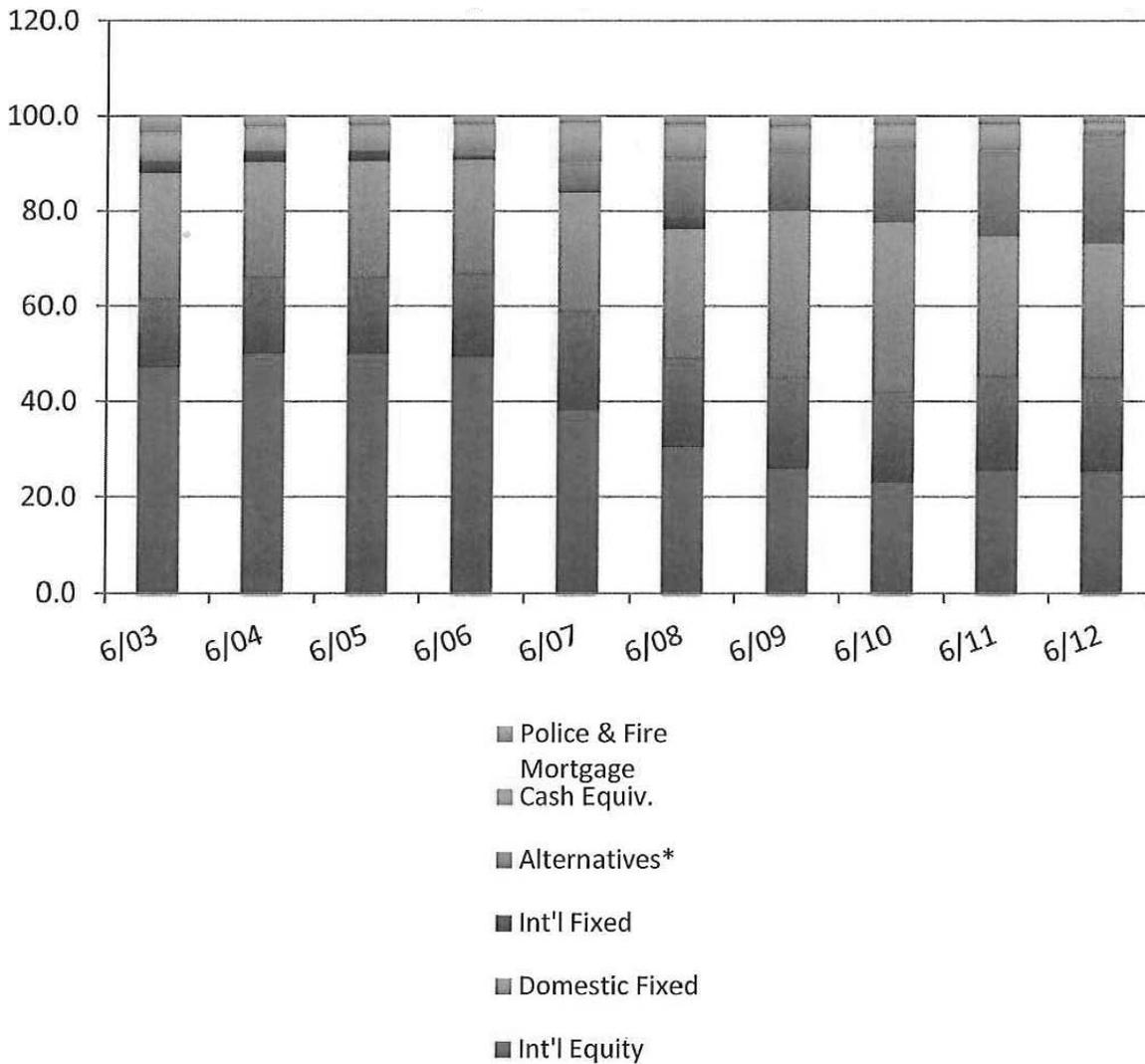
<sup>(2)</sup> Police & Fire Mortgage Program is not included in target asset allocation; assets are private mortgages that cannot be sold.

Totals may not equal sum of components due to rounding.

# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

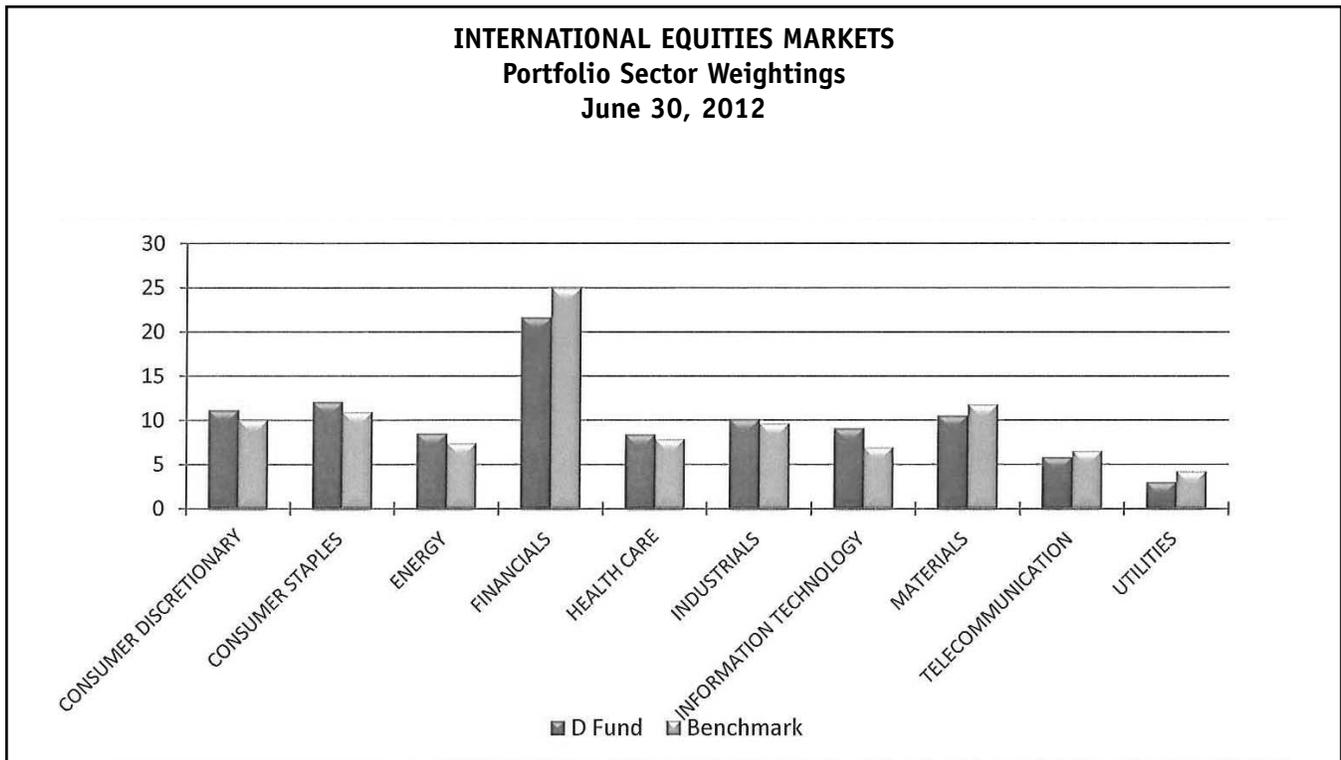
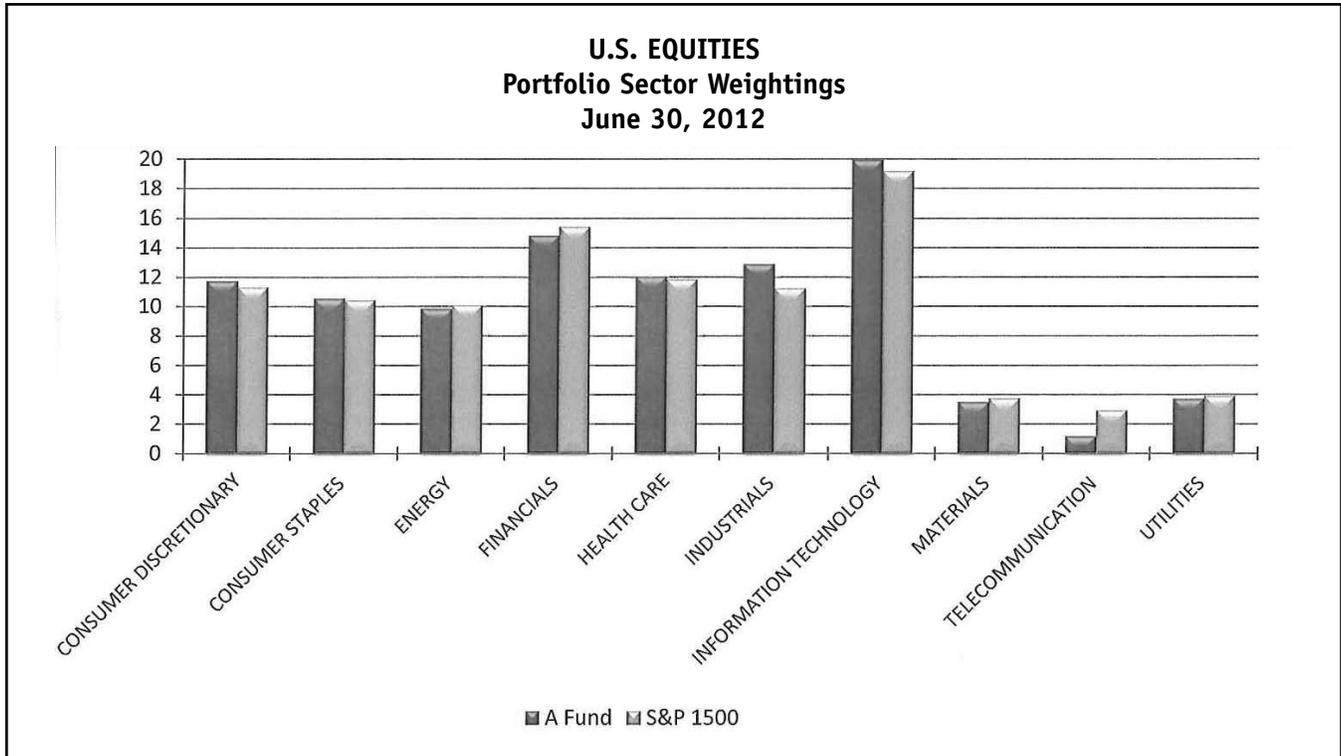
### STATE OF NEW JERSEY COMPOSITE ASSET ALLOCATION HISTORY



\*Alternative Investment Program started 9/05

# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS



# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

### LIST OF THE LARGEST ASSETS HELD LARGEST DOMESTIC STOCK HOLDINGS (BY FAIR VALUE) JUNE 30, 2012

	SHARES	STOCK	FAIR VALUE (USD)
1)	1,812,000	Apple Inc.	\$1,058,208,000
2)	5,716,834	Exxon Mobile Corp.	489,189,485
3)	21,155,000	General Electric Co.	440,870,200
4)	12,150,000	Microsoft Corp.	371,668,500
5)	7,045,909	Merck & Co. Inc.	294,166,701
6)	8,404,890	Wells Fargo Co.	281,059,522
7)	7,350,000	J.P. Morgan Chase & Co.	262,615,500
8)	11,346,425	Pfizer Inc.	260,967,775
9)	3,744,945	Proctor & Gamble	229,377,881
10)	2,601,000	Philip Morris International	226,963,260

### LARGEST DOMESTIC BOND HOLDINGS (BY FAIR VALUE) JUNE 30, 2012

	PAR	BONDS	COUPON	DUE	FAIR VALUE (USD)
1)	372,139,846	US Treasury Tips	2.000%	1/15/2026	\$474,914,451
2)	320,417,750	US Treasury Tips	2.125	2/15/2041	457,296,368
3)	310,000,000	US Treasury Bonds	6.000	2/15/2026	454,440,780
4)	294,676,250	US Treasury Tips	2.500	1/15/2029	408,932,251
5)	215,598,500	US Treasury Tips	1.125	1/15/2021	248,106,657
6)	295,000,000	US Treasury Strips	0.000	2/15/2025	222,196,655
7)	300,000,000	US Treasury Strips	0.000	8/15/2025	221,477,400
8)	130,000,000	Verizon Communications	8.950	3/1/2039	214,121,050
9)	175,000,000	Providence of British Columbia	2.650	9/22/2021	185,392,200
10)	105,000,000	General Electric Capital Corp.	6.750	3/15/2032	130,009,215

A complete listing of the portfolio is available on the Division of Investment's  
Web site at [www.state.nj.us/treasury/doinvest](http://www.state.nj.us/treasury/doinvest).

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# INVESTMENTS

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STATE OF NEW JERSEY  
DIVISION OF PENSIONS AND BENEFITS

LARGEST INTERNATIONAL STOCK HOLDINGS (BY FAIR VALUE)  
JUNE 30, 2012

	SHARES	STOCK	FAIR VALUE (USD)
1)	44,852,700	Vanguard MSCI Emerging Markets	\$1,791,865,365
2)	25,900,000	IShares MSCI EAFE Index Fund	1,293,964,000
3)	12,200,000	IShares MSCI Emerging Markets	478,118,000
4)	8,210,338	Glaxosmithkline PLC	186,337,529
5)	11,000,000	IShares S+P/TSX 60 Index Fund	179,224,091
6)	877,642	Roche Holding AG Genusschein	151,698,078
7)	4,912,290	Diageo PLC	126,510,891
8)	1,236,208	Anheuser Busch Inbev NV	96,168,041
9)	795,425	L Oreal Prime De Fidelite	93,330,046
10)	4,261,475	BG Group PLC	86,890,853

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# INVESTMENTS

## STATE OF NEW JERSEY DIVISION OF PENSIONS AND BENEFITS

### DOMESTIC EQUITY TRADING FISCAL YEAR 2012

<u>DOMESTIC EQUITY BROKERS</u>	<u>SHARES<sup>(1)</sup></u>	<u>TOTAL COMMISSIONS<sup>(1)</sup></u>	<u>COMMISSIONS PER SHARE</u>
Instinet LLC	34,742,708	\$1,236,511	\$0.036
JP Morgan Securities LLC	30,304,195	1,211,999	0.040
Citigroup Global Markets Inc	22,218,000	885,000	0.040
CAPIS	17,202,000	860,100	0.050
Sanford C. Bernstein & Co., LLC	45,140,039	720,999	0.016
Morgan Stanley & Co. LLC	18,849,335	682,001	0.036
UBS Securities LLC	20,923,336	629,000	0.030
Credit Suisse Securities LLC	41,016,610	626,205	0.015
Deutsche Bank Securities	17,506,452	574,800	0.033
Barclays Capital Inc.	12,918,888	515,996	0.040

<sup>(1)</sup> Excludes options written on approximately 41.3 million shares with total commissions of \$1,694,691.

### INTERNATIONAL EQUITY TRADING FISCAL YEAR 2012

<u>INTERNATIONAL EQUITY BROKERS</u>	<u>SHARES</u>	<u>TOTAL COMMISSIONS</u>	<u>COMMISSIONS PER SHARE</u>
Credit Suisse AG	107,023,317	\$1,230,249	\$0.011
Credit Agricole Securities Inc.	58,870,547	453,747	0.008
Deutsche Bank Securities Inc.	87,201,439	435,218	0.005
Morgan Stanley & Co. LLC	247,919,086	388,521	0.002
Instinet LLC	70,813,899	376,423	0.005
Goldman, Sachs & Co.	43,222,811	369,010	0.009
WallachBeth Capital, LLC	28,350,000	274,124	0.010
Citigroup Global Markets Inc.	9,711,733	260,392	0.027
CAPIS	57,032,120	256,729	0.005
G-Trade Services LLC	78,369,997	245,672	0.003

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