Commonwealth of Pennsylvania
State Employees' Retirement System

Comprehensive Annual Financial Report

For the year ended December 31, 2007

07

A Component Unit of the Commonwealth of Pennsylvania

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State Employees' Retirement System

Comprehensive Annual Financial Report

For the year ended December 31, 2007

Prepared by the staff of the
Pennsylvania State Employees' Retirement System

Leonard M. Knepp
Executive Director

Francis J. Donlevy
Chief Financial Officer

State Employees' Retirement System
30 North Third Street, Suite 150
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A Component Unit of the Commonwealth of Pennsylvania

Commonwealth of Pennsylvania
State Employees' Retirement System
30 North Third Street, Suite 150
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Nicholas J. Maiale
Chairman

June 2008

Honorable Edward G. Rendell, Governor
Commonwealth of Pennsylvania

Members, Pennsylvania General Assembly

Members, Pennsylvania State Employees' Retirement System

Dear Governor Rendell, Legislators and Members:

The Board of the Pennsylvania State Employees' Retirement System ("SERS") is pleased to present our Comprehensive Annual Financial Report ("CAFR") on the SERS Fund for calendar year 2007. The CAFR provides us with a vehicle to compile and publicly disclose extensive financial, investment, and actuarial reports with introductions from SERS management and the fund's consulting actuary.

This 2007 report reflects a fifth consecutive year of strong investment performance for the Fund: Overall 2007 return on the portfolio was 17.2 percent, or more than $5.2 billion, net of fees. Investment earnings are critically important to SERS' long-term soundness, comprising by far our single largest source of revenue: Over the last ten years, 85 percent of SERS' funding has come from investment earnings, compared to nine percent from employees and six percent from employers.

Our investment success is a direct result of an innovative and diversified investment strategy, through which we have diversified the fund not only across but also within asset classes, and, increasingly, across global geographic boundaries.

We believe that as a result of long–term investment portfolio planning and the prudent management of Fund assets, the System is well prepared to meet its obligations again this year and in the future.

The 11-member SERS Board represents the interest of public employees, public employers, and the taxpayer, in careful balance. SERS Board, staff, and I will continue to pursue prudent long–term investment strategies to assure the solvency of the Fund and the quality of pension–related services to all SERS members.

Sincerely,

Nicholas J. Maiale
SERS Board Chairman

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Certificate of Achievement for Excellence in Financial Reporting

Presented to

Commonwealth of Pennsylvania State Employees' Retirement System

For its Comprehensive Annual Financial Report for the Fiscal Year Ended December 31, 2006

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

President

Executive Director

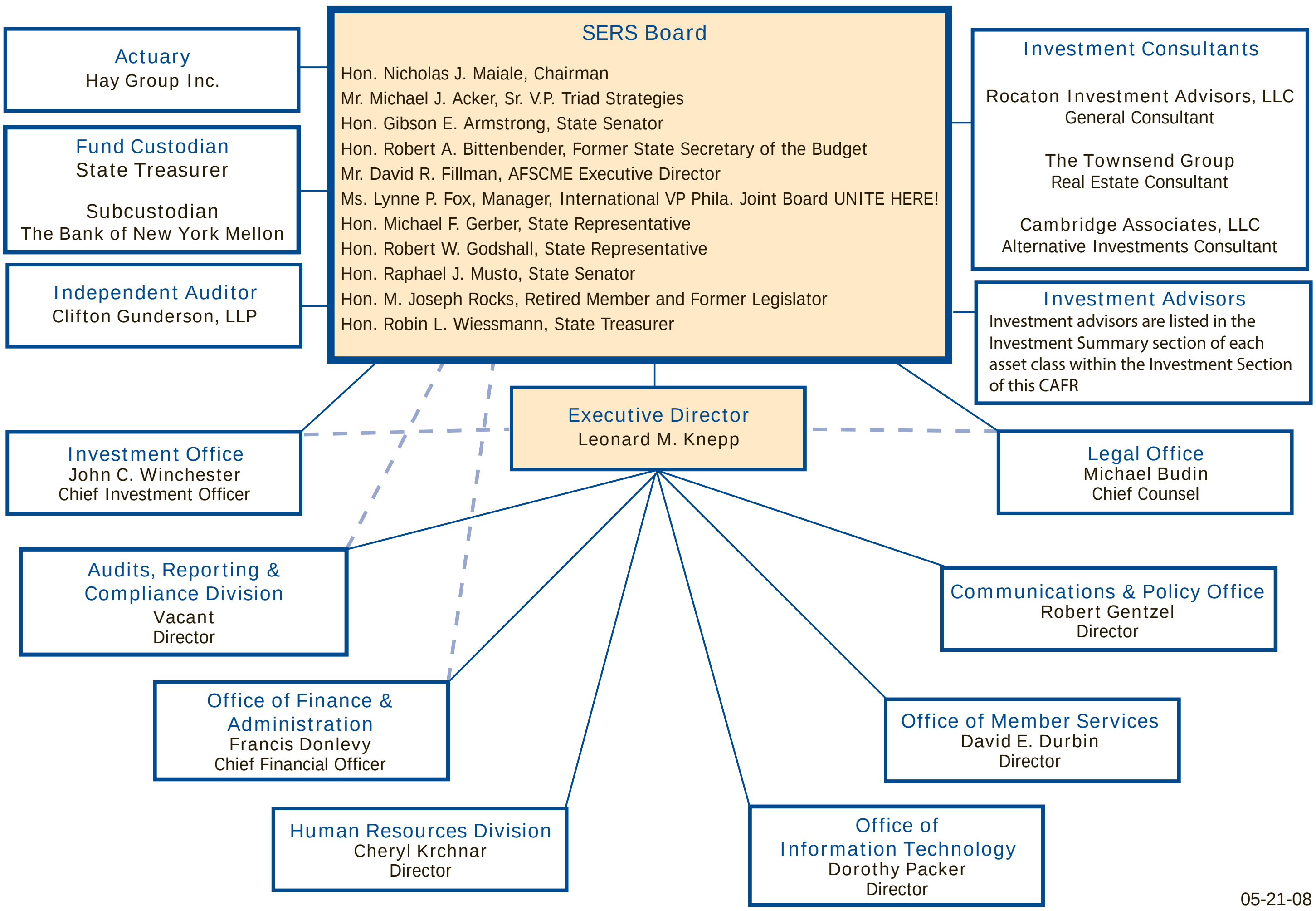
SERS' Vision

By 2010, SERS will be prepared for personnel and leadership transitions while continuing to meet operational, financial and public policy challenges of fulfilling our mission.

SERS' Mission

The mission of SERS is to provide retirement benefits and services to our members through sound administration and prudent investments.

SERS' Organizational Chart



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May 30, 2008

Mr. Chairman and Members of the Board:

We are pleased to present you with the Comprehensive Annual Financial Report (CAFR) of the Pennsylvania State Employees' Retirement System ("the System" or "SERS") for the calendar year ended December 31, 2007. Although SERS is not legally required to produce a CAFR, we do so in the interest of public accountability. Publication of this CAFR also serves to comply with the requirement, contained in the State Employees' Retirement Code, that SERS' financial statements be published, after auditing by an independent certified public accountant, on or before July 1 of each year.

Financial Information

The System's management is responsible for the preparation, accuracy and objectivity of the information included in this report, and accepts full responsibility for the contents, including not only the audited financial statements but all other information as well. The basic financial statements were prepared by management in accordance with generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board, and have been audited by an independent auditor. Users of the financial statements are encouraged to review the Management's Discussion and Analysis ("MD&A"), which accompanies the basic financial statements and discusses the market conditions, legislation and changes in operations that affected the financial results and funded status of the System.

SERS maintains an effective system of internal controls designed to provide reasonable assurance that assets are properly safeguarded, transactions are properly executed and the financial statements conform to generally accepted accounting principles. It should be recognized, however, that all internal controls have inherent limitations. These limitations exist because of several factors, including cost: The cost of attempting to establish a perfect internal control system would far outweigh the benefits derived. Another limitation is the potential for controls to be overridden by management, either individually or through collusion of two or more staff. To mitigate the risk caused by these inherent limitations, the System's Audits, Reporting, and Compliance division provides a continuing review of the adequacy and effectiveness of the System's internal control structure. Also, our independent external auditor, Clifton Gunderson LLP, conducts an annual audit of the financial statements in accordance with generally accepted auditing standards. Their audit includes tests and procedures designed to provide reasonable assurance that the financial statements are fairly presented. The external auditors have full and unrestricted access to the SERS Board members to discuss their audit and related findings regarding the integrity of financial reporting and adequacy of the internal control structure.

The annual financial audits show that the money entrusted to SERS is being properly managed so that we can continue meeting our obligation to our active and retired members, and their beneficiaries. Our members can be reassured that their retirement system is well managed and their benefits are secure.

The System also receives independent financial audits on all of its private equity, venture capital, pooled real estate, and absolute return fund–of–funds limited partnerships, as well as audits for its directly held real estate portfolios and collective trust fund statements.

Profile of SERS

SERS is a component unit of the Commonwealth of Pennsylvania, and administers a cost-sharing, multiple-employer defined benefit retirement plan. Founded in 1923, SERS is a mature pension plan with the number of annuitants and active members rapidly approaching a 1:1 ratio; as of December 31, 2007 the System had 109,610 active members and 107,130 annuitants and beneficiaries.

The System is administered by an independent 11 member administrative board comprised of: the State Treasurer, ex officio; two senators; two members of the House of Representatives; and six members appointed by the Governor. Through the Governor, the Board submits to the General Assembly an annual budget covering all proposed administrative expenditures, which includes proposed expenditures the Board intends to pay through the use of directed commissions. The expenditures are approved by the General Assembly in an appropriation bill and paid from the Fund.

Membership, Funding and Contribution Trends

As a mature plan, SERS pays out far more in benefits and refunds each year than it receives in contributions: $2.3 billion in payouts versus $578 million in contributions in 2007. The difference must come from the Fund's earnings and accumulated reserves, necessitating an investment policy that maintains the short-term liquidity required to fund payouts, while pursuing long-term returns of at least the actuarially assumed rate of 8.5%.

SERS achieved that goal again in 2007. The System posted an overall return of 17.2%, which placed it among the top 5% of all large public pension funds nationwide. This marked the fifth straight year of returns far in excess of the actuarial assumption, producing a five-year net compounded annualized return of 17.5%. That cumulative performance is reflected in an increase in the system's funded status, from 92.7% to 97.1%. Even at the previous funding ratio, SERS was among the best-funded public pension plans in the United States and that remains the case.

Although the purpose of the CAFR is to provide information regarding SERS status as of December 31, 2007, readers also should be aware of two anticipated future developments:

First, as the Fund continues to mature, the number of retired members is expected to continue to grow, while the number of active members is expected to remain relatively constant. As the number of retirees grows, the amount that must be paid out in benefits is expected to continue to increase. It is projected that by 2010 the number of retired members will exceed the number of active members and by 2012 annual benefit payments will reach $3 billion, 56% more than in 2006.

Second, the anticipated 2012 rate "spike," which has been addressed in prior CAFRs, has been significantly moderated as a result of the continued strong investment performance and legislative action. Act 2003-40, which changed the amortization period of SERS' unfunded liability, had been expected to maintain employer contributions in single digits through 2011, even dropping back down to zero for four years, followed by a steep increase for the 2012-13 fiscal year. However, legislation enacted last June, Act 8 of 2007, extended the 4% rate floor, thereby preventing a temporary drop in employer support, and the 2007 earnings reduced the system's unfunded liability to less than $1 billion. It is now projected that the peak employer rate, effective July 1, 2012, will be 5.7%, versus the 10.6% that was projected last year prior to the adoption of Act 8 and versus the 2007 employer normal cost of 8.21%. Current projections also show employer rates falling below 5.7% for at least a decade thereafter. It must be emphasized, however, that these projections assume, first, that the system will continue to achieve its assumed rate of return of 8.5% per year, and, second, that no new supplemental annuities ("COLAs") are granted. If earnings fall short of assumptions or if supplemental annuities are granted, projected rates could be significantly higher.

Initiatives

The SERS Board further refined the diversified investment portfolio in 2007, implementing a stand-alone absolute return strategy to complement the "portable alpha" absolute return strategy already in place. The Board also adopted a rebalancing strategy intended to enhance the Fund's liquidity profile by providing a ready pool of cash equitized with synthetic investments, including futures and swaps, to provide measured equity and fixed income exposure. Administrative initiatives included further progress on succession planning and a concerted and highly successful initiative to process a surge of retirements in June 2007. Prompted by impending changes in retiree health benefits, some 4,000 members retired in that one month. Given that an average year sees fewer than 4,500 retirements, the one-month volume presented a daunting challenge but one that the Office of Member Services met within the established processing timeframes. The year also was noteworthy for the system's uninterrupted performance, both administratively and fiscally, despite the unrelated departures of both the Executive Director and the Chief Investment Officer. Both were succeeded by individuals drawn from existing staff, which greatly helped to facilitate the dual transitions.

Awards

We are very pleased to note that the Government Finance Officers Association of the United States and Canada (GFOA) again awarded the Certificate of Achievement for Excellence in Financial Reporting to the System for the year ended December 31, 2006. The Certificate of Achievement is a national award, recognizing conformance with the highest standards for preparation of a state and local government financial report.

A Certificate of Achievement is valid for a period of one year only. We believe that our current Comprehensive Annual Financial Report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgements

This report reflects the dedicated efforts of the SERS staff under the direction of the SERS Board. We would like to take this opportunity to express our gratitude to the Board, the staff, our advisors and others who have worked diligently to administer the System, enhance delivery of member services and manage the Fund's assets in a prudent fashion.

We will continue to strive to administer the System in a manner that ensures the accurate, timely payment of benefits, prompt and courteous service, and prudent management of the Fund's assets on behalf of our members and the Commonwealth's taxpayers.

Respectfully submitted,

Leonard M. Knepp
Executive Director

Francis J. Donlevy
Chief Financial Officer

Honorable Nicholas J. Maiale

Chairman

Michael J. Acker

Senior Vice President Triad Strategies

Honorable Gibson E. Armstrong

State Senator

Honorable Robert A. Bittenbender

Former State Secretary of the Budget

David R. Fillman

Executive Director, AFSCME Council 13

Ms. Lynne P. Fox

Manager, International VP Phila. Joint Board UNITE HERE!

Honorable Michael F. Gerber

State Representative

Honorable Robert W. Godshall

State Representative

Honorable Raphael J. Musto

State Senator

Honorable M. Joseph Rocks

Retired Member and Former State Senator

Honorable Robin L. Wiessmann

State Treasurer

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Financial Section

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report

Members of the Board
Commonwealth of Pennsylvania
State Employees' Retirement System

We have audited the accompanying statements of plan net assets of the Commonwealth of Pennsylvania State Employees' Retirement System (the System), a component unit of the Commonwealth of Pennsylvania, as of and for the years ended December 31, 2007 and 2006, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Commonwealth of Pennsylvania State Employees' Retirement System as of December 31, 2007 and 2006, and its changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The information included in Management's Discussion and Analysis and Required Supplemental Schedules 1 and 2 and the notes thereto is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The Supplemental Schedules 1 and 2 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The introductory section, investment section, actuarial section and statistical section as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. The introductory, investment, actuarial and statistical sections have not been subject to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Clifton Gunderson LLP

Baltimore, Maryland
May 14, 2008

Offices in 17 states and Washington, DC

Member of HLB International

This section presents Management's Discussion and Analysis of the Pennsylvania State Employees' Retirement System's (the System) financial statements and the significant events and conditions which affected the operations and performance of the System during the years ended December 31, 2007 and 2006.
The Management's Discussion and Analysis includes forward-looking statements that involve certain risks and uncertainties. Actual results and performance may differ materially from those expressed or implied in the forward looking statements due to a wide range of factors including: changes in securities markets, general economic conditions, interest rates, energy policies, legislation and global conflicts

Overview of the Financial Statements and Accompanying Information

1) **Fund Financial Statements.** The System presents Statements of Plan Net Assets as of December 31, 2007 and 2006 and Statements of Changes in Plan Net Assets for the years then ended. These statements reflect resources available for the payment of benefits as of year-end, and the sources and use of those funds during the year.

2) **Notes to Financial Statements.** The notes to financial statements are an integral part of the financial statements. We encourage readers to review them because the additional detailed information will provide a better understanding of the financial statements. The notes provide information about the System's organization, benefits and contributions, how asset values are determined, the use of derivatives in managing the System's assets, and contingencies and commitments.

3) **Required Supplementary Information.** The required supplementary information consists of:

   - A schedule reflecting the funding progress of the System
   - A schedule showing the employer required contributions in dollars and percentage
   - Related notes to those schedules discussing actuarial assumptions and information
   - This Management's Discussion and Analysis.

4) **Other Supplemental Schedules.** Other schedules include detailed information on administrative expenses incurred by the System, a breakout of investment related expenses, and fees paid to consultants for professional services.

Financial Analysis

The System provides retirement benefits to the employees of the Commonwealth of Pennsylvania and certain other public agencies. The System's benefits are funded through member and employer contributions, and investment income. The net assets of the System increased approximately $3.5 billion and $3.3 billion in each of the years ending December 31, 2007 and 2006, respectively, as reflected in the table on page 7. Investment returns for both 2007 and 2006 reflect strong returns from the non-US equity securities markets, real estate, inflation protection and private equity asset classes, which enabled the System's investments to earn approximately $5.2 billion and $4.7 billion, respectively, in net investment income. The System's 2007 funded status of 97.1% increased from 92.7% in 2006. By comparison, as reported in the Wilshire Associates' "2008 Wilshire Report on State Retirement Systems", a compilation of 2007 data on 56 state pension plans, the average funding level of state plans was 85%. Every five years, the System undergoes an Actuarial Experience study to determine whether the assumptions used in the annual actuarial valuation are representative of current and anticipated trends. The latest experience study for the five year period 2001 – 2005 was completed in 2006.

The System reviews and modifies, if necessary, its *Annual Strategic Investment Plan*. These processes enable the System to position itself to respond to changing dynamics and fulfill its primary mission of meeting its benefit obligations to the System's members. Benefit expenses, including refunds of contributions, were $2.3 billion in 2007. This expense level represents an increase in benefit expenses of 21.7% over the $1.9 billion for 2006 and 2005. The System experienced a large increase in retirements in June 2007 due to recent employee contract changes, resulting in higher benefit payments for the last half of 2007. Retirements are not expected to continue at this level as the number of retirement age employees has declined. There are currently more than 6,400 employees with 30 years or more of service. This number compares to over 8,400 employees in 2006.

Funded Ratio

The funded ratio of the plan measures the ratio of actuarially determined assets against actuarial liabilities and is a good indicator of a pension fund's fiscal strength and ability to meet its obligations to its members.

The System is required by statute to perform an annual actuarial valuation. The actuarial process to develop the funded ratio is highly dependent on estimates and assumptions, particularly those regarding investment returns, salary growth, inflation, and demographics. In addition, the selection of methods such as amortization periods affects employer contribution rates and the funded ratio of the Plan. The Plan's funded ratio as of December 31, 2007 was 97.1%, an increase from 92.7% at December 31, 2006. The funded ratio of the Plan changed due to a larger increase in actuarial assets than the increase in actuarial liabilities. Actuarial assets increased from $28,149 million at December 31, 2006 to $30,840 million at December 31, 2007 for a 9.6% increase. The increase is primarily attributable to investment returns above the actuarial assumed rate of 8.5% over the five year period then ended. The increase in actuarial liabilities from $30,365 million at December 31, 2006 to $31,754 million at December 31, 2007 or 4.6% is primarily attributable to wage increases.

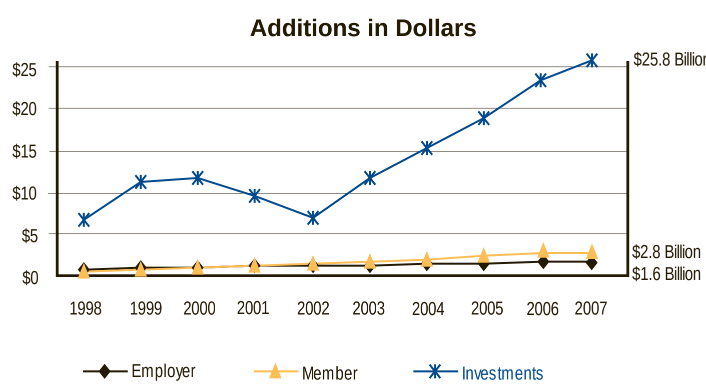
Member Contributions

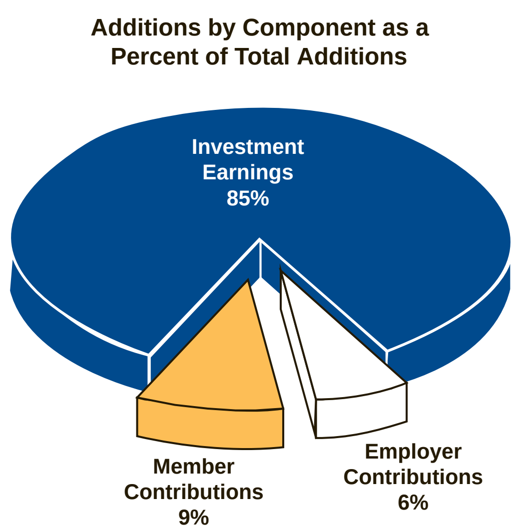
Additions to plan net assets include employer and member contributions and net income from investment activities. Member contributions were approximately $334 million, $318 million, and $306 million for the years ended December 31, 2007, 2006 and 2005, respectively, with 2007 contributions representing an increase of approximately $16 million compared to 2006. The employee rate of 6.25% of gross salary for most members is set by statute and has remained unchanged. The increase in gross salary of active members was the primary reason for the increase in contributions. The gross salary increased to $5.3 billion in 2007 from $5.1 billion in 2006.

Employer Contributions

Employer contributions were approximately $244 million, $196 million, and $148 million, for the years ended December 31, 2007, 2006, and 2005, respectively, for a year-over-year increase of $48 million for both 2007 and 2006. The increase is a result of several factors; an increase in the employer contribution rate, an increase in employee salaries, and an increase in inter-agency receipts for multiple service payouts due to increased retirements from 2006 to 2007. The employer composite rates as of December 31, 2007, 2006, and 2005 were 4.0%, 4.0% and 3.0% of total employer payroll. The employer contribution rate floor, originally established by Act 40 in 2003 and set to expire in 2007, was made permanent at 4% by Act 8 of 2007. Although the employer contributions have increased over the last three years, they still represent less than half of the normal cost and have been low when compared to historical standards. Over the last 10 years, employer contributions have been the smallest component of additions to the System's plan net assets. From 1998 through 2007, employer contributions totaled $1.6 billion, representing 6% of total additions to plan net assets, compared to $2.8 billion or 9% of total additions attributed to employee contributions and $25.8 billion or 85% of total additions attributed to investment earnings as demonstrated in the following chart.

Ten Year Cumulative Additions to Plan Net Assets

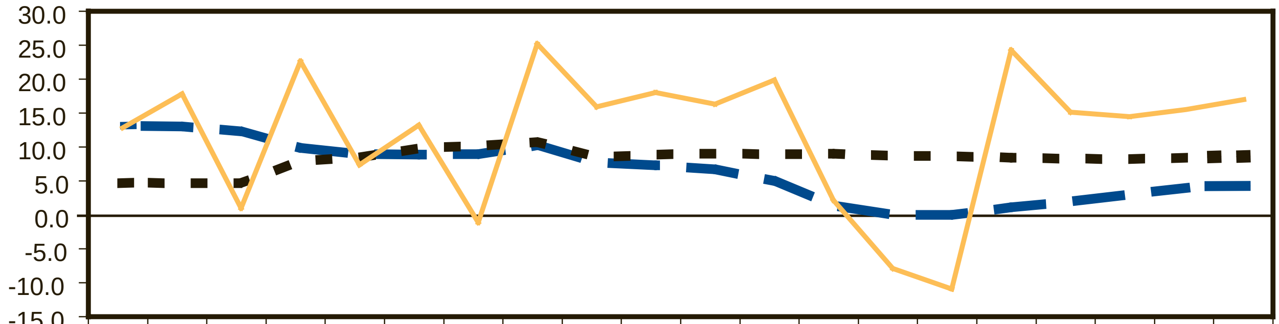




Over this time period, the active membership payroll has grown from $4.2 billion in 1998 to slightly over $5.3 billion.

The System's investment returns, which have exceeded the actuarial assumed rate of return of 8.5%, are the primary reason for the low employer contribution rate. The benefits of reduced employer contributions pass directly back to the participating Commonwealth agencies

History of SERS Employer Contribution Rates and Investment Returns



	88	89	90	91	92	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07
Employer Contribution Rates %	13.1	13.0	12.3	9.9	8.9	8.9	8.9	10.3	7.7	7.3	6.7	5.0	1.4	-	-	1.1	2.0	3.0	4.0	4.0
Employer Normal Cost Rates %	4.7	4.7	4.7	7.9	8.5	9.8	10.2	10.7	8.5	8.9	9.0	9.0	9.0	8.7	8.6	8.4	8.3	8.3	8.4	8.2
Investment Returns %	12.8	17.8	1.0	22.6	7.4	13.2	(1.1)	25.2	15.4	18.5	16.3	19.9	2.2	(7.9)	(10.9)	24.3	15.1	14.5	16.4	17.2

Employer Contribution Rates %
Employer Normal Cost Rates %
Investment Returns %

and the taxpayers of Pennsylvania. For example, had the Commonwealth agencies paid the Employer Normal Cost rate over the last 10 years, there would have been an additional $2.8 billion in employer contributions into the System. The Normal Cost is the cost of future benefits that is allocated to the current year by the actuarial cost method. In theory, if the unfunded actuarial liability were zero, and there were no deviations from the actuarial assumptions or amendments to the Retirement Code, the Normal Cost would be that amount required to fund the on-going liabilities for plan participants. The above chart presents the relationship between investment returns and contribution rates. When returns are strong and above the actuarial assumed rate, as in the 1990's and most recent five years, the employer's level of contributions will generally be below the Normal Cost. Conversely, when investment returns lag the actuarially assumed rate of 8.5%, those losses are amortized into the fund through increased employer contributions.

Net Investment Income

Investment portfolio performance produced investment returns of 17.2%, 16.4%, and 14.5% for the years 2007, 2006, and 2005, respectively. That performance generated net investment income totaling approximately $5.2 billion during 2007, $4.7 billion in 2006, and $3.6 billion in 2005. Strong international equity markets continued to fuel performance in all three years. The MSCI World ex US Index returned 12.9% for 2007 and 17.9% for the three year period ending 2007 while the domestic Russell 3000 index returned 5.1% for 2007 and 8.9% for the three year period ending 2007. For the three, five, and ten year periods ended December 31, 2007, the System earned compounded annual rates of return of 16.0%, 17.5% and 10.1%, respectively, which exceeded the actuarial assumption of 8.5%. Below are the System's annual rates of returns by major asset class:

Annual Rates of Returns

Asset Class	2007	2006	2005
Global Equities	12.3%	N / A	N / A
Domestic Equities	9.5	18.8	7.3
International Equities	17.0	26.7	19.3
Fixed Income Securities	6.1	7.7	4.9
Cash / STIF	5.1	4.9	2.9
Real Estate	22.6	17.6	30.9
Private Equity	41.0	23.2	36.5
Venture Capital	16.7	5.4	8.3
Inflation Protection	31.4	-6.3	24.7
Total Fund	**17.2%**	**16.4**	**14.5**

The most significant deduction from investment income is investment manager fees. The System's assets are managed 100% by external investment advisors hired by the Board. Many of these managers are paid a fee based on the assets under management. Accordingly, those managers were generally compensated more in 2007 than in prior years because of the effect of increasing asset values. However, the industry practice for the limited partnership investments is for the limited partners to pay fees to the general partner based on commitments to the partnership during the initial years. The $47 million increase in investment expenses in 2007 was due to several factors. Real Estate manager fees increased by $19 million primarily as a result of incentive fees. Alternative Investment manager fees increased by $12 million primarily as a result of an increased number of managers and funds in this asset class. The balance of the increase was the result of the fair value increase of the overall System's investment portfolio.

Benefits, Refunds and Expenses

Benefits are the most significant recurring deduction from Plan Net Assets. During 2007 the System paid out approximately $2.3 billion in benefits and refunds compared to $1.9 billion for 2006. There were 8,761 new retirees added to the annuity payroll in 2007 with an average annual benefit of $26,776. These new additions retired with a much higher annual benefit than those removed from rolls. There were 3,691 retirees removed from the rolls with an average annual benefit of $11,444. The increase in new retirees added to the rolls in 2007 increased total benefits and refunds paid in 2007.

Primarily due to the larger than normal number of retirements in 2007, supplemental payments increased 111% from $273 million in 2006 to $575 million in 2007. These supplemental payments are mainly the result of members withdrawing their accumulated contributions and interest from the System. Those withdrawals reduce the retirees' annuity payments over the annuitants remaining life. The System expects fewer retirees to be added to the rolls for the next several years however salaries are increasing which could increase annual benefit expenses. More than 6,400 current employees have 30 years or more of service with average salaries of approximately $65,600.

The System was established in 1923 but did not pay more than $1 billion in annual benefits until 1997. The System's annual benefit payments reached $2 billion in 2007 and based on recent actuarial projections it will reach $3 billion by 2012. The following table shows the increase in retirees and monthly benefit payments since 2005.

The administrative costs of the System represented less than 0.08% of average net assets in 2007 and 2006. All costs were within budget.

Growth in Annuity Payroll

	Dec. 2007	Dec. 2006	Dec. 2005
Monthly Annuity Payroll	$154 million	$138 million	$133 million
Retirees	107,130	102,060	101,179

Plan Assets

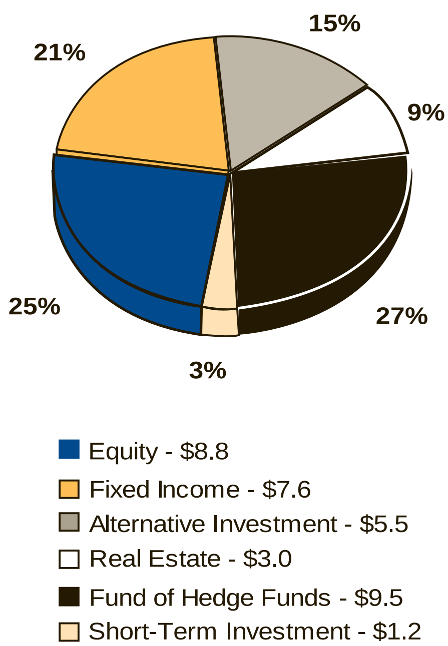
The System's investments are the most significant component of the System's assets. Investments increased to $35.7 billion in 2007 from $32.1 billion as of December 31, 2006. The $3.6 billion increase in investments is even more impressive considering the System paid out $2.3 billion in benefit payments in 2007.

The System values its assets at "fair value" as discussed in the accounting policies Note 2(c) to the financial statements. Fair value is the value the System expects to receive in a current sale between a willing buyer and a willing seller that are equally motivated; that is, other than a forced or liquidation sale. The value of publicly traded securities, stocks and bonds, are determined using the latest quote from national exchanges or pricing services. Those prices reflect the securities' pricing at the close of business and are affected by such items as liquidity, current events and the size of lots being traded. Real Estate is valued by the investment advisor using discounted cash flows, recent comparable sales, and current market conditions to arrive at a fair value. The real estate portfolios undergo an annual independent financial audit of the estimated fair values as well as an independent appraisal process on a routine cycle conducted by approved appraisers who meet specified professional qualifications. The appraisal process involves a significant amount of judgment and estimating. As a result, the ultimate value on sale of the asset may differ from the appraised value.

Values for investments in private equity and venture capital limited partnerships are determined by the general partners and by valuation committees. The partnerships' investments, as well as the assumptions and estimates used in developing the investment values, are subject to annual independent audits. Because the investments in those partnerships are generally illiquid and holding periods may last for several years, the ultimate value realized by the System on the disposition may differ from the estimated values reflected in the financial statements, and those differences could be material.

As of December 31, 2007, fund of hedge funds fair values were $9.5 billion, an increase of $1.4 billion from December 31, 2006. Equity fair values of $8.8 billion, an increase of $1.2 billion over 2006 are due to strong returns for international equities. The fixed income fair values were $7.6 billion, an increase of $2.3 billion from December 31, 2006. Included in fixed income were Treasury Inflation Protection securities which underlie certain inflation protection assets. The inflation protection assets posted very strong returns for the fund. The alternative investment and real estate asset classes increased $1.3 billion and $523 million respectively from strong returns. The total investment portfolio fair value of $35.7 billion was comprised as shown in the below chart:

Investments at Fair Value and Allocation Percentages
Investment Fair Values in Billions
As of December 31, 2007



The System earns additional investment income by lending investment securities to brokers. The brokers provide collateral to the System for borrowed securities generally equal to 102% to 105% of the borrowed securities. The System invests the collateral to earn interest. Income, net of expenses, from security lending is dependent on the volume of lending generated at the custodian bank and the spreads (profits) on those loaned securities. Volume was down 11.4% from 2006 and net security lending revenue was up 23.8% in 2007. The security lending assets on loan was $3.1 billion at December 31, 2007 compared to $3.5 billion at December 31, 2006. Net security lending revenue was $13.0 million, in 2007, an increase of $2.5 million from 2006 net lending revenue of $10.5 million. Spreads increased significantly in the Treasury class which would include the TIP securities. Spreads also increased in the sovereign debt securities loaned from the System's emerging markets. Within these portfolios, certain bonds were in very high demand in 2007, increasing 2007 income. The volume of the Treasury class increased while the sovereign debt volume declined significantly.

Derivatives

The System uses derivatives as a means to provide market exposure to domestic and global equity markets, and commodity asset classes, and to manage interest rate risk in the fixed income portfolios. Used properly, these derivatives deliver returns similar to indexed returns in the respective asset classes in a cost-efficient manner without disrupting the liquidity needs of the System. The System's investment advisors manage counterparty credit risk by entering into contracts with parties with strong credit ratings and by establishing collateral requirements. The System monitors derivative levels and types to ensure that portfolio derivatives are consistent with the intended purpose and at the appropriate level.

Liquidity

The System's liquidity needs are met through employee and employer contributions, earnings from investments, and its well diversified investment portfolio. The Investment Plan calls for minimizing cash balances while meeting cash flow requirements. In 2007 the Fund adopted a rebalancing strategy that would enhance the Fund's liquidity profile by providing a ready pool of cash that would be equitized with synthetic investments, including futures and swaps, to provide measured equity and fixed income exposure. So, while the cash balances have increased, it has not resulted in an effective increase of the Fund's allocation to cash. The Fund was able to preserve its historical asset allocation of zero percent to cash; while earning market returns as though those funds were invested in equity or fixed income markets. The rebalancing strategy does not use leverage.

Exposure to commodity markets is achieved, in part, by using swap contracts to generate returns consistent with the Goldman Sachs Commodity Index (GSCI). Those contracts overlay a highly liquid, intermediate duration U.S. TIPS portfolio of approximately $706 million. The fund also holds over $4 billion in highly liquid large cap equity securities. Investments in real estate and alternative investments are generally considered illiquid. Because of their characteristics, investments in emerging market debt and fund-of-hedge-funds strategies, are not considered a primary source of liquidity.

Condensed Financial Information
(in Millions)

Net Assets

Assets:	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Total receivables	$296	39	257	(471)	728
Total investments	35,699	3,648	32,051	3,474	28,577
Security lending collateral pool	2,636	(603)	3,239	123	3,116
Total assets	38,631	3,084	35,547	3,126	32,421
Liabilities:					
Accounts payable and accrued expenses	58	(11)	69	(3)	72
Investment purchases and other liabilities	421	235	186	(295)	481
Obligations under security lending	2,636	(603)	3,239	123	3,116
Total liabilities	3,115	(379)	3,494	(175)	3,669
Total net assets	**$35,516**	**3,463**	**32,053**	**3,301**	**28,752**

Changes in Net Assets

Additions:	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Member contributions	$334	16	318	12	306
Employer contributions	244	48	196	48	148
Investment gain	5,246	516	4,730	1,107	3,623
Total additions	5,824	580	5,244	1,167	4,077
Deductions:					
Benefits and refunds	2,336	417	1,919	(24)	1,943
Administrative expenses	25	1	24	1	23
Total deductions	2,361	418	1,943	(23)	1,966
Increase in net assets	**$3,463**	**162**	**3,301**	**1,190**	**2,111**

Statements of Plan Net Assets
As of December 31, 2007 and 2006
(Dollar Amounts in Thousands)

	2007	2006
Assets:		
Receivables:		
Plan members	$ 855	682
Employers	7,752	7,824
Investment income	84,374	86,140
Investment proceeds and other receivables	190,076	157,368
Miscellaneous	12,472	4,536
Total receivables	295,529	256,550
Investments:		
Short-term investments	1,183,444	717,568
United States government securities	2,363,079	2,356,930
Corporate and foreign bonds and notes	2,595,382	2,895,263
Common and preferred stocks	6,550,846	7,643,937
Collective trust funds	4,901,215	3,535,532
Fund of hedge funds	9,520,352	8,153,360
Real estate	3,044,609	2,521,441
Alternative investments	5,540,567	4,227,663
Total investments	35,699,494	32,051,694
Securities lending collateral pool	2,635,880	3,239,461
Total assets	38,630,903	35,547,705
Liabilities:		
Accounts payable and accrued expenses	58,004	68,822
Investment purchases and other liabilities	420,821	186,592
Obligations under securities lending	2,635,880	3,239,461
Total liabilities	3,114,705	3,494,875
Net assets held in trust for pension benefits	**$ 35,516,198**	**32,052,830**

(A Schedule of Funding Progress is presented on page 22.)

These financial statements should be read only in connection with the accompanying notes to the financial statements.

Statements of Changes in Plan Net Assets
For the Years Ended December 31, 2007 and 2006
(Dollar Amounts in Thousands)

	2007	2006
Additions:		
Contributions:		
Plan members	$333,818	317,790
Employers	243,936	196,420
Total contributions	577,754	514,210
Investment gain:		
Net appreciation in fair value of investments	4,164,231	3,723,160
Collective trust fund appreciation and income	798,941	641,718
Interest	347,507	350,783
Dividends	149,488	152,690
Real estate	112,148	145,871
Miscellaneous	6,149	3,519
	5,578,464	5,017,741
Investment expenses	(344,707)	(298,204)
Net gain from investing activities	5,233,757	4,719,537
From securities lending activities:		
Securities lending income	155,067	170,675
Securities lending expenses	(142,094)	(160,169)
Net income from securities lending activities	12,973	10,506
Total net investment gain	5,246,730	4,730,043
Total additions	5,824,484	5,244,253
Deductions:		
Benefits	2,328,185	1,911,330
Refunds of contributions	8,183	8,096
Administrative expenses	24,748	23,868
Total deductions	2,361,116	1,943,294
Net increase	3,463,368	3,300,959
Net assets held in trust for pension benefits:		
Balance, beginning of year	32,052,830	28,751,871
Balance, end of year	**$ 35,516,198**	**32,052,830**

These financial statements should be read only in connection with the accompanying notes to the financial statements.

(Dollar Amounts in Thousands)

(1) Organization and Description of the System

(a) Organization

The Commonwealth of Pennsylvania State Employees' Retirement System (the System) was established as of June 27, 1923, under the provisions of Public Law 858, No. 331. The System was developed as an independent administrative agency of the Board which exercises control and management of the System, including the investment of its assets. The System's board has eleven members including the State Treasurer (ex officio), two Senators or former Senators, two members or former members of the House of Representatives, and six members appointed by the Governor, one of whom is an annuitant of the System. At least five board members are active members of the System and at least two have ten or more years of credited service.

The System is the administrator of a cost-sharing multiple-employer defined benefit retirement plan established by the Commonwealth of Pennsylvania (Commonwealth) to provide pension benefits for employees of state government and certain independent agencies. The System is a component unit of the Commonwealth and is included in the Commonwealth's financial report as a pension trust fund. Administration costs are financed through contributions and investment earnings.

Membership in the System is mandatory for most state employees. Members and employees of the General Assembly, certain elected or appointed officials in the executive branch, department heads, and certain employees in the field of education are not required, but are given the option to participate. At December 31, 2007 and 2006, System membership consisted of:

System Membership

	2007	2006
Retirees and beneficiaries currently receiving benefits	107,130	102,060
Terminated employees entitled to benefits but not yet receiving them	5,692	5,843
Current active employees	109,610	110,972
Total members	**222,432**	**218,875**
Number of participating agencies	108	108

(b) Pension Benefits

The System provides retirement, death, and disability benefits. Cost of Living Adjustments (COLA) are provided at the discretion of the General Assembly. Article II of the Commonwealth of Pennsylvania's Constitution assigns the authority to establish and amend the benefit provision of the plan to the General Assembly.

Employees who retire at age 60 with 3 years of service, or with 35 years of service if under age 60, are entitled to a normal annual retirement benefit. Members of the General Assembly and certain employees classified in hazardous duty positions can retire with full benefits at age 50, with at least 3 years of service.

Most members of the System, and all state employees hired after June 30, 2001 (except State Police officers and certain members of the judiciary and legislators), are Class AA members. The multiplier for Class AA is 1.25, which translates into an annual benefit of 2.5% of the member's highest three-year average salary times years of service and became effective for members July 1, 2001. The general annual benefit for Class A members is 2% of the member's highest three-year average salary times years of service. State police are entitled to a benefit equal to a percentage of their highest annual salary, excluding their year of retirement. The benefit is 75% of salary for 25 or more years of service and 50% of salary for 20-24 years of service. Judges are entitled to a benefit of 4% of final average salary for each of the first 10 years of service and 3% for subsequent years. District Justices are entitled to a benefit of 3% of final average salary for each year of service. Act 9 also created a new class of service for current legislators, Class D-4. The multiplier for Class D-4 is 1.5, which translates into an annual benefit of 3% of the final average salary for each year of service. Most members vest with 5 years of credited service.

According to the Retirement Code, all obligations of the System will be assumed by the Commonwealth should the System terminate.

(c) Contributions

The System's funding policy, as set by the System's Board, provides for periodic active member contributions at statutory rates. The System's funding policy also provides for periodic employer contributions at actuarially-determined rates, expressed as a percentage of annual covered payroll, such that they, along with employee contributions and an actuarially determined rate of investment return, are adequate to accumulate assets to pay benefits when due. A variation of the entry-age normal actuarial cost method is used to determine the liabilities and costs related to all of the System's benefits, including superannuation, withdrawal, death, and disability benefits, and to determine employer contribution rates. The significant difference between the method used for the System and the typical entry-age normal actuarial cost method is that the normal cost is based on the benefits and contributions for new employees rather than for all current employees from their date of entry. The System believes that this variation should produce approximately the same results as the typical method over the long run. These rates are computed based upon actuarial valuations on the System's fiscal year end of December 31 and applied to the Commonwealth based on its fiscal year end June 30; therefore, the employer contribution rates, in effect for the System's year-end of December 31, reflect a blended average of calculated rates. The blended contribution rates were as follows:

(Dollar Amounts in Thousands)

Blended Contribution Rates

	2007	2006
Employer normal cost	8.30%	8.32
Amortization of unfunded actuarial assets in excess of liabilities	(11.39)	(12.16)
Amortization of supplemental annuities	5.08	5.35
Minimum rate factor	2.04	2.01
Total employer cost	**4.03%**	**3.52**

In addition to the employer normal cost, the total employer cost includes other costs and credits resulting from COLA differences between actual investment results and actuarial estimated returns, and changes in benefits. These additional costs and credits are amortized over a period of future years as set by the Legislature. On December 10, 2003, Act 2003-40 (Act 40) revised the amortization periods of these additional costs and credits to the following amortization periods:

Act 40 Amortization Periods

Pre-Act 2001-9 funding credit	10 years
Act 2001-9 Liability	30 years
Post 2000 gains and losses	30 years
Existing and future COLAs	10 years

Additionally, Act 40 revised minimum employer contribution rates to 2%, 3%, 4% effective July 1, 2004, 2005, and 2006, respectively. Act 2007-8 established a permanent minimum employer contribution rate floor of 4%.

The general membership contribution rate for all Class A and Class AA members is 5% and 6.25% of salary, respectively. The contribution rate for Class D-4 members is 7.5%. Judges and district justices have the option of electing special membership classes requiring a contribution of 10% and 7.5%, respectively. All employee contributions are recorded in an individually identified account that is credited with interest, calculated at 4% per annum, as mandated by statute. Accumulated employee contributions and credited interest vest immediately and are returned to the employee upon termination of service if the employee is not eligible for other benefits.

(d) Benefits Completion Plan (BCP)

Act 2002-234 amended the State Employees Retirement Code by adding Section 5941 to the Code. Section 5941 directs the State Employees Retirement Board to establish and serve as trustee of a retirement benefit plan that is in conformity with Internal Revenue Code (IRC) Section 415(m), the Benefits Completion Plan (BCP). The BCP is a separate trust fund established to provide benefits to all annuitants of the System's Defined Benefit Plan and their survivor annuitants and beneficiaries whose retirement benefit exceeds the IRC Section 415(b) limits.

The BCP is funded on an annual basis. A monthly annuity or death benefit is paid under the BCP only if a corresponding monthly annuity or death benefit is paid from the Defined Benefit Plan to the extent permitted by IRC Section 415(b) and the Retirement Code. At December 31, 2007, there were 13 members receiving benefits from the BCP.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

The financial statements of the System are prepared on the accrual basis of accounting under which expenses are recorded when the liability is incurred, revenues are recorded in the accounting period in which they are earned and become measurable, and investment purchases and sales are recorded as of their trade date. Member and employer contributions are based on when member salaries are earned and are recognized when due, pursuant to statutory requirements and formal commitments. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

(b) Use of Estimates

Management of the System has made certain estimates and assumptions relating to the reporting of assets and liabilities, and the disclosure of contingent assets and liabilities, to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

Investments in venture capital, alternative investments, and real estate are generally illiquid. Because of the inherent uncertainty in valuing privately held securities, the fair value may differ from the values that would have been used had a ready market for such securities existed, and the difference can be material. Accordingly, the realized value received upon the sale of the asset may differ from the fair value.

(c) Investments

The System's investments are reported at fair value. Fair value is the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller – that is, other than in a forced or liquidation sale. The investments in short-term investment funds, including those managed by the Treasurer of the Commonwealth of Pennsylvania, are reported at cost plus accrued interest, which approximates fair value. The security lending collateral pool, which is a fund operated by the securities lending agent, also is accounted for at cost plus accrued interest, which approximates fair value. U.S. government securities, corporate and foreign bonds and notes, common and preferred stocks, and the underlying holdings in funds-of-hedge funds, are generally valued based on published market prices and quotations from national security exchanges and securities pricing services. Securities that are not traded on a national security exchange are valued by the asset manager or third parties based on similar sales. The System has entered into certain swap contracts with a notional amount equivalent to the System's investment in funds-of-hedge funds which are designed to produce low volatility, uncorrelated, diversified returns that will help preserve and enhance the real value of the Fund over long periods of time. Real estate is primarily valued based on independent appraisals. Properties that have not been appraised are valued using the present value of the projected future net income stream. Alternative investments, which include interests in limited partnerships invested in venture capital, leveraged buyouts, private equities, and other investments, are valued based on estimated fair value established by valuation committees, which are subject to an annual independent audit. Foreign exchange and futures contracts are marked-to-market daily with changes in fair value recognized as part of investments and investment income. The fair value of equity and commodity swaps are determined no less than monthly based on the return of the underlying indices, which is generally exchanged for a short-term rate plus a spread.

The collective trust funds (CTF) consist primarily of domestic and international institutional mutual and index funds. The funds do not pay interest or dividends to shareholders, and reinvest all income earned on securities held by the fund. The fair value of the CTF is based on the reported share value of the respective fund. The CTF is subject to annual independent audit.

Unsettled investment sales are reported as investment proceeds receivable and unsettled investment purchases are reported as investment purchases payable. Investment expenses consist of investment managers' fees and those expenses directly related to the System's investment operations.

(d) Commitments

As of December 31, 2007 and 2006, the System had contractual commitments totaling approximately $4.0 billion and $3.7 billion, respectively, to fund future alternative investments, and $591 million and $548 million, respectively, to fund future real estate investments.

(e) Compensated Absences

The System accrues a liability for vacation leave as the benefits are earned by the employees to the extent the System will compensate the employee for the benefits through paid time off or some other means, such as cash payments at termination or retirement. Vacation leave vests 100% at the time it is earned up to 45 days, which is carried over to the next year at December 31. The System also accrues a liability for sick leave as the benefits are earned by the employees to the extent the System will compensate the employee for the benefits through cash payments at termination or retirement. Retiring employees of the System that meet service, age, or disability requirements are paid between 30% and 100% of sick days available at retirement, up to 163 maximum days. As of

(Dollar Amounts in Thousands)

December 31, 2007 and 2006, $2.7 million and $2.8 million, respectively, was accrued for unused vacation and sick leave for System employees.

(f) Federal Income Taxes

Management believes the System meets the definition of a Governmental Plan. In the System's communications with the Internal Revenue Service (IRS), it has been treated as a qualified plan, and is, therefore, considered exempt from federal income taxes. Therefore, the System has not requested a determination letter from the IRS relating to the status of the System under the Internal Revenue Code.

(g) Risk Management

The System is exposed to various liabilities and risks of loss related to theft or destruction of assets, injuries to employees, and court challenges to fiduciary decisions. As an administrative agency of the Commonwealth, the System is accorded sovereign immunity. The System participates in certain Commonwealth pooled insurance programs and requires asset managers to carry certain insurance coverage. The System is self-insured for fiduciary and director and officer liability. During the past three years, SERS' insurance settlements did not exceed insurance coverage.

(3) Description of Funds

The Retirement Code requires the System to maintain the following funds representing the net assets held for future and current benefit payments:

The **Member Savings Account** accumulates contributions and interest earnings of active employees. Member balances are transferred to the Annuity Reserve Accounts as members retire.

The **State Accumulation Account** accumulates contributions of the employer and the net earnings of the fund. Funds are transferred to the Annuity Reserve Accounts as members retire. The amount transferred is determined actuarially.

The **Supplemental Annuity Account** accumulates contributions for supplemental annuities. The negative balances represent the liability for past cost of living adjustments that are being amortized to actuarial required contributions. The balance in this account is actuarially determined.

The **Annuity Reserve Accounts** are the accounts from which all death and retirement benefits and supplemental annuities are paid. The balance in this account is actuarially determined.

The **Interest Reserve Account** accumulates all income earned by the fund and from which all administrative and investment expenses incurred by the fund and the Board necessary for operation of the System are paid. Any balance in this reserve is transferred to the State Accumulation Account at year-end.

The **Benefit Completion Plan (BCP) Reserve Account** accumulates all BCP employer contributions and net earnings of the fund less any benefits paid out of the fund.

Fund balances at December 31, 2007 and 2006 are as follows:

Funds

	2007	2006
Members Savings Account	$3,849,293	3,916,841
State Accumulation Account	16,227,380	14,960,940
Supplemental Annuity Account	(999,666)	(1,173,628)
Annuity Reserve Accounts:		
Annuitants and Beneficiaries	15,008,395	12,992,383
State Police	1,381,739	1,310,797
Enforcement Officers	44,065	41,780
Benefit Completion Plan Reserve Account	4,992	3,717
Total	**$35,516,198**	**32,052,830**

(4) Investments

As provided by statute, the System's Board has exclusive control and management responsibility of System funds and full power to invest the funds. In exercising its fiduciary responsibility to System membership, the Board is governed by the "prudent investor" rule in establishing investment policy. The "prudent investor" rule, requires the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence, who are familiar with such matters, exercise in the management of their own affairs not in regard to speculation, but in regard to permanent disposition of the funds, considering the probable income to be derived therefrom, as well as the probable safety of their capital. The Board has adopted its Statement of Investment Policy to formally document investment objectives and responsibilities. This policy, as well as applicable state law, establishes guidelines for permissible investments of the System.

The System's investments are subject to various risks. Among these risks are custodial credit risk, credit risk, interest rate risk, and foreign currency risk. Each one of these risks is discussed in more detail below.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System would not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Pursuant to Title 71, Pennsylvania Consolidated Statutes Section 5931 [c], the State Treasurer serves as custodian of the fund. In accordance with a contractual relationship between the Commonwealth's Treasury Department and its custodial agent, substantially all investments, where securities are used as evidence of the investment, are held by the custodian in book-entry form in the System's name. Those investments are defined as insured or registered investments for which the securities are held by the System or its agent and, therefore, have very minimal level of custodial credit risk losses. All remaining investments do not have securities that are used as evidence of the investments. These investments are primarily in collective trust funds and limited partnerships, which include real estate, alternative investments, and absolute return funds-of-funds.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of a debt instrument is measured by nationally recognized statistical rating agencies such as Moody's Investors Services (Moody's), Standard & Poor's, and Fitch Ratings (Fitch). As directed by the System's investment policy, each year the Board approves an *Annual Strategic Investment Plan*. This plan manages the overall credit risk of the fixed income asset class through a clearly defined long-term asset allocation policy, which established a long-term target allocation to the fixed income asset class at 15% of the Fund. Of the 15% allocation, 6% of the Fund will be allocated to a core segment of the fixed income asset class and composed of investment grade, relatively liquid public domestic securities. These securities will be comprised of two components: 1) a dedicated portfolio of Treasury Inflation-Protection Securities (TIPS) that are designed to capture unanticipated changes in inflation, and 2) Treasury and credit strategies based on the Lehman Aggregate Index. In addition to the core segment, the system will also allocate fixed income investments to a high yield segment. The high yield segment is composed primarily of less liquid, public and private securities and has a target allocation of 5% of the Fund. The high yield component will focus on debt instruments offering higher return premiums and different risk characteristics than traditional core fixed income securities. The fixed income class also has dedicated a 4% allocation of the fund to emerging market debt. Emerging market debt investments are made using dollar denominated sovereign debt as well as local currency sovereign and corporate debt. For securities exposed to credit risk in the fixed income portfolio, the table on the following page discloses aggregate fair value, by the least favorable credit rating issued using Moody's, Standard & Poor's, and Fitch credit ratings at December 31, 2007 and 2006.

U.S. Treasuries with a fair value of $1.8 billion and $1.9 billion as of December 31, 2007 and 2006 respectively, were not included in the table on the next page because they are not subject to credit risk.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. As a means for limiting the System's exposure to fair value losses arising from rising interest rates, the System's long-term asset allocation policy diversifies its fixed income core segment. Duration is a measure of an investment's sensitivity to changes in interest rates. The higher the duration, the greater the changes in fair value when interest rates change. The System measures interest rate risk using option-adjusted duration, which considers the effect of a security's embedded options on cash flows. At December 31, 2007 and 2006, the System's fixed income portfolio had the option-adjusted durations by fixed income sector as listed in the table on the next page.

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. As part of the System's program to manage risk and enhance returns, the System invests in global markets. At December 31, 2007 and 2006, the System had the currency exposures listed in the tables on page 16.

(Dollar Amounts in Thousands)

Fixed Income Securities Exposed to Credit Risk

Rating[a.]	2007 Fair Value	2006 Fair Value
AGY[b.]	$542,683	458,711
AAA	432,948	601,617
AA	45,576	52,653
A	215,069	227,139
BAA	295,343	383,152
BA	616,948	622,479
B	799,257	721,218
CAA	177,688	195,787
CA	2,202	1,677
C	2,893	1,963
D	11,834	5,560
NA[c.]	109,647	270,431
STIF[d.]	1,066,068	532,186
Total	**$4,318,156**	**4,074,573**

[a.] The rating represents all of the securities that fall within Moody's equivalent subcategories of the ratings shown in this table. For example, a security with a rating of Ba1 is shown as a rating of BA in this table.

[b] AGY rating is assigned to securities issued by privately owned government sponsored enterprises (GSEs) such as Federal National Mortgage Association (Fannie Mae), Federal Home Loan Bank Corporation (Freddie Mac) and several others entities that do not have a rating. Although created by Congress as a publicly chartered entity, GSE issued securities are not U.S. backed government securities and, therefore, are subject to credit risk.

[c.] NA represents securities that were either not rated or had a withdrawn rating. NA also includes the fair value of certain swaps, which by nature do not have credit quality ratings. See Note 6 for additional information regarding the nature of these swap agreements.

[d.] Represents investments in the Commonwealth Treasury Department's Short-Term Investment Fund (STIF). This fund is comprised of short-term, investment grade securities, which are mainly U.S. Treasuries, agencies, or repurchase agreements.

Fixed Income Portfolio Option-Adjusted Durations

	2007		2006	
Fixed Income Sector	Fair Value	Option-Adjusted Duration	Fair Value	Option-Adjusted Duration
Agencies	$52,060	2.1	$201,960	2.2
Asset Backed Securities	128,341	0.9	332,130	1.0
CMBS and CMO	327,273	2.3	294,246	1.4
Corporates	1,285,624	3.6	1,329,327	3.2
Government	1,822,787	4.1	1,898,745	4.2
Sovereign Debt	521,593	5.7	561,376	5.6
U.S. Govt Mortgages	488,231	3.2	256,225	2.8
U.S. Private Placements	373,114	4.2	345,986	3.9
STIF	1,066,068	0.1	532,186	0.1
Other Investments[a.]	76,813	N / A	217,579	N / A
Total Fixed Income and STIF	**$6,141,904**		**$5,969,760**	

[a.] Other Investments represents certain securities with maturities ranging through the year 2027 and the value of swap agreements as of December 31.

(Dollar Amounts in Thousands)

Foreign Currency Exposures 2007

Currency	Short Term Investments[a]	Fixed Income	Equity	Real Estate	Alternative Investments	Total
Euro Currency Unit	$21,949	6,367	1,521,034	42,047	233,454	1,824,851
British Pound Sterling	(5,166)	654	961,353	35,058	-	991,899
Japanese Yen	503	-	715,889	60,008	-	776,400
Hong Kong Dollar	(37)	-	360,465	61,956	-	422,384
Swiss Franc	2,899	-	333,979	-	-	336,878
South Korean Won	375	-	196,911	-	-	197,286
Australian Dollar	(1,747)	-	88,637	61,625	-	148,515
Singapore Dollar	526	-	90,663	13,696	-	104,885
Norwegian Krone	(2,712)	-	104,451	1,642	-	103,381
Brazil Real	823	38,944	55,951	2,376	-	98,094
Swedish Krona	(233)	-	95,442	1,536	-	96,745
New Taiwan Dollar	4,824	-	70,948	-	-	75,772
Canadian Dollar	21	6,725	39,454	5,432	-	51,632
S African Comm Rand	51	-	48,586	-	-	48,637
Indian Rupee	(101)	-	47,869	-	-	47,768
Malaysian Ringgit	882	12,264	30,015	-	-	43,161
Mexican New Peso	144	9,743	23,277	-	-	33,164
Danish Krone	(904)	-	29,715	-	-	28,811
Thailand Baht	109	-	27,227	-	-	27,336
Other Currencies (15)	59	26,396	92,441	-	1	118,897
Total	**$22,265**	**101,093**	**4,934,307**	**285,376**	**233,455**	**5,576,496**

[a] *Includes receivables and payables as of December 31, for securities sold and purchased.*

Foreign Currency Exposures 2006

Currency	Short Term Investments[a]	Fixed Income	Equity	Real Estate	Alternative Investments	Total
Euro Currency Unit	$35,572	8,630	1,292,941	52,434	165,942	1,555,519
British Pound Sterling	(851)	-	918,534	64,835	-	982,518
Japanese Yen	(1,486)	-	735,881	61,299	-	795,694
Hong Kong Dollar	1,158	-	314,094	35,942	-	351,194
Swiss Franc	(607)	-	340,506	-	-	339,899
South Korean Won	(559)	-	213,389	-	-	212,830
Australian Dollar	(141)	-	101,932	56,959	-	158,750
Swedish Krona	(364)	-	122,224	5,019	-	126,879
Singapore Dollar	285	-	82,377	10,249	-	92,911
New Taiwan Dollar	1,274	-	88,684	-	-	89,958
Norwegian Krone	3,280	-	81,396	2,444	-	87,120
S African Comm Rand	2,429	-	52,853	-	-	55,282
Brazil Real	400	730	49,011	-	-	50,141
Canadian Dollar	17	3,568	25,197	13,086	-	41,868
Mexican New Peso	137	3,186	36,035	-	-	39,358
Danish Krone	144	-	38,748	-	-	38,892
Indian Rupee	2,147	-	33,692	-	-	35,839
Malaysian Ringgit	31	-	27,785	-	-	27,816
Thailand Baht	49	-	22,401	-	-	22,450
Israeli Shekel	1,794	-	20,281	-	-	22,075
Other Currencies (12)	(796)	-	67,424	-	1	66,629
Total	**$43,913**	**16,114**	**4,665,385**	**302,267**	**165,943**	**5,193,622**

[a] *Includes receivables and payables as of December 31, for securities sold and purchased.*

(5) Securities Lending

As provided for by the Master Custody Agreement executed between the Commonwealth's Treasury and the sub-custodian, Title 71 PaC.S.A.; Section 5931(a) authorizes the System to participate in a securities lending program.

The custodian, acting as lending agent, lends the System's equity, debt, and money market securities for cash, securities, or letter-of-credit collateral. Collateral is required at 102% of the fair value of the securities loaned except for the equity securities of non-U.S. corporations, for which collateral of 105% is required. Collateral is marked-to-market daily. If the collateral falls below guidelines for the fair value of the securities loaned, additional collateral is obtained. Cash collateral is invested by the lending agent in accordance with investment guidelines approved by the Board. The lending agent cannot pledge or sell securities collateral unless the borrower defaults.

As of December 31, 2007 and 2006, the System's credit exposure to individual borrowers was limited because the amounts the System owed the borrowers exceeded the amounts the borrowers owed the System. The Treasurer's contract with the lending agent requires the agent to indemnify the System if the borrowers fail to return the underlying securities and the collateral is inadequate to replace the loaned securities or if the borrowers fail to pay income distributions on the loaned securities.

All loaned securities at December 31, 2007 and 2006 could be terminated on demand by either the lending agent or the borrower. Cash collateral is invested, together with the cash collateral on loaned securities of other Commonwealth entities, in a short-term collective investment pool. The duration of the investments in the pool at December 31, 2007 and 2006 was 21 days and 31 days, respectively. The relationship between the average maturities of the investment pool and the System's loans is affected by the maturities of the loans made by other entities in the investment pool. In addition, the interest rate risk posed by mismatched maturities is affected by other program features, such as the lending agent's ability to reallocate loaned securities among all of its lending customers.

As of December 31, 2007 and 2006, the fair value of loaned securities was $3.0 billion and $3.3 billion, respectively; the fair value of the associated collateral was $3.0 billion and $3.4 billion, of which $2.6 billion and $3.2 billion was cash, respectively.

(6) Derivative and Structured Financial Instruments and Restricted Assets

The System enters into certain derivative and structured financial instruments primarily to enhance the performance and reduce the volatility of its portfolio. It enters into foreign exchange contracts and foreign currency options contracts to hedge foreign currency exposure, futures contracts to gain or hedge exposure to certain equity markets and to manage interest rate risk, and swaps to gain equity exposure on its absolute return fund-of-hedge-funds investments, as well as hedge against the effects of inflation.

Foreign exchange contracts are agreements to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. The System uses these contracts primarily to hedge the currency exposure of its international investments. To reduce the risk of counterparty nonperformance, the System generally enters into these contracts with institutions regarded as meeting high standards of credit worthiness. The unrealized gain / loss on contracts is included in the System's net assets and represents the fair value of the contracts on December 31. The figures for 2007 are significantly lower than 2006 due to the termination of the currency overlay program. At December 31, 2007 and 2006, the System's contracts to purchase and sell by major foreign currencies were as listed in the tables on the next page.

(Dollar Amounts in Thousands)

Foreign Exchange Contracts

Contracts as of December 31, 2007

Currency	Purchases	Unrealized Gain/(Loss)	Sells	Unrealized Gain/(Loss)
Japanese Yen	$65,781	2,409	61,499	(2,174)
Swiss Franc	28,623	1,883	38,190	(1,772)
Euro Currency Unit	9,678	(30)	53,968	(946)
British Pound Sterling	5,222	(12)	95,476	1,835
Chinese Yuan Renminbi	3,598	37	1,886	(12)
Brazil Real	2,820	258	3,777	(287)
Norwegian Krone	2,742	12	-	-
Russian Rubel	2,214	61	-	-
Hong Kong Dollar	1,741	1	1,800	(1)
Australian Dollar	1,297	1	-	-
Other (10)	2,515	(11)	3,344	(47)
Total	**$126,231**	**4,609**	**259,940**	**(3,404)**

Contracts as of December 31, 2006

Currency	Purchases	Unrealized Gain/(Loss)	Sells	Unrealized Gain/(Loss)
Japanese Yen	$2,035,285	(99,167)	2,926,774	106,071
Euro Currency Unit	1,494,543	34,171	1,627,684	(49,116)
British Pound Sterling	979,649	36,015	1,101,384	(46,925)
Swiss Franc	607,661	(2,890)	712,462	(3,192)
Swedish Krona	110,668	5,054	121,841	(6,957)
Australian Dollar	76,156	2,271	87,091	(3,893)
Other (8)	6,390	34	8,203	(34)
Total	**$5,310,352**	**(24,512)**	**6,585,439**	**(4,046)**

(Dollar Amounts in Thousands)

Futures contracts are standardized, exchange-traded contracts to purchase or sell a specific financial instrument at a predetermined price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. Because of daily settlement, the futures contracts have no fair value.

The System has entered into certain futures contracts maturing through March 15, 2010. The notional value of these contracts at December 31, 2007 and 2006 is listed below.

The exchange on which futures contracts are traded assumes the counterparty risk and generally requires margin payments to minimize such risk. The System pledges investment securities to provide the initial margin requirements on the futures contracts it buys.

Swap agreements provide for periodic payments between parties based on the change in value of underlying assets, indexes, rates and credit worthiness. During 2007 and 2006, the System entered into commodity swaps, S&P 500 total return swaps, Russell 2000 swaps, MSCI-EAFE swaps, MSCI Emerging Market Free (EMF) swaps, credit default swaps, and interest rate swaps. Under the commodity swap arrangement, the System receives the net return of the GSCI from the swap counterparty in return for a spread, which it pays to the counterparty. The commodity swaps are used as an inflation hedge and settle on a monthly basis. The S&P 500 total return swaps, Russell 2000 swaps, MSCI-EAFE swaps, and MSCI EMF swaps are used to gain broad market equity exposure on certain absolute return funds-of-funds. Under those arrangements, the System receives the net return of the respective equity indices in exchange for a short-term rate plus a spread. The System uses multiple contracts with counterparties as well as collateral posting requirements to manage its counterparty credit risk. The contracts have varying maturity dates ranging from February 20, 2008 through December 31, 2008. Credit default swaps are agreements with counterparties to either purchase or sell credit protection. The System's advisors use credit default swaps to either increase or decrease credit exposure to certain credit markets. Interest rate swaps are over-the-counter contracts that allow counterparties to exchange a fixed rate liability for a floating rate liability. The System uses interest rate swaps as the most cost-effective way of gaining exposure to certain sectors of the fixed income market.

The below table presents the System's swap exposure at December 31.

Futures Contracts

	2007		2006	
	Buy Contracts	Sell Contracts	Buy Contracts	Sell Contracts
Treasury Futures	$510,799	302,933	236,184	28,972
S&P 500 Futures	86,564	-	-	-
Russell 2000 Futures	14,595	-	-	-
Eurodollar Futures	316,550	56,741	168,337	142,155

Swap Exposure

	Notional Value		Receivable/(Payable)	
	2007	2006	2007	2006
S&P 500 Total Return Index	$4,761,782	5,493,078	32,786	440,484
MSCI EAFE Index	1,581,651	2,451,978	(17,591)	97,293
MSCI EMF Index	87,503	-	2,821	-
GSCI	711,885	1,595,177	39,146	(117,788)
Russell 2000 Index	349,517	498,704	(1,540)	(500)
Interest Rate	130,000	22,550	(236)	867
Credit Default	121,325	239,200	(2,729)	1,577

The System mitigates its legal risk on investment holdings, including the previously discussed instruments, by carefully selecting portfolio managers and extensively reviewing their documentation. It manages its exposure to market risk within risk limits set by management.

The System also indirectly holds foreign exchange contracts, futures contracts, and certain swap contracts through its investments in collective trust funds. Those collective trust funds invest in those instruments directly, and indirectly (through a securities lending collateral pool), to hedge foreign exchange exposure, to synthetically create equity-like returns, and to manage interest rate risk by altering the average life of the portfolio.

(7) Commission Recapture Program

The System has commission recapture contracts with several brokers. These contracts generally stipulate that the brokers rebate a percentage of commissions earned on investments directly to the System. During the years ended December 31, 2007 and 2006, the System earned $254 thousand and $310 thousand of benefits resulting from a commission recapture program, respectively. No expenditures were paid from the program in either year. At December 31, 2007 and 2006, the System has accumulated $3.4 million and $3.2 million, respectively, that are available for future expenditures.

(8) Pension Plan for Employees of the System

The System makes employer contributions to the pension plan. The System's employees' contribution requirements and benefits are described in Note 1 to these financial statements. The System also participates in the Commonwealth of Pennsylvania Office of Administration's (OA's) Retired Employees Health Program (REHP). The REHP is a single-employer plan and provides certain healthcare benefits to qualifying individuals meeting specified age and / or service requirements. The Office of Administration, in its sole discretion, determines available REHP benefits on an ongoing basis. REHP funding is arranged between OA and the Pennsylvania Employees' Benefit Trust Fund (PEBTF). The PEBTF is a third-party administrator for the REHP under the provisions of an Administrative Agreement between OA and PEBTF.

(9) Litigation and Contingencies

The System is involved in various individual lawsuits, generally related to benefit payments, which, if settled adversely, could increase estimated actuarial liabilities by approximately $1 billion. Some of the individual cases involve legal issues that, if extended to the entire membership, may result in significant costs to the System. If such an event were to occur, the additional costs would be recovered by the System through adjustments to the employer contribution rate.

(10) Additional Pension Disclosures as Mandated by GASB 50

(a) Plan Description

The System is the administrator of a cost-sharing multiple-employer defined benefit pension plan. The System provides retirement, death, and disability benefits. COLAs are provided at the discretion of the General Assembly. The System was developed as an independent administrative agency of the Board which exercises control and management of the System, including the investment of its assets. The System issues a publicly available financial report that includes financial statements and required supplementary information.

The System's investments are reported at fair value as discussed in Note 2 (c) Summary of Significant Accounting Policies. The annual required contribution (ARC) is actuarially determined. There is no maximum annual contribution rate; however the minimum has been set at 4% through Act 8.

(b) Funding Status and Funding Progress

As of December 31, 2007, the most recent actuarial valuation date, the plan was 97.1% funded. The actuarial accrued liability for benefits was $31.8 billion, and the actuarial value of assets was $30.8 billion, resulting in an unfunded actuarial accrued liability (UAAL) of $0.9 billion. The covered payroll (annual payroll of active employees covered by the plan) was $5.5 billion, and the ratio of the UAAL to the covered payroll was 16.5%.

The schedule of funding progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

(c) Actuarial Methods and Assumptions

In the December 31, 2007 actuarial valuation, a variation of the entry-age actuarial cost method was used. The significant difference between the method used for SERS and the typical entry-age actuarial cost method is that the normal cost is based on the benefits and contributions for new employees rather than for all current employees from their date of entry. The SERS variation should produce approximately the same results as the typical method over the long run. The actuarial assumptions included (a) 8.5% investment rate of return, (b) projected salary increases ranging from 4.9 to 20.2% with an average increase of 7.1%, and (c) 3.0% rate of inflation. The assumptions did not include a cost-of-living adjustment. The remaining amortization period at December 31, 2007, was 4 - 30 years.

(11) Reclassification

Certain amounts in the 2006 financial statements have been reclassified to be in conformity with the presentation of these amounts in the 2007 financial statements.

This information is an integral part of the accompanying financial statements.

Schedule 1
Schedule of Funding Progress
(Dollar Amounts in Millions)

Actuarial Valuation Year Ended December 31	Actuarial Value of Assets	Actuarial Accrued Liabilities (AAL)	Unfunded Actuarial Accrued Liabilities (UAAL)	Ratio of Assets to AAL	Covered Payroll	UAAL as a Percentage of Covered Payroll
2007	$30,840	31,754	914	97.1%	$5,529	16.5%
2006	28,149	30,365	2,216	92.7	5,662	39.1
2005	26,794	28,852	2,058	92.9	5,138	40.1
2004	26,900	27,999	1,099	96.1	5,094	21.6
2003	27,466	26,180	(1,286)	104.9	4,965	(25.9)
2002	27,498	25,650	(1,848)	107.2	5,093	(36.3)

Schedule 2
Schedule of Employer Contributions
(Dollar Amounts in Thousands)

Year Ended December 31	Annual Required Contributions	Percentage Contributed
2007	$617,253	39.3%
2006	548,745	35.6
2005	319,190	46.1
2004	105,229	100.0
2003	55,079	123.4
2002	22,906	221.9

During the years 2003 and 2002, actual contributions exceeded the Annual Required Contributions (ARC). For the period July 1, 2001 through June 30, 2003 the ARC was set at zero. However, the System required payment from certain agencies that provided age 50 retirement and from special classes for payment for past liabilities for retroactive benefit enhancements. Collection of those amounts resulted in the actual contributions exceeding the ARC.

See accompanying notes to required supplementary schedules of funding progress and employer contributions.

Actuarial Information as of the Latest Actuarial Valuation

Valuation date	December 31, 2007
Actuarial cost method (b)	Variation of entry-age actuarial cost method
Amortization method (a)	10 year and 30 year schedules with level payments
Remaining amortization period (a)	4 - 30 years, closed
Asset valuation method	5-year smoothed market
Actuarial assumptions:	
Investment rates of return (c)	8.5%
Projected salary increases (c)	4.9% - 20.2%, average of 7.1%
Cost-of-living adjustments (d)	As described below

GASB 25 establishes a range of actuarial cost and amortization methods for the Unfunded Actuarial Accrued Liability. The scheduled payments for the year beginning July 1, 2005 are below the minimum amount required to meet the GASB 25 minimum. This is a temporary result of financing implemented by Act 2003-40 in December 2003. After 2009, the employer contribution is expected to exceed the GASB 25 minimum.

(a) The December 31, 2001 valuation included the effect of Act 9, which increased the actuarial accrued liabilities by approximately $2.7 billion. Act 2003-40 revised the amortization method and remaining amortization periods as discussed in Note 1(c) to the audited financial statements.

(b) A variation of the entry-age normal actuarial cost method is used to determine the liabilities and costs related to all of the System's benefits including superannuation, withdrawal, death and disability benefits. The significant difference between the method used for the System and the typical entry-age normal actuarial cost method is that the normal cost is based on the benefits and contributions for new employees rather than for all current employees from their date of entry. This variation should produce approximately the same results as the typical method over the long run.

(c) Includes inflation at 3%.

(d) Information presented in the required supplementary schedules was determined as part of the actuarial valuation at the dates indicated. The effects of COLAs granted to annuitants were included in the respective valuations as presented in the table below:

Effects of COLAs

Valuation Year	Effective Retirement Date	COLA Range (based on date of retirement)	Effective Date of COLA	Increase to Actuarial Accrued Liabilities
2002	Between July 2, 1990 and July 1, 2002	2.3% - 9.0%	July 1, 2003	$396 million
2002	On or before July 1, 1990	8.0 - 25.0	July 1, 2002	257 million
1997	On or before June 30, 1997	1.9 - 25.0	July 1, 1998	478 million

Schedule of Administrative Expenses
(Dollar Amounts in Thousands)
December 31, 2007

Personnel services:		
Salaries	$10,350	
Benefits	4,768	
Temporary personnel wages, overtime, and outservice training	324	
Total personnel services		$15,442
Professional services:		
Consultant fees	2,451	
Treasury Department services	861	
Commonwealth Central services	591	
Consultant contractual services vendor provided	381	
Consultant services EDP	51	
Legal fees	35	
Total professional services		4,370
Rentals:		
Real estate rent	1,589	
Other equipment rental	388	
Total rentals		1,977
Communication:		
Postage	558	
Telephone	369	
Printing and advertising	203	
Total communication		1,130
Other expenses:		
Supplies	466	
EDP and office equipment	436	
EDP software	354	
Subscriptions and memberships	228	
Maintenance	183	
Travel and conferences	162	
Total other expenses		1,829
Total Administrative Expenses		**$24,748**

Summary of Investment Expenses and Consulting Fees
(Dollar Amounts in Thousands)
December 31, 2007

Investment Expenses

	Fees
Investment manager fees:	
Alternative Investments	$115,178
Equities	115,015
Real Estate	42,097
Absolute Return	22,689
Fixed Income	18,813
Inflation Protection	13,349
Total investment manager fees	327,141
Investment Related Expenses:	
Alternative Investments	12,215
Real Estate	5,265
Custodial	225
Other	(139)
Total investment related fees	17,566
Total Investment Expenses	**$344,707**

Consulting Fees

Firm	Category	Fees
Cambridge Associates, LLC	Private Equity	$1,133
Rocaton Investments Advisors, LLC	General Consultant	467
Hay Goup Inc.	Actuary	263
The Townsend Group	Real Estate	229
EFL Associates of Colorado	General Consultant	130
Institutional Shareholder Services	Proxy Services	103
Other		126
Total Consulting Fees		**$2,451**

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Investment Section

John C. Winchester
Chief Investment Officer

May 30, 2008

Dear Members:

I am pleased to present the results of the investment operations for SERS for the calendar year 2007. The data contained in the Investment Section was compiled in conjunction with SERS investment, financial reporting and auditing staff; SERS' consultants Rocaton Investment Advisors, Cambridge Associates and the Townsend Group; and our custodian, BNY Mellon. Performance was calculated using the Modified Dietz day–weighted return methodology.

The growth and changes to the Fund are managed in accordance with the investment policy and objectives set out by the Board, operating as fiduciaries in the sole interest of the beneficiaries and members of the Fund. The primary investment objective is to assure the adequate accumulation of reserves in the Fund at the least cost to the citizens of the Commonwealth, while preserving the principal of the Fund against erosion due to inflation. The objectives further state that the Board seeks to meet these objectives within acceptable risk parameters through adherence to a policy of diversification of investments by type, industry, investment manager style and geographic location. As a long–term investor, this concept of diversification is key, as it allows the Fund to achieve its return objectives while controlling risk.

The SERS Investment Office, in conjunction with the Fund's three consultants, performs a review of the asset allocation annually, recommending modifications to asset classes and future allocations as appropriate. The results are reviewed and adopted by the Board. The asset allocation decisions are among the most important decisions the Board makes in striving to achieve the Fund's investment objectives. The Fund invests in a broad range of diversified asset classes and strategies. Perusal of the Investment Summary in the following pages will reveal the diversification of both asset classes and investment manager styles.

Following are some highlights of the investment program during 2007:

The financial markets were bifurcated in 2007. The first half of the year saw continued economic growth and generally favorable financial markets. However, declining housing prices fueled speculation about the safety of mortgage investments. The second half of the year experienced a complete reversal of investor sentiment. As investors realized that mortgage defaults were imminent based on rapidly declining real estate values, and as a result, investments in these mortgages were at risk, a sharp correction occurred. Investors suddenly became risk averse, with the fixed income and cash markets virtually shutting down.

Despite the sharp reversal in investor sentiment, SERS was relatively immune to events that occurred in the latter half of the year. Stock and fixed income investments were affected, but the diversification of asset classes and investment strategies built into the investment program proved their worth. The 2007 investment return for the Total Fund was 17.2%. This performance ranked SERS among the top public pension funds nationwide for 2007.

As always, the performance across asset classes was mixed. The success achieved in 2007 was the result of investing in non–core asset classes such as private equity, real estate and inflation protection (including commodities). The returns of these asset classes, which drove 2007 performance, were private equity, 41.0%;

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inflation protection, 31.4%; and real estate, 22.6%. In addition, all of SERS asset classes out–performed their respective benchmarks in 2007, with the exception of venture capital, which returned 16.7%. Asset classes that did out–perform their benchmarks generated an aggregate 4.5% of return above the Total Fund benchmark. This performance fueled the growth of Fund assets which climbed to $35.5 billion at year–end. SERS' growth in assets is stated net of benefit payments and expenses of $2.4 billion incurred in 2007.

Longer term, SERS' ten year performance was 10.1%, placing SERS in the top quartile of a universe of large public pension funds. This 10.1% return exceeded the actuarial return assumption of 8.5%, thereby contributing significantly toward holding employer contributions at the statutorily required floor of 4.0%, well below the 8.21% normal employer contribution rate. In addition, these returns helped to enhance the well–funded status of the Fund.

SERS continues to invest in the Commonwealth of Pennsylvania, providing funding for investments that have a positive impact on the economy of the State. In aggregate, the Fund had $1.4 billion, or 4.1% of the total Fund, invested in Pennsylvania. Those investments include U.S. stocks, fixed income, real estate, venture capital and private equity asset classes.

As in the past, we caution you not to presume that this past record of performance will persist into the future. Financial markets are cyclical and unpredictable. The events that began to play out in the latter half of 2007 have lingered into 2008, and are expected to take some time to completely work through the system. This environment would lead one to conclude that near–term returns may be somewhat more muted than those experienced in the recent past.

SERS' Investment Office continuously monitors economic and market events, working to position the Fund through broad diversification to perform well under a wide variety of economic scenarios. Under the supervision and guidance of the Board, the Fund is well positioned to ensure that SERS' members receive the financial security that they have earned and deserve.

Sincerely,

John C. Winchester

John C. Winchester
Chief Investment Officer

The State Employees' Retirement Board originally adopted a formal Statement of Investment Policy in 1979. It has been revised periodically, to reflect and incorporate legislative changes governing investments and amendments to policies and procedures guiding the investment of the defined benefit portfolio. The latest Statement of Investment Policy was adopted in 2007. The purpose of the statement is to formalize the Board's investment objectives, policies, and procedures: to establish guidelines for the investment of Fund assets, and to define the duties and responsibilities of the various entities involved in the investment process. The major elements of the statement are:

- As fiduciaries, the Board will exercise that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence, who are familiar with such matters, exercise in the management of their own affairs in investment matters;

- The Fund's overall investment objective is to provide a total rate of return, over full economic cycles, which exceeds the return of a fully diversified market portfolio within each asset class. The Board seeks to meet this objective within acceptable risk parameters through adherence to a policy of diversification of investments by type, industry, quality and geographic location;

- The Board employs an investment staff and also contracts with investment advisors and consultants to provide expert, professional judgment in all investment decisions;

- An annual Investment Plan is prepared to establish the allocation of funds during the year among investment advisors and categories of assets;

- Guidelines are established for each category of assets used by the Fund's investment advisors to provide a framework for monitoring quality, diversification and liquidity; and

- Where investment characteristics, including yield, risk and liquidity are equivalent, the Board's policy favors investments which have a positive impact on the economy of Pennsylvania.

To assure an adequate accumulation of reserves in the Fund at the least cost to the citizens of the Commonwealth and to provide some protection against the erosion of principal by inflation, the long–term investment objectives of the Fund, are:

- Achieve a net total return equivalent to the actuarial return assumption, or preferably in excess of this rate over market cycles in order to improve the funded ratio of the Fund through investment earnings;

- Achieve in Global Stocks a total return that exceeds the total return of the MSCI World Index;

- Achieve in the Stand Alone Absolute Return Strategy a total return that exceeds LIBOR plus 300 basis points;

- Achieve in U.S. Stocks a total return that exceeds the total return of the Russell 3000 Index;

- Achieve in Non–U.S. Stocks a total return that exceeds the total return of the SERS Custom International Stock Index;

- Achieve in the Fixed Income asset class a total return that exceeds the total return of the SERS Custom Fixed Income Index;

- Achieve in Inflation Protection a total return that exceeds the total return of the SERS Custom Inflation Protection Benchmark;

- Achieve in the Real Estate asset class a total return that exceeds the total return of the Townsend Stylized Benchmark;

- Achieve in the Cash asset class a total return that exceeds the total return on U.S. Treasury Bills (90 days);

- Achieve in the Venture Capital asset class a total return that exceeds the Cambridge Venture Capital Benchmark;

- Achieve in the Private Equity asset class a total return that exceeds the Cambridge Private Equity Benchmark.

Total return includes income and both realized and unrealized gains and losses and is computed on market value. The Board seeks to meet these objectives within acceptable risk parameters through adherence to a policy of diversification of investments by type, industry, investment manager style and geographic location.

Schedule of Portfolio Returns* After Fees
For the period ending December 31, 2007

Asset Class	1 Year Total Return	3 Year Total Return	5 Year Total Return	10 Year Total Return
Global Stocks	12.3%	N / A	N / A	N / A
MSCI World	*9.0*	*N/A*	*N/A*	*N/A*
U.S. Stocks	9.5	11.8	16.6	7.8
Russell 3000 Index [a.]	*5.1*	*8.9*	*13.6*	*6.2*
Non–U.S. Stocks	17.0	20.9	24.6	12.0
SERS Custom International Stock Benchmark [b.]	*15.2*	*21.1*	*25.2*	*10.6*
Fixed Income	6.1	6.2	7.8	6.7
SERS Custom Fixed Income Benchmark	*5.4*	*5.7*	*6.5*	*6.0*
Cash	5.1	4.3	3.2	3.9
90 day U.S. T–bills	*5.0*	*4.3*	*3.1*	*3.8*
Real Estate [c.]	22.6	23.5	19.1	14.4
Townsend Stylized Benchmark	*16.6*	*19.1*	*16.6*	*13.4*
Private Equity [c.]	41.0	33.1	27.1	19.2
Cambridge Private Equity Index	*28.0*	*28.9*	*23.5*	*14.9*
Venture Capital [c.]	16.7	11.2	2.6	6.4
Cambridge Venture Capital Index	*22.5*	*14.9*	*8.0*	*15.0*
Inflation Protection [d.]	31.4	15.3	17.0	N / A
SERS Custom Inflation Protection Index	*24.7*	*13.3*	*15.5*	*N/A*
Total Fund	**17.2%**	**16.0**	**17.5**	**10.1**
Total Fund Benchmark	*12.7*	*14.2*	*15.8*	*8.9*

** Returns for periods longer than one year are annualized.*

[a.] The U.S. Stocks Benchmark is the Wilshire 5000 Index through 12/31/98, and the Russell 3000 thereafter.

[b.] The Non–U.S. Stocks Composite and the Custom International Index were hedged between May 1, 1996 ending January 31, 2007.

[c.] Results for the Real Estate, Private Equity, Venture Capital and Indices are lagged one quarter.

[d.] Inflation Protection was initially funded in November, 2001.

Note: Performance was calculated using the Modified Dietz day weighted return methodology.

Domestic Equity

Holding	Fair Value
Virgin Media	$31,517,289
Time Warner Cable	21,961,430
Ansys Inc.	21,567,741
Simon PPTY Group Inc	19,799,476
Schlumberger Ltd	17,391,816
Triumph Group Inc	15,417,567
II-VI Inc	15,189,766
Ansoft Corp	13,525,315
Wabtec	13,468,106
Bentley Systems Inc	13,361,923

International Equity

Holding	Fair Value
Nestle SA	$92,382,387
Cadbury Schweppes	44,462,877
Telefonica SA	42,703,867
Bayer AG	41,835,524
BP PLC	41,343,908
Hutchinson Whampoa	40,972,755
Novartis AG	38,365,914
Mitsubishi Estate Co	37,881,737
British American Tobacco	36,703,167
Vodafone Group	36,031,080

International Fixed Income

Holding	Fair Value
Russian Federation Bond STEP, March 31, 2030	$35,260,557
Federative Republic of Brazil, 10.000% January 1, 2017	23,444,037
Federative Republic of Brazil, 8.000% January 15, 2018	17,900,000
Republic of Venezuela, 9.375% January 13, 2034	14,145,318
Republic of Argentina, 8.280% December 31, 2033	13,591,051
Federative Republic of Brazil, 8.750% February 4, 2025	13,514,425
Videotron Group Ltd Senior Note, 6.875% January 15, 2014	12,872,092
Federative Republic of Brazil, 7.875% March 7, 2015	12,475,650
Petronas Capital Bonds, 7.875% May 22, 2022	12,110,742
Mexico Notes 6.625%, March 3, 2015	11,796,003

US Government and Government Related

Holding	Fair Value
U S Treasury Inflation Index Note, 3.375% January 15, 2012	$308,183,639
U S Treasury Inflation Index Note, 1.875% July 15, 2013	267,397,972
U S Treasury Inflation Index Note, 3.000% July 15, 2012	224,835,664
U S Treasury Inflation Index Note, 2.000% January 15, 2014	156,133,794
U S Treasury Inflation Index Note, 3.500% January 15, 2011	146,424,363
U S Treasury Inflation Index Note, 0.875% April 15, 2010	143,756,405
U S Treasury Inflation Index Note, 2.375% April 15, 2011	142,317,549
U S Treasury Inflation Index Note, 2.000% April 15, 2012	110,615,674
U S Treasury Bond Stripped Principal Payment, 8.750% August 15, 2020	60,909,461
U S Treasury Note, 4.875% August 31, 2008	43,512,392

Domestic Corporate Fixed Income

Holding	Fair Value
Freeport McMoran Copper & Gold, 8.375% April 1, 2017	$32,711,250
Range Residential Corp Senior Sub Note, 7.500% October 1, 2017	31,108,000
Texas Competitive Electric, 8.396% October 10, 2014	22,611,875
NRG Energy Inc Senior Note, 7.375% February 1, 2016	15,892,500
Davita Inc. Senior Sub Note, 7.250% March 15, 2015	14,019,963
Plains Exploration & Production Co Senior Note, 7.750% June 15, 2015	13,600,000
Ford Motor Credit Co Note, 8.000% December 15, 2016	12,974,127
Nalco Company Senior Sub Note, 8.875% November 15, 2013	12,176,400
Dresser Rand Group Inc, STEP November 1, 2014	11,842,340
BNP Paribas NY, 5.000% January 28, 2008	10,000,000

Note: A detailed list of SERS' investment holdings at December 31, 2007, may be viewed at www.sers.state.pa.us

Schedule of Trading Broker Commissions
Year Ended December 31, 2007

Broker	Commissions	Broker	Commissions
C S First Boston	$834,052	Cantor Fitzgerald	$63,533
Merril Lynch	791,623	Euromobilare	61,060
Deutsche Bank	734,216	ING Bank	59,330
UBS Securities	632,684	Oddo Secs	58,147
Goldman Sachs	615,155	Fortis Securities	58,023
J P Morgan	593,633	Petercam	57,801
Salomon Smith Barney	582,065	Warburg Dillon Read	57,417
Lehman Brothers	500,792	KAS Bank	55,165
Morgan Stanley	488,886	Svenska International	51,064
Kleinwort Benson	343,568	Banco De Portugal	51,041
ABN AMBRO	333,289	Caib Securites	50,621
Credit Lyonnais	321,920	Ci Nordic Securities	49,563
Cazenove	254,645	Investec Bank Ltd.	46,651
Bear Stearns	237,969	Boenning & Scattergood	46,327
Credit Agricole	226,448	Egnatia Securities SA	45,696
Union Bank of Switzerland	217,773	Knight Securities Broadcort	45,242
Macquarie Bank	210,129	BNP Capital Markets	43,689
Nomura Bank International	189,684	Rabobank Nederland	42,810
Berenborg Gossler	187,238	Banco Espirito Santo	42,284
Citigroup Global Markets	159,727	Deutsche Securities	41,690
Bank of New York	152,067	Instinet	40,745
Exane	149,134	Nationsbank	40,393
Kay Hian James Capel Ptd	141,204	Jefferies & Company	39,913
Carnegie	134,966	Renaissance Capital	38,489
Bank Am Bellevue	116,988	Mitsubishi Finance Int	38,243
HSBC Securities	114,883	Dexia Bank	37,806
Liquidnet	108,076	Banc of America Securities	37,754
Samsung Securities	102,404	Den Danske Bank	36,944
Pershing	88,925	Caylon Securities	36,938
KBC Bank NV	88,465	Beeson Gregory	35,788
Weeden & Company	86,901	Wachovia Securities	33,679
Julius Baer Securities	82,954	Enskilda Securities	30,709
B Trade Services	82,104	Intermonte Sec Cim	30,654
NZB Neue Zuercher Bank	79,524	Citation Group	29,930
SG Securities	79,276	KBC Peel Hunt	29,766
Sanford C. Bernstein & Co	76,209	Sturdivant & Company	29,017
Investment Technology Group	73,644	GK Goh Securities	28,788
Banco Santander	72,753	Citibank	28,261
Societe Generale	66,580	Janney Montgomery Scott	27,788
ABG Securities	66,378	Raymond James & Assoc. Inc.	27,564

Schedule of Trading Broker Commissions (Continued)

Broker	Commissions	Broker	Commissions
SunTrust Equitable Sec	$27,206	Morgan Keegan	$16,398
Keefe Bruyette & Woods	26,648	Baypint Trading	16,322
Daiwa Bank	26,440	Teather & Greenwood	16,107
Stifel Nicolaus	25,913	Tokyo Mitsubishi Plc	16,048
Heflin & Company	25,449	William Blair & Company	15,712
Numis Securities Ltd	24,797	Man Financial Limited	15,441
CIBC World Mkts Inc	24,722	Europeenne D'Intermediation	14,833
Redburn Partners	23,865	Mogavceo Lee & Company	14,550
West Deutsche Landesbanken	23,275	Wave Securities	14,330
Westminster Research Associates	23,148	Brockhouse And Cooper	13,903
Oppenheimer	23,010	CIMB Investment Bank	13,900
Davy Stockbrokers	21,843	China Intl Cap Corp Hk Secs	13,812
Mizuho Securities	21,802	SG Cowen Securities	13,799
Pulse Trading	20,575	UNX Com	13,487
Svenska Handelsbanken	20,056	Pereire-Tod Ltd	12,545
Singer And Friedlander	20,037	RBC Dominion Sec. Corp.	12,178
Capital Institutional Investors	20,021	La Branche Financial	12,139
Finsettle Services Pty	19,107	Thomas & Weisel	11,888
Panmure Gordon And Company	18,351	Baird Robert W & Co Inc	11,878
Screaming Eagle Trading	18,178	Mischler Financial Equities	11,819
NKB	16,957	Ferris Baker Watts	11,539
Merriman Curhan Ford	16,789	Friedman Billings	11,270
Green Street Advisors	16,784	JMP Securities	10,269
SK International Securities	16,739	Kaupthing Bank Sverige Ab	10,059
Investment Bank of Greece	16,559	Skandinavian Bank Group	10,012
Jonestrading Instl Svcs	16,442	Other (181)	606,271
		Total Commissions	**$13,620,476**

SERS' assets are administered by the SERS Board. The Board has adopted an Investment Policy (Policy) that incorporates the provisions of the Retirement Code which govern the investment of SERS' assets. The Policy provides investment objectives and guidelines. The Investment Plan is reviewed and updated annually for strategic asset allocation purposes, as well as for diversification needs within each asset class.

Market Exposure as of December 31, 2007: SERS' assets had an unaudited market exposure of approximately $35,542.2 million.

SERS Asset Allocation

Assets	Market Exposure (Unaudited) $ (Millions)	Market Exposure (Unaudited) %	Long–Term Target Allocation
Global Stocks	$1,733.4	4.9%	5.0
U.S. Stocks	7,129.1	20.0	21.0
Non–U.S. Stocks	7,203.3	20.3	21.0
Absolute Return	3,340.5	9.4	9.0
Fixed Income	4,913.7	13.8	15.0
Real Estate	3,054.4	8.6	8.0
Alternative Investments	5,543.3	15.6	14.0
Inflation Protection	2,624.4	7.4	7.0
Cash	0.0	0.0	0.0
Total	**$35,542.2**	**100.0%**	**100.0**

Numbers may not add due to rounding.

Number of Investment Advisors: SERS had 190 external investment advisory firms managing portfolios. There are 47 advisors in the public markets domain and 168 covered alternative investments and real estate. Sixteen of these advisors manage 41 portfolios across asset classes.

- 3 Global Stock advisors
- 11 U.S. Stock advisors
- 12 Non-U.S. Stock advisors
- 2 Absolute Return advisors
- 1 Currency Overlay advisor
- 13 Fixed Income advisors
- 2 Cash advisors
- 3 Inflation Protection advisors
- 27 Real Estate advisors
- 54 Venture Capital general partners managing limited partnerships
- 87 Private Equity general partners managing limited partnerships

In addition, Board appointments included one real estate advisor.

Number of Investment Portfolios: SERS had 439 investment portfolios / accounts. Fifty–five of these accounts are public market investments, while 384 covered private markets.

- 3 Global Stock portfolios
- 2 Cash portfolios
- 12 U.S. Stock portfolios
- 3 Inflation Protection portfolios
- 16 Non-U.S. Stock portfolios
- 62 Real Estate portfolios
- 2 Absolute Return portfolios
- 114 Venture Capital limited partnership interests
- 1 Currency Overlay portfolio
- 208 Private Equity limited partnership interests
- 16 Fixed Income portfolios

In addition, Board appointments included two real estate portfolios, one international equity portfolio, and three private equity limited partnerships.

Global stocks is one of eight major asset classes which SERS uses to diversify the investments of the Fund. SERS' investment plan diversifies stock investments while maintaining a reasonable risk posture relative to the benchmarks. SERS contracts with external investment advisors to manage the portfolios.

Investment Objective: Stock investments are employed by the Fund primarily because their expected return premiums versus inflation will, if realized, help preserve and enhance the real value of the Fund over long periods of time. The global stocks accounts are managed on a total return basis.

SERS' long term investment objective for the global stock component of the stock asset class is to achieve a total return, net of fees, that exceeds the total return of the MSCI World Index.

SERS' 2008 Investment Plan targets an allocation of 5% of Fund assets to global stocks.

Market Exposure as of December 31, 2007: Global stocks had a $1,733.4 million market exposure, 4.9% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracts with 3 external investment advisors to manage global stock portfolios.

Number of Investment Portfolios: SERS had 3 global stock portfolios managed by the 3 investment advisors.

Type of Investment Portfolios: As of December 31, 2007, SERS global stock allocation was to all capitalization strategies.

SERS Global Stock Investments

	Global Stock Investment Advisor	Investment Style	Market Exposure* as of 12/31/07 ($ Millions)
1.	Walter Scott & Partners Limited	Growth	$718.4
2.	Marathon–London Global Fund	Contrarian sector relative value	1,059.2
3.	NISA Investment Advisors, LLC	Rebalancing and equitization	(44.2)
	Total Global Stocks		**$1,733.4**

**Includes stocks and cash which the manager had available for investment. Numbers may not add due to rounding.*

U.S. Stocks is one of eight major asset classes which SERS uses to diversify the investments of the Fund. SERS' investment plan diversifies stock investments while maintaining a reasonable risk posture relative to the benchmark. SERS contracts with external investment advisors to manage portfolios.

Investment Objective: Stock investments are employed by the Fund primarily because their expected return premiums versus inflation will, if realized, help preserve and enhance the real value of the Fund over long periods of time. The U.S. stock asset class is managed on a total return basis.

SERS' long term investment objective in the U.S. Stock asset class is to achieve a total return, net of fees, that exceeds the total return of the Russell 3000 Index.

Stock investments shall include, but not be limited to, publicly traded securities which provide SERS with an equity interest, (e.g, common stock, preferred stock, convertible preferred stock, and convertible bonds); as well as derivative instruments that provide stock like returns.

SERS' 2007 Investment Plan targets a long–term allocation of 21.0% of assets to U.S. Stocks. The U.S. stocks structure reflects the broad U.S. market in terms of capitalization (large and mid / small). SERS' U.S. stock portfolio, in aggregate, will strive to reflect the risk characteristics of the Russell 3000 Index, which is a good proxy for the broad, investable U.S. stock market.

The large cap segment of the portfolio is benchmarked to the S&P 500 Index utilizing enhanced indexed and a transportable alpha strategy utilizing funds–of–hedge funds. The remainder of the portfolio represents the mid / small capitalization segment of the U.S. stock market. Exposure to the mid / small capitalization segment of the market is achieved with traditional active strategies benchmarked to the Russell Midcap Index, the Russell 2500 Index, and the Russell Microcap Growth Index as well as synthetic index replication through the use of futures and swaps.

Market Exposure as of December 31, 2007: U.S. Stocks had a $7,129.1 million market exposure, 20.0% of the total fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracts with 11 external investment advisors to manage 12 U.S. Stock portfolios.

Number of Investment Portfolios: SERS had 12 U.S. Stock portfolios managed by the 11 investment advisors.

Type of Investment Portfolios: As of December 31, 2007, 81.2% of SERS U.S. Stock allocation was in large capitalization stock strategies, and 18.8% was in mid / small capitalization stock strategies. SERS has one equitization manager to replicate equity indices for the equitization portion of the portable alpha and rebalancing strategies.

SERS U. S. Stock Investments

	U.S. Stock Investment Advisor	Investment Style	*Market Exposure As of 12/31/07 ($ Millions)
Large cap			
S&P 500 Index swaps and portable alpha strategies			
1.	NISA Investment Advisors, LLC	Rebalancing and equitization	$831.3
2.	Blackstone Alternative Asset Management LP	Fund–of–Hedge Funds	2,153.0
3.	Pacific Alternative Asset Management Company, LLC	Fund–of–Hedge Funds	2,221.0
4.	Robeco Sage Capital	Fund–of–Hedge Funds	24.9
Traditional large cap			
5.	Barclays Global Investors Alpha Tilts Fund	Enhanced S&P 500 Index	556.7
Mid/small cap			
Traditional mid/small cap			
6.	Iridian Asset Management LLC	Midcap private business value	183.6
7.	AXA Rosenberg Investment Management LLC	Risk–controlled Russell 2500	165.7
8.	Emerald Advisers, Inc.	Pennsylvania companies	315.7
9.	Mellon Capital Management Corporation	Pennsylvania companies	245.6
10.	NorthPointe Capital, LLC	Microcap growth	33.4
11.	Turner Investment Partners, LLC	Quantitative microcap growth	34.3
	NISA Investment Advisors, LLC	Rebalancing and equitization	363.9
	Total U.S. Stocks		**$7,129.1**

**Includes stocks and cash which the manager had available for investment. Numbers may not add due to rounding.*

Non–U.S. stocks is one of eight major asset classes that SERS uses to diversify the investments of the Fund. SERS' investment plan diversifies stock investments while maintaining a reasonable risk posture relative to the benchmarks. SERS contracts with external investment advisors to manage portfolios.

Investment Objective: Stock investments are employed by the Fund primarily because their expected return premiums versus inflation will, if realized, help preserve and enhance the real value of the Fund over long periods of time. The Non–U.S. Stock asset class is managed on a total return basis.

SERS' long term investment objective for the non–U.S. stock asset class is to achieve a total return, net of fees, that exceeds the total return of the MSCI EAFE Index, a proxy for large cap stocks in non–U.S. developed markets; the S&P / Citigroup Extended Market Index Europe and Pacific, a proxy for mid / small cap stocks in non–U.S. developed markets; and the MSCI Emerging Markets Index, a proxy for stocks in emerging markets.

SERS' 2008 Investment Plan targets a long–term allocation of 21.0% of assets to Non–U.S. Stocks comprised of 17.0% to developed markets and 4.0% to emerging markets.

Market Exposure as of December 31, 2007: Non–U.S. Stocks had a $7,203.3 million market exposure, or 20.3% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracts with 12 external investment advisors to manage 16 non–U.S. stock portfolios.

Number of Investment Portfolios: SERS had 16 accounts managed by the 12 investment advisors

Type of Investment Portfolios: As of December 31, 2007, assets were diversified among direct accounts, synthetic equitization, and a transportable alpha strategy utilizing funds–of–hedge funds. Exposure, representing 16.4% of total Fund assets was allocated to stocks in non–U.S. developed markets, while 3.9% of total Fund assets was allocated to strategies dedicated to stocks in emerging markets.

SERS Non-U.S. Stock Investments

	Non–U.S. Stock Investment Advisor	Investment Style	Market Exposure* as of 12/31/07 ($ Millions)
Large Cap			
MSCI EAFE Index Exposure			
1.	NISA Investment Advisors, LLC	Rebalancing and equitization	$(186.5)
2.	Arden	Fund–of–Hedge Funds	888.1
3.	Rock Creek	Fund–of–Hedge Funds	892.8
Traditional Large Cap			
4.	Artisan Partners Limited Partnership	Global ex U.S. growth	855.8
5.	Templeton Investment Counsel, LLC	Global ex U.S. 5–year stock value	1,058.6
6.	Morgan Stanley Investment Management Limited	Developed ex U.S. cash flow value	973.5
Mid/Small Cap			
7.	BlackRock Investment Management International Limited	Growth	473.0
8.	Pictet Asset Management Limited	Value with growth	431.0
9.	Harris Associates LP	Intrinsic value	437.6
Emerging Markets			
10.	Rexiter Capital Management Limited	Core	225.7
11.	Bernstein Investment Research and Management	Value	222.4
	Pictet Asset Management Limited Emerging Markets Equity Team	Value	317.6
	Templeton Asset Management Ltd. TIFI Emerging Markets Series	Value	309.6
	Templeton Asset Management Ltd. Templeton Strategic Emerging Markets Fund II, LP	Private placements with public companies	217.0
12.	Oaktree Capital Management	Long/short Hedge Fund	153.1
	NISA Investment Advisors, LLC	Rebalancing and equitization	(66.0)
	Total Non–U.S. Stocks		**$7,203.3**

**Includes stocks and cash which the manager had available for investment. Numbers may not add due to rounding.*

SERS uses Absolute Return Strategies as part of its program to diversify the investments of the Fund. This mandate is expected to enhance the fund's overall risk-adjusted profile, thereby increasing the fund's long-term efficiency, as measured by the fund's expected return per unit of risk. SERS contracts with external funds-of-hedge funds investment advisors to manage these portfolios.

Investment Objective: Absolute Return Strategies are intended to produce low volatility uncorrelated diversified return streams in the portfolio to help preserve and enhance the real value of the Fund over long periods of time. Stand-Alone Absolute Return Strategies are managed on a total return basis.

SERS' long term investment objective for the Stand-Alone Absolute Return Strategies is to achieve a total return, net of fees, that exceeds Libor plus 300 basis points.

SERS' 2008 Investment Plan targets an allocation of 9.0% of Fund assets to Stand-Alone Absolute Return Strategies.

Market Exposure as of December 31, 2007: Stand-Alone Absolute Return Strategies had a $3,340.5 million market exposure, approximately 9.4% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracted with two external investment advisors to manage the Stand-Alone Absolute Return Strategies.

Number of Investment Portfolios: SERS had two Stand-Alone Absolute Return Strategies portfolios managed by the two fund-of-hedge-funds investment advisors.

Type of Investment Portfolios: As of December 31, 2007, SERS' Absolute Return Strategies were globally diversified across all major asset classes and includes six major strategies and 20 sub-strategies.

SERS Absolute Return Strategies Investments

	Investment Advisor	Strategy	Market Exposure* as of 12/31/07 ($ Millions)
1.	Mesirow	Fund–of–Hedge Funds	$1,809.4
2.	Morgan Stanley	Fund–of–Hedge Funds	1,531.1
	Total Absolute Return Strategies		**$3,340.5**

**Includes stocks and cash which the manager had available for investment. Numbers may not add due to rounding.*

Fixed Income is one of eight major asset classes that SERS uses to diversify the investments of the Fund. The SERS' Investment Plan diversifies Fixed Income investments and strategies. SERS contracts with external investment advisors to manage portfolios.

Investment Objective: The Fixed Income asset class is employed by the Fund because of its ability to generate current income from interest payments, increase the value of the Fund through the reinvestment of those interest payments, serve as a hedge against disinflation and / or deflation, and to help diversify the overall Fund. The Fixed Income asset class is managed on a total return basis.

In the Fixed Income asset class, SERS' long–term investment objective is to achieve a total return, net of fees, that exceeds the total return of the SERS Custom Fixed Income Index which is comprised of the Lehman Intermediate, Lehman Aggregate, the Citigroup High Yield Market and J.P. Morgan Emerging Market Bond indices.

SERS' 2008 Investment Plan targeted a long–term allocation of 15.0% of assets of the total Fund to the Fixed Income asset class. Of this amount, 39% is targeted to the core strategies and 61% to specialty strategies (High–yield and emerging market debt).

Market Exposure as of December 31, 2007: Fixed Income had a $4,913.7 million market exposure, 13.8% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracts with 13 external investment advisors to manage 16 portfolios within the Fixed Income asset class as of December 31, 2007.

Number of Investment Portfolios: SERS had a total of 16 portfolios within the Fixed Income asset class.

Type of Investment Portfolios: The Fixed Income asset class is divided into core and specialty segments.

Core: Core portfolios invest in relatively liquid, high quality, fixed income securities with intermediate term durations that meet return, disinflation / deflation, high quality liquidity and diversification needs of the Fund. SERS had three actively managed core bond portfolios: one Custom Intermediate Duration Treasury Inflation Protection (TIPS) portfolio, one Lehman Aggregate portfolio, and one Lehman Credit portfolio. The three actively managed core portfolios totaled $1,680.1 million. In addition, SERS had one passively managed Lehman Aggregate bond portfolio of $286.3 million. The combination of core portfolios represented 40.3% of the asset class.

Specialty: The specialty strategy portfolios (high–yield, emerging market debt, subordinated debt, and mezzanine debt) focus on debt instruments offering higher return premiums and different risk characteristics than core fixed income securities. SERS has corporate high yield portfolios with a fair value of $1,186.5 million, emerging market debt portfolios with a fair value of $1,448.0 million, and one high yield commercial mortgage–backed securities portfolio with a fair value of $297.5 million. The specialty portfolios represent 59.7% of the asset class.

SERS Fixed Income Investments

	Fixed Income Investment Advisor	Investment Style	Market Exposure* As of 12/31/07 ($ Millions)
Core			
1.	Standish (Mellon)	Domestic – index	$286.3
2.	Morgan Stanley	Active domestic	924.6
3.	Taplin, Canida & Habacht	Active domestic	108.9
4.	NISA Investment Advisors	Active intermediate duration TIPS	646.8
	NISA Investment Advisors, LLC	Rebalancing and equitization	15.0
Specialty			
5.	Berwind (Eureka) Financial Group	PA Capital Fund	5.0
6.	Pyramis Global Advisors	Commercial mortgage backed securities	297.5
7.	Oaktree Capital Management	Mezzanine Fund	1.3
8.	Stone Harbor (Salomon)	Global high yield	689.4
	Stone Harbor (Salomon)	Emerging market debt	432.8
9.	W. R. Huff Asset Management	High yield bonds	490.9
10.	Ashmore AEMDF	Emerging market debt ($U.S.)	257.5
	Ashmore LCD	Emerging market debt – local	173.9
11.	Gramercy Advisors	Emerging market debt –absolute return	134.3
12.	Greylock Capital Management	Emerging market debt –absolute return	120.1
13.	PIMCO	Emerging market debt	329.4
	Total Fixed Income Investments		**$4,913.7**

**Includes securities and cash that the manager had available for investment. Numbers may not add due to rounding.*

Cash is one of eight major asset classes that SERS uses for investments of the Fund. The SERS' Investment Plan calls for minimizing cash balances while meeting cash flow requirements. In 2007 the Fund adopted a rebalancing strategy that would enhance the Fund's liquidity profile by providing a ready pool of cash that would be equitized with synthetic investments, including futures and swaps, to provide measured equity and fixed income exposure. So, while the cash balances have increased, it has not resulted in an effective increase of the Fund's allocation to cash. The Fund was able to preserve its historical asset allocation of 0% to cash; while earning market returns as though those funds were invested in equity or fixed income markets. The rebalancing strategy does not use leverage.

Investment Objective: Cash investments are employed by the Fund to provide for SERS' liquidity needs and to accumulate funds for future investment. The Cash asset class is to be managed on a total return basis, with the exception that temporary investments such as overnight repurchase agreements, commercial paper, and banker's acceptance may alternatively be evaluated on a yield–to–maturity basis given their extremely short maturities.

Cash balances are evaluated on a monthly basis to determine that appropriate equity and fixed income market exposures are being maintained, and adjusted if necessary using swaps and futures to obtained the desired market exposure.

In the Cash asset class, SERS' long term investment objectives are to achieve a total return, net of fees, that exceeds the total return on 90 day U.S. Treasury Bills. SERS' current Investment Plan targets an allocation of 0% of dedicated assets to the Cash asset class, while maintaining between $300-$900 million in short term investments equitized with equity and fixed income derivatives. The cash liquidity is used to support the Fund's benefit payments, swap payments for its portable alpha program and operational expenses of the Fund. The cash return offsets the cost of the derivatives used to rebalance the program.

Market Exposure as of December 31, 2007: The effective cash exposure at December 31, 2007 was zero. Cash investment underlying the rebalancing and equitization strategies had a $709.4 million fair value, 2.0% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: The cash and rebalancing strategies use two advisors. The Pennsylvania State Treasury Department manages the uninvested cash in the liquidity accounts; and NISA Investment Advisors manages the cash and synthetic overlays for the rebalancing account. The $709.4 million of cash holdings have been allocated to the respective asset classes in this report based upon the synthetic exposures in place on December 31, 2007.

Number of Investment Portfolios: SERS' cash portfolio is managed primarily by the Treasurer. Certain short term cash investments and the synthetic overlays for the fixed income and equity markets are managed by NISA Investment Advisors.

Type of Investment Portfolios: SERS Cash asset class currently employs a money market short–term investment strategy. The portfolio also contains the uninvested cash balances held by other SERS investment advisors in other asset classes. Cash held in the rebalancing account are invested in high-quality, highly liquid, short-term investments including the Treasurer's STIF pool.

In the aggregate, the State Treasury managed approximately $1,055.8 million on behalf of SERS and SERS' external investment advisors as of December 31, 2007.

Real Estate is one of eight major asset classes that SERS uses to diversify the investments of the Fund. SERS' investment plan diversifies Real Estate investments and balances real estate management styles. In accordance with the plan, SERS contracts with external investment advisors to manage portfolios.

Investment Objective: Real Estate investments are generally long–term, illiquid investments that, due to their high correlation with inflation, provide an inflation hedge and, due to their low correlation with stocks and bonds, provide diversification within the total portfolio. It is expected that the long–term total return (income and appreciation) for real estate will fall between that of stocks and bonds. The Real Estate asset class is managed on a total return basis.

In the Real Estate asset class, SERS' long–term investment objective is to achieve a total net return that exceeds the total return of the NCREIF Index for rolling five year periods. SERS' 2008 Investment Plan targets a long–term allocation of 8% of assets to the Real Estate asset class.

Investments are made through commingled fund investments, limited partnerships, REITs and separate account portfolios where SERS contracts with external investment advisors to own properties directly or with other co–investors. SERS' Real Estate portfolio provides for diversification by:

- Transaction structure;
- Property type;
- Geographic location; and
- Development phase.

Fair Value as of December 31, 2007: Real Estate had an estimated $3,054.4 million fair value, approximately 8.6% of the total Fund's December 31, 2007 fair value. This fair value represents September 30, 2007 actual numbers adjusted for cash flows, which occurred in the fourth quarter 2007. Real estate fair values and detailed property data is lagged by one quarter due to the timing of the receipt of the private market valuations and information.

Number of Investment Advisors: SERS had contracts with 27 external investment advisors to manage real estate portfolios as of September 30, 2007.

Number of Investment Portfolios: SERS had investments in 62 real estate portfolios managed by the 27 investment advisors.

Type of Investment Portfolios: As of September 30, 2007, the composition of the real estate portfolio was:

- 30% pooled funds, 70% separate accounts
- 25% office, 6% industrial, 8% retail, 22% residential, 12% hotel / motel, 8% timber, 19% other (including senior and student housing, land and various niche property investments)
- 12% Pennsylvania, 26% East excluding PA, 28% West, 14% South, 5% Midwest, 15% International
- 28% of the market value of the separate accounts was invested in seventeen investments located in Pennsylvania

SERS Real Estate Investments

	Real Estate Investment Advisor	SERS Initial Funding	Property Type	Transaction Structure	*Fair Value as of 9/30/07 ($ Millions)
1.	AG Asia Realty Fund	04/26/07	Int'l Opportunistic	Equity and debt	$2.1
2.	Apollo – AREF III	06/26/98	Opportunistic	Equity and debt	28.1
3.	Berwind – BPG Fund IV	04/20/98	Opportunistic	Equity and debt	4.0
	BPG Fund V	11/29/99	Opportunistic	Equity and debt	16.1
	BPG Fund VI	09/09/02	Opportunistic	Equity and debt	17.3
	BPG Fund VII	09/12/05	Opportunistic	Equity and debt	23.6
	BPG Fund VIII	07/16/07	Opportunistic	Equity and debt	3.2
4.	Blackstone – BREP III	10/22/99	Opportunistic	Equity and debt	3.0
	BREP IV	12/08/03	Opportunistic	Equity and debt	24.5
	BREP V	01/24/06	Opportunistic	Equity and debt	53.3
	BREP VI	03/28/07	Opportunistic	Equity and debt	15.6
5.	Cliffwood Select Equity Fund	08/04/00	Long/Short REITs	Public securities	45.0
6.	Colony Investors Fund VIII	09/18/07	Opportunistic	Equity and debt	2.6
7.	ING Real Estate Securities	01/31/96	REITs	Public securities	495.8
8.	Fidelity Opp. Income Fund	04/02/07	Debt	Debt	22.0
9.	Fillmore East Capital Partners	06/29/06	Debt	Debt	19.4
10.	Forest Investment Assoc.	10/30/92	Timber	Equity ownership	220.0
11.	Grosvenor Investment Mgmt.	10/01/93	PA diversified	Equity ownership	373.0
	Eastern Retail Holdings	01/07/99	Retail	Equity and debt	0.2
	Grosvenor Residential Ptrs I	04/26/07	Residential	Equity and debt	0.8
12.	Hawkeye Partners – Scout Fund	**	Opportunistic	Equity and debt	0
13.	Heitman Capital Mgmt	12/28/87	Diversified	Equity ownership	70.0
	Heitman America RE Trust	03/29/07	Diversified	Equity ownership	37.1
14.	LaSalle Investment Mgmt.	10/01/93	Diversified	Equity ownership	328.1
15.	Lowe Enterprises	10/01/93	Diversified	Equity ownership	494.0
16.	Lubert–Adler Fund II	10/30/98	Opportunistic	Equity and debt	8.7
	Lubert–Adler Fund III	11/10/00	Opportunistic	Equity and debt	12.6
	Lubert–Adler Fund IV	03/31/04	Opportunistic	Equity and debt	22.1
	Lubert–Adler Fund V	04/10/06	Opportunistic	Equity and debt	15.8
17.	Miller Global Fund III	01/19/99	Diversified	Equity and debt	1.0
18.	Oaktree Capital Management:				
	TCW Fund VI	04/20/94	Opportunistic	Equity and debt	0.6
	OCM Opportunity Fund A	05/09/96	Opportunistic	Equity and debt	3.1
	OCM Opportunity Fund II	12/15/98	Opportunistic	Equity and debt	5.2
	OCM Opportunity Fund III	03/05/03	Opportunistic	Equity and debt	23.4
19.	Oxford GSA Fund	11/06/06	Development	Equity and debt	3.3

SERS Real Estate Investments (continued)

	Real Estate Investment Advisor	SERS Initial Funding	Property Type	Transaction Structure	*Fair Value as of 9/30/07 ($ Millions)
20.	Prudential – Senior Housing I	12/22/98	Senior housing	Equity and debt	$0.4
	Senior Housing II	06/12/01	Senior housing	Equity and debt	16.7
	Senior Housing III	01/12/06	Senior housing	Equity and debt	22.6
	Mexico Retail Fund	09/19/06	Int'l Opportunistic	Equity and debt	7.4
21.	Rockpoint Group – Fund I	09/28/04	Opportunistic	Equity and debt	10.3
	Rockpoint Fund II	09/27/05	Opportunistic	Equity and debt	28.5
	Rockpoint Fund III	12/21/07	Opportunistic	Equity and debt	0
	Rockpoint Finance Fund	03/13/07	Opportunistic	Debt	1.0
22.	Sentinel Corp.	07/31/84	Diversified	Equity ownership	81.8
23.	Starwood: SOF IV	03/24/97	Opportunistic	Equity and debt	3.3
	SOF V	05/14/99	Opportunistic	Equity and debt	2.8
	SOF VI	03/27/03	Opportunistic	Equity and debt	52.7
	SOF VII	01/13/06	Opportunistic	Equity and debt	26.1
24.	UBS: PMSA	09/30/83	Diversified	Equity mortgages	77.0
	RESA	06/3/ /84	Diversified	Equity ownership	93.0
	Multifamily Trust	08/02/99	Residential	Equity ownership	0.4
25.	Urdang Investment Mgmt.	05/15/02	REITs	Public securities	69.6
26.	Westbrook Partners: WREF II	06/16/97	Opportunistic	Equity and debt	4.7
	WREF III	09/01/98	Opportunistic	Equity and debt	4.1
	WREF IV	05/01/01	Opportunistic	Equity and debt	5.6
	WREF V	02/16/05	Opportunistic	Equity and debt	6.4
	WREF VI	05/10/06	Opportunistic	Equity and debt	31.3
	WREF VII	12/03/07	Opportunistic	Equity and debt	0
27.	Goldman Sachs: Whitehall V&VI	04/20/94	Opportunistic	Equity and debt	5.0
	Whitehall V–S & VI–S	12/11/95	Opportunistic	Equity and debt	0.2
	Whitehall VII & VIII	05/28/96	Opportunistic	Equity and debt	1.0
	September 30, 2007 Total Real Estate Investments				**$2,946.5**
	4th Quarter Net Cash Flow Adjustments				107.9
	December 31, 2007 Total Real Estate Investments				**$3,054.4**

**Fair values are lagged by one quarter due to the timing of the receipt of private market valuations and information.*
*** Not funded as of 9/30/07*
Numbers may not add due to rounding.

Alternative Investments is comprised of Venture Capital and Private Equity investments, both of which take the form of limited partnerships, and is one of eight major asset classes that SERS uses to diversify the investments of the fund.

Venture Capital and Private Equity Defined

Venture Capital is the financing of young, rapidly growing companies, typically at three stages of development. (1) Seed and Early Stage: Seed is the form of venture capital that supports companies in their conceptual phase, i.e., a product and market are identified, and a corporation may have been formed. Early Stage financing supports companies pursuing a business plan but not yet generating meaningful revenues. The product has been developed and may have been shipped to customers for testing. Management positions have been filled and an operating team is in place. (2) Late Stage financing supports companies that have proven revenues, and are in the process of rolling out operations and building sales to achieve profitability. (3) Growth or Expansion financing supports profitable or nearly profitable businesses that, lacking access to significant debt financing, need capital for growth and expansion. Companies at either the later stage or growth or expansion stage may be nearing a strategic sale to another company or an initial public offering.

Private Equity primarily refers to investments in the equity and subordinated debt of established companies. Private equity approaches undertaken by SERS' limited partnerships include: (1) Leveraged buyouts and management buyouts in which companies are acquired through the use of borrowed funds, or a combination of borrowed funds and contributed equity capital. The acquired company's assets serve as collateral for the borrowed funds, which are repaid from the company's cash flows. (2) Distressed debt investing involves: (a) deleveraging of debt–laden, but successful, companies by infusing capital to permit debt reduction in exchange for an equity stake in the company, or (b) acquiring debt of a troubled, sometimes bankrupt company, at steep discounts to face value, followed by assistance to return the company to profitability to permit selling of the debt securities at levels above the discounted purchase price. (3) Secondary interests in established private equity funds – these interests are purchased from other investors who seek liquidity or desire to realign or rebalance their investment portfolios, often for non–financial reasons. Such partnership interests can be purchased at significant discounts to net asset value and often occur when the acquired partnerships begin to realize profits.

Investment Objective: SERS' long term investment objective for Alternative Investments is to outperform the appropriate Cambridge Benchmark, while generating a risk-adjusted total return, net of fees, in excess of the return generated by the S&P 500 Index. SERS' 2007-2008 Investment Plan anticipates a long-term allocation range with a midpoint of 14%.

Fair Value as of December 31, 2007: The asset class total fair value stood at $5,543.3 million after adjusting the September valuation for subsequent cash flows in the 4th quarter. Alternative Investment fair values lag one quarter due to timing of the receipt of private market valuations, reports and other information. These values do not include 4th quarter unrealized appreciation / depreciation. Alternative Investments represent 15.6% of the Fund. Sub–asset class fair values and fund percentages were as follows:

SERS Alternative Investments

	Unfunded Commitments ($ Millions)	Fair Value ($ Millions)	Percent of Total Fund
Venture Capital	$969.1	1,379.3	3.9%
Private Equity	3,160.5	4,164.0	11.7
Total Alternative Investments	**$4,129.6**	**5,543.3**	**15.6%**

Number of Limited Partnerships: As of December 31, 2007, SERS had commitments to 322 active Alternative Investments limited partnerships, 114 to Venture Capital partnerships and 208 to Private Equity partnerships. (This does not include 29 partnerships – 18 Venture Capital and eight Private Equity – that are now "inactive" and three investments pending contract approval.)

Portfolio: SERS' Alternative Investment Program's scope has expanded over the years to include top investment funds nationally and internationally. The Program holds indirect investment interests in over 4,500 companies. The Venture Capital Program includes investments working to commercialize novel solutions to current and future challenges in information technology, communications, and medicine. In addition to direct fund investments, the Venture Capital Program includes investments in several fund–of–funds. A fund–of–funds is a limited partnership that, in turn, invests in other limited partnerships. Five of these fund–of–funds commitments have the strategic goal of enabling SERS to gain indirect exposure to many top–tier venture capital funds that SERS would otherwise have difficulty accessing directly. Another two of these commitments are to funds investing in minority–focused venture capital funds.

The Private Equity Program invests in buyout, distressed, international, and secondary oriented partnerships. Buyout transactions are privately negotiated or result from investment bank sponsored auctions, and are usually completed with present management in place; hostile acquisitions are generally avoided. Distressed investment managers employ differentiated strategies, i.e., they employ control or non–control approaches, and accordingly, have differing degrees of active influence over the companies in which they invest. European funds are attempting to capitalize on trends favoring the restructuring of large companies, generational succession in businesses established after World War II, and cross–border business opportunities within the region since the formation of the European Economic Union and currency harmonization. Asian investments focus on the expanded opportunities in the region created by changing attitudes in many Asian countries regarding foreign investment, favorable demographic trends, globalization opportunities, and economic growth. The Program typically gains initial exposure to emerging markets and other target regions through the use of funds–of–funds. The portfolio's exposure to energy markets is also expanding. Additionally, SERS utilizes one manager to oversee stock distributions and another manager for co–investment opportunities.

Alternative Investment Portfolio Exposure: The Alternative Investment Program is well–diversified by stage of investment, industry focus, and geography. As of September 30, 2007, based on fair value, the program's exposure was as follows:

By Sub Sector:

U.S. Private Equity	44.6%
U.S. Venture Capital	22.0
International	17.1
Distressed / Opportunistic	8.3
Pennsylvania	4.6
Other	3.4

By Style:

LBO	42.9%
Expansion Stage	15.8
Early Stage	10.3
Start–Up	8.2
Acquisition / Platform	5.4
Senior Debt LBO	5.4
Other	12.0

By Geography:

U.S. Northeast	18.2%
U.S. West Coast	12.9
U.S. Southwest / Rockies	10.5
U.S. Midwest / Plains	8.5
U.S. Mid–Atlantic	7.7
U.S. Southeast	7.6
U.S. Pacific Northwest	1.7
United Kingdom	7.5
Germany	3.4
France	2.7
Netherlands	2.3
Denmark	2.0
Rest of World	15.0

By Industry:

Communications	23.5%
Consumer	21.8
Healthcare	15.9
Financial	10.1
Manufacturing	7.2
Software	7.2
Electronics	4.0
Energy	3.2
Other	7.1

SERS Venture Capital Committed, Drawn and Distributed

The Capital Committed column represents total dollars allocated from SERS to each limited partnership. Capital Drawn is the portion of SERS capital commitments drawn by the General Partner to be invested with underlying portfolio companies. The Distributions column shows the value of original capital and profits returned to SERS.

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
1. APAX Excelsior VI	Later Stage	07/03/00	$35,000,000	33,211,781	23,791,256
P/A Fund I	Later Stage	06/30/93	30,000,000	29,999,999	66,195,539
P/A Fund III	Later Stage	03/31/97	100,000,000	100,000,000	151,420,448
2. APEX Investment Fund IV	Early Stage	09/17/99	25,000,000	25,000,000	257,566
APEX Investment Fund V	Early Stage	04/19/02	20,000,000	19,200,000	1,707,066
3. Adams Capital Management II	Early Stage	10/01/99	30,000,000	30,000,000	0
Adams Capital Management III	Early Stage	11/21/00	30,000,000	28,500,000	4,761,905
4. Advanced Technology Ventures VI	Early Stage	03/09/00	10,000,000	10,000,000	240,896
Advanced Technology Ventures VII	Early Stage	07/11/01	27,000,000	23,084,700	6,580,846
5. Alloy Annex I	Seed/Early Stage	10/31/03	5,000,000	4,000,000	0
Alloy Ventures 2000	Early Stage	05/19/00	20,000,000	20,000,000	2,074,620
Alloy Ventures 2002	Early Stage	07/22/02	25,000,000	18,250,000	5,604,706
Alloy Ventures 2005	Seed/Early Stage	08/11/05	25,000,000	10,500,000	0
6. Artiman Ventures II	Seed/Early Stage	10/27/06	25,000,000	3,250,000	0
7. Atlas Venture Fund IV	Early Stage	03/31/99	26,000,000	23,202,503	6,135,410
Atlas Venture Fund V	Early Stage	02/07/00	37,200,000	36,970,720	10,090,936
Atlas Venture Fund VI	Early Stage	08/01/01	24,800,000	23,405,324	3,122,782
8. Austin Ventures IX	Early Stage	01/09/06	15,000,000	4,857,143	881,830
Austin Ventures VIII	Early Stage	07/26/01	20,932,140	20,590,058	5,749,677
9. Battery Ventures VIII	Diversified	08/13/07	25,000,000	2,411,950	0
10. Birchmere Ventures III	Early Stage	05/05/05	10,000,000	5,324,524	0
11. Care Capital Investments III	Later Stage	02/08/06	25,000,000	3,000,000	0
12. Charles River Partnership XI	Early Stage	02/15/01	11,032,259	10,011,776	2,590,731
13. Clearstone Venture Partners III-A	Early/Late Stage	12/22/04	25,000,000	12,250,000	0
14. Cross Atlantic Technology Fund	Early Stage	02/14/00	20,000,000	19,949,041	7,591,801
Cross Atlantic Technology Fund II	Early Stage	01/28/02	32,900,000	32,242,000	6,955,131
Novo Vita	Early Stage	12/26/00	11,616,498	11,616,498	1,613,690
15. Devon Park Bioventures	Early/Late Stage	12/15/06	10,842,697	503,565	26
16. Draper Fisher Jurvetson Fund VII	Early Stage	09/22/00	20,000,000	16,910,000	3,178,088
Draper Fisher Jurvetson VI	Early Stage	08/13/99	8,000,000	7,760,000	94,810
17. Draper Triangle Ventures	Early Stage	12/20/99	20,000,000	21,453,575	2,195,783
Draper Triangle Ventures II	Early Stage	10/13/04	12,000,000	4,646,840	71,158
18. Edison Venture Fund III	Later Stage	03/31/94	25,000,000	25,000,000	45,769,784
19. Fairview Capital	Fund of Funds	09/30/94	10,000,000	10,000,000	4,434,328
Fairview II	Fund of Funds	03/31/98	10,000,000	9,600,000	2,602,239
20. Frazier Healthcare III	Early Stage	03/31/99	30,000,000	29,475,000	9,927,334
Frazier Healthcare IV	Early Stage	09/27/01	30,000,000	25,722,010	8,265,506
Frazier Healthcare V	Early/Late Stage	05/10/05	30,000,000	11,220,000	2,742,043
21. Grotech PA III	Later Stage	06/29/90	3,000,000	3,014,865	2,910,452
Grotech Partners V	Later Stage	09/30/98	25,000,000	25,000,000	23,671,934
22. Halpern Denny Fund II	Later Stage	03/31/98	25,000,000	25,116,871	4,513,556
Halpern Denny Fund III	Later Stage	04/26/00	25,000,000	23,631,740	16,626,928

SERS Venture Capital Committed, Drawn and Distributed (continued)

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
23. HarbourVest Partners VI	Fund of Funds	05/07/99	$200,000,000	176,586,055	61,504,217
HarbourVest Partners VII	Fund of Funds	03/24/03	75,000,000	44,250,000	1,113,750
HarbourVest Partners VIII	Fund of Funds	10/05/06	100,000,000	7,000,000	0
24. Healthcare Ventures III	Early Stage	09/30/92	15,000,000	15,000,000	30,778,200
Healthcare Ventures V	Early Stage	12/31/97	25,000,000	25,000,000	51,990,128
Healthcare Ventures VI	Early Stage	06/19/00	35,000,000	34,125,000	3,462,611
Healthcare Ventures VII	Early Stage	10/29/02	35,000,000	26,250,000	0
Healthcare Ventures VIII	Early Stage	08/22/05	30,000,000	6,450,000	2,568,786
25. Highland Capital Partners VI	Early Stage	10/25/01	25,000,000	22,687,500	14,164,592
Highland Capital Partners VII	Early Stage	10/13/06	35,000,000	7,262,500	0
Highland Consumer Fund I	Diversified	05/04/07	25,000,000	3,263,199	0
26. IP II	Early Stage	12/17/01	8,600,000	8,240,074	1,006,296
IP III	Seed/Early Stage	11/19/04	10,500,000	6,930,000	0
IP IV	Seed/Early Stage	09/21/07	14,000,000	840,000	0
27. InterWest Partners IX	Early Stage	10/19/05	20,000,000	7,000,000	1,106,563
InterWest Partners VIII	Early Stage	08/25/00	25,000,000	21,250,000	5,323,829
28. J.H. Whitney Equity Fund III	Later Stage	03/31/98	20,000,000	20,171,316	39,740,353
J.H. Whitney IV	Later Stage	02/01/00	20,000,000	16,712,208	4,169,263
29. JP Morgan Venture Capital Investors	Fund of Funds	07/08/99	100,000,000	97,559,706	22,861,587
JP Morgan Venture Capital Investors II	Fund of Funds	09/08/00	100,000,000	73,526,757	14,388,050
JP Morgan Venture Capital Investors III	Fund of Funds	06/20/06	100,000,000	12,855,936	3,580
30. JMI Equity Fund V	Early/Late Stage	06/07/05	24,000,000	18,269,205	0
JMI Equity Fund VI	Early/Late Stage	06/27/07	40,000,000	3,600,000	0
31. Keystone V	Later Stage	03/31/98	25,000,000	25,117,132	2,082,064
Keystone Venture IV	Later Stage	07/21/93	15,000,000	15,045,275	11,249,174
32. Kline Hawkes Pacific	Early Stage	08/30/00	15,000,000	14,839,616	4,828,419
33. Knightsbridge Venture Capital VI	Fund of Funds	12/07/04	20,000,000	6,150,000	0
34. Lightspeed Venture Partners VII	Early Stage	02/27/06	18,000,000	7,364,913	0
35. Meritech Capital Partners II	Later Stage	01/02/01	26,475,166	20,593,454	12,358,859
Meritech Capital Partners III	Later Stage	04/05/06	35,000,000	12,425,000	0
36. Morgenthaler Partners VII	Early Stage	07/26/01	35,000,000	29,750,000	11,147,420
Morgenthaler Partners VIII	Diversified	10/03/05	35,000,000	10,500,000	866,827
37. Mid-Atlantic III	Early Stage	06/30/97	20,008,308	20,111,247	5,025,301
Mid-Atlantic Venture Fund IV	Early Stage	05/04/00	30,000,000	27,900,000	217,297
NEPA Venture-II	Early Stage	12/31/92	7,500,000	7,526,234	34,879,769
38. New Enterprise Associates VI	Early Stage	03/31/94	25,000,000	25,000,000	198,142,418
New Enterprises Associates VII	Early Stage	12/31/96	30,000,000	30,000,000	97,217,571
New Enterprise Associates IX	Early Stage	11/15/99	20,000,000	19,600,000	3,096,428
New Enterprise Associates X	Early Stage	12/11/00	35,000,000	32,928,000	14,057,500
New Enterprise Associates 11	Early Stage	03/01/04	25,000,000	20,250,000	5,273,208
New Enterprise Associates 12	Diversified	06/26/06	35,000,000	9,279,833	280,998
39. NewSpring Ventures II	Later Stage	04/20/07	10,000,000	1,000,000	0
40. Oak Investment Partners XI	Later Stage	07/21/04	35,000,000	30,460,294	5,500,388
Oak Investment Partners XII	Early/Late Stage	07/10/06	40,000,000	10,934,910	0
41. PA Early Stage Partners III	Early Stage	04/17/03	10,000,000	5,150,000	404,667

SERS Venture Capital Committed, Drawn and Distributed (continued)

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
42. Polaris Venture Partners	Early Stage	06/30/96	$15,000,000	14,595,000	46,501,899
Polaris Venture Partners II	Early Stage	09/30/98	25,000,000	24,750,000	24,859,456
Polaris Venture Partners III	Early Stage	01/21/00	50,000,000	48,500,000	13,041,838
Polaris Venture Partners IV	Early Stage	09/30/02	50,000,000	42,750,000	3,312,172
Polaris Venture Partners V	Diversified	08/08/06	50,000,000	6,250,000	0
43. Quaker Bio Ventures	Early Stage	02/20/03	20,000,000	14,922,958	3,526,430
Quaker BioVentures II	Middle/Later Stage	04/03/07	25,000,000	250,000	0
44. Sofinnova Venture Partners VII	Early Stage	01/18/07	20,000,000	2,400,000	0
45. Sprout VII	Early Stage	03/31/95	18,000,000	18,000,000	40,500,717
46. Summit Accelerator Fund	Early Stage	11/15/99	8,000,000	7,560,000	6,747,995
Summit Partners V. C. Fund II	Diversified	09/22/06	15,000,000	2,100,000	0
Summit IV	Later Stage	09/30/95	25,000,000	24,250,000	182,561,331
Summit V	Later Stage	03/31/98	37,500,000	36,000,000	46,278,130
47. T.Rowe Price Stock Distribution Account	Stock Distribution	01/03/05	0	223,842,864	168,740,567
48. TA/Advent VIII	Later Stage	06/30/97	30,000,000	29,541,093	58,866,034
49. Three Arch Capital	Early Stage	12/20/00	20,000,000	17,500,000	3,145,142
Three Arch Partners IV	Early/Late Stage	06/04/04	20,000,000	8,050,000	465,004
50. TL Ventures III	Early Stage	03/31/97	15,000,000	15,062,614	18,874,357
TL Ventures IV	Early Stage	05/13/99	35,000,000	35,000,000	20,103,600
TL Ventures V	Early Stage	10/18/00	40,000,000	30,848,219	5,978,047
51. US Venture Partners VII	Early Stage	02/18/00	13,750,000	13,750,000	1,875,020
US Venture Partners VIII	Early Stage	06/01/01	26,250,000	23,865,000	5,722,728
52. Weathergage Venture Capital	Fund of Funds	06/26/07	25,000,000	937,500	0
53. Weston Presidio III	Later Stage	12/31/98	35,000,000	31,237,086	20,994,821
Weston Presidio IV	Later Stage	06/21/00	35,000,000	33,197,500	13,404,271
Weston Presidio V	Later Stage	12/08/05	50,000,000	24,850,000	0
54. Worldview Technology Partners IV	Early Stage	01/31/01	18,130,023	16,225,974	1,907,983
Total Active Venture Capital Commitments			**$3,326,037,091**	**2,582,873,655**	**1,782,588,460**

Cash flows as of 9/30/07

Inactive Venture Capital Funds

Limited Partnership	Capital Committed	Capital Drawn	Distributions
Total Inactive Venture Capital	**$199,700,000**	**189,657,125**	**395,994,167**

SERS Private Equity Investments Committed, Drawn and Distributed

The Capital Committed column represents total dollars allocated from SERS to each limited partnership. Capital Drawn is the portion of SERS capital commitments drawn by the General Partner to be invested with underlying portfolio companies. The Distributions column shows the value of original capital and profits returned to SERS.

	Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
1.	ABRY Broadcast Partners III	Buyouts	03/31/97	$25,000,000	27,172,386	22,020,945
	ABRY Broadcast Partners IV	Buyouts	03/30/01	35,000,000	27,906,686	29,228,929
	ABRY Partners V	Buyouts	07/29/05	45,000,000	29,533,448	435,031
	ABRY Mezzanine Partners	Mezzanine	03/15/02	30,000,000	32,294,981	29,026,236
	ABRY Senior Equity II	Secondaries	07/27/06	30,000,000	8,839,644	77,544
2.	ABS Capital Partners III	Buyouts	03/31/99	35,000,000	29,428,915	16,906,256
	ABS Capital Partners IV	Buyouts	10/13/00	35,000,000	31,035,121	30,917,069
	ABS Capital Partners V	Buyouts	11/14/05	20,000,000	10,836,118	48,924
3.	AG Capital Recovery Partners II	Distressed Debt	10/01/01	17,600,000	17,695,470	26,940,586
	AG Capital Recovery Partners III	Distressed Debt	04/01/02	20,000,000	16,000,000	25,124,698
	AG Capital Recovery Partners IV	Distressed Debt	02/04/03	50,000,000	35,415,216	52,457,171
	AG Capital Recovery Partners V	Distressed Debt	04/17/06	20,000,000	8,300,000	0
4.	APAX Europe IV	Buyouts	03/31/99	35,000,000	29,445,670	31,281,236
	APAX Europe V	Buyouts	04/27/01	70,000,000	67,680,079	114,167,411
	APAX Europe VI	Buyouts	05/19/05	76,349,190	61,590,370	24,103,804
	APAX Europe VII	Buyouts	06/27/07	132,900,000	25,435,450	0
	APAX Germany II	Middle/Later Stage	06/30/97	8,737,262	8,455,477	16,916,389
	APAX UK Ventures VI	Middle/Later Stage	12/31/97	6,558,000	6,918,899	12,587,930
5.	AXA Secondary Fund III	Secondaries	11/19/04	26,000,000	17,387,109	19,117,760
	AXA Secondary Fund III-2	Secondaries	11/24/04	14,000,000	9,343,346	9,818,583
	AXA Secondary Fund IV	Secondaries	02/26/07	80,000,000	7,244,688	432,702
6.	Abingworth Bioventures IV	Seed/Early Stage	09/01/03	20,000,000	13,440,000	1,492,347
	Abingworth Bioventures V	Early Stage	01/23/07	33,775,000	4,148,893	541
7.	Accel Europe	Early Stage	07/02/01	15,000,000	9,625,000	0
8.	Advent Latin American PE Fund IV	Buyouts	08/02/07	30,000,000	3,300,000	0
9.	Alpha Private Equity Fund 4	Mid Mkt. Buyouts	05/15/02	26,580,000	34,973,099	55,446,521
	Alpha Private Equity Fund 5	Mid Mkt. Buyouts	04/01/06	72,233,400	28,286,650	0
10.	Apollo Investment Fund IV	Buyouts	09/30/98	75,000,000	74,024,589	88,395,747
	Apollo Investment Fund V	Buyouts	08/23/01	50,000,000	46,936,735	71,119,071
	Apollo Investment Fund VI	Buyouts	07/19/06	40,000,000	14,384,059	394,070
11.	Asia Alternatives Capital Partners	Fund of Funds	06/26/07	50,000,000	5,469,656	12,963
12.	Asia Pacific Growth Fund III	Global Situations	09/28/99	15,000,000	15,257,100	6,017,004
13.	Audax Private Equity Fund	Mid Mkt. Buyouts	05/25/00	35,000,000	35,881,508	46,333,995
	Audax Private Equity Fund II	Mid Mkt. Buyouts	06/17/05	25,000,000	17,097,191	2,660,969
	Audax Private Equity Fund III	Mid Mkt. Buyouts	*	40,000,000	0	0

SERS Private Equity Investments Committed, Drawn and Distributed (continued)

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
14. Avenue Asia Special Situations Fund IV	Distressed Debt	06/30/06	$50,000,000	13,219,617	8,850
Avenue Special Situations Fund III	Distressed Debt	08/25/03	50,000,000	42,428,808	58,684,846
Avenue Special Situations Fund IV	Distressed Debt	03/27/06	50,000,000	50,000,000	0
Avenue Special Situations Fund V	Distressed Debt	06/04/07	70,000,000	13,347,117	160,278
15. B III Capital Partners	Distressed Debt	09/30/97	35,000,000	34,503,390	49,303,904
16. Bain Capital Fund VII	Buyouts	07/06/00	25,000,000	24,562,500	33,016,907
Bain Capital Fund VIII-E	Buyouts	12/15/04	13,405,000	10,611,493	0
Bain Capital IX Coinvestment Fund	Buyouts	04/20/06	15,000,000	10,612,500	0
Bain Capital Fund IX	Buyouts	04/10/06	75,000,000	53,250,000	4,937,278
Bain Capital X Coinvestment Fund	Buyouts	*	10,000,000	0	0
Bain Capital Fund X	Buyouts	*	90,000,000	0	0
Bain Capital Asia Fund	Distressed Debt	*	12,000,000	0	0
17. Baring Vostok Private Equity Fund IV	Buyouts	05/07/07	30,000,000	150,137	0
18. BC European Capital VII	Buyouts	07/28/00	37,345,000	37,754,746	44,326,163
BC European Capital VII Top Up	Buyouts	07/02/01	12,090,549	12,278,596	10,210,906
BC European Capital VIII	Buyouts	12/13/05	97,635,000	18,185,645	0
19. Berkshire Fund VI	Mid Mkt. Buyouts	07/11/02	20,000,000	16,738,760	10,962,024
Berkshire Fund VII	Mid Mkt. Buyouts	11/15/06	32,000,000	4,844,675	0
20. Blackstone Communications Partners I	Buyouts	08/29/00	25,000,000	26,329,274	21,971,315
Blackstone Capital II	Buyouts	09/30/94	40,000,000	42,827,676	92,873,019
Blackstone Capital III	Buyouts	12/31/97	75,000,000	74,342,317	115,013,533
Blackstone Capital IV	Buyouts	02/26/03	75,000,000	74,050,712	95,033,382
Blackstone Capital Partners V	Buyouts	05/30/06	150,000,000	81,681,925	6,684,825
21. Brait IV	Buyouts	04/02/07	25,000,000	7,126,561	0
22. Brynwood Partners V	Mid Mkt. Buyouts	07/31/05	10,000,000	8,719,160	0
23. Centerbridge Capital Partners I	Distressed Debt	02/27/07	50,000,000	5,946,145	0
24. Cerberus Institutional Partners	Distressed Debt	03/05/99	35,000,000	35,000,000	75,275,135
Cerberus Institutional Partners Series Two	Distressed Debt	10/09/01	35,000,000	30,100,793	65,460,759
Cerberus Institutional Partners Series Three	Distressed Debt	11/13/03	35,000,000	22,321,354	1,697,911
Cerberus Institutional Partners Series Four	Distressed Debt	11/27/06	75,000,000	33,375,000	0
25. Charterhouse Equity Partners II	Buyouts	03/31/94	40,000,000	43,849,172	100,462,834
Charterhouse Equity Partners III	Buyouts	12/31/97	50,000,000	55,395,586	65,848,588
26. Charterhouse Capital Partners VII	Buyouts	01/17/03	52,120,000	50,895,877	60,278,034
Charterhouse Capital Partners VIII	Buyouts	04/19/06	74,400,000	37,586,944	0
27. Chequers Capital XV	Buyouts	07/05/06	31,434,000	9,709,417	0
28. CID Greater China Venture Capital Fund II	Early Stage	08/10/07	20,000,000	8,000,000	0
29. Clayton Dubilier & Rice V	Buyouts	06/30/95	50,000,000	49,756,029	49,826,483
Clayton Dubilier & Rice VI	Buyouts	12/31/98	50,000,000	35,905,272	55,410,949

SERS Private Equity Investments Committed, Drawn and Distributed (continued)

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
30. Code Hennessy & Simmons	Buyouts	09 / 28 / 89	$10,000,000	9,650,000	29,205,907
Code Hennessy & Simmons II	Buyouts	06 / 30 / 94	20,000,000	20,000,000	69,111,676
Code Hennessy & Simmons III	Buyouts	09 / 30 / 97	40,000,000	38,724,000	54,918,648
Code Hennessy & Simmons IV	Mid Mkt. Buyouts	09 / 16 / 99	100,000,000	97,170,000	132,172,889
Code Hennessy & Simmons Equity V	Mid Mkt. Buyouts	11 / 10 / 05	50,000,000	24,293,109	1,878,892
31. Cognetas Fund II	Buyouts	11 / 02 / 05	52,072,000	22,504,180	2,566,249
32. CVI Global Value Fund	Distressed Debt	02 / 23 / 07	50,000,000	27,651,667	0
33. DLJ Merchant Banking Fund II	Buyouts	03 / 31 / 97	75,000,000	82,044,731	97,465,686
DLJ Merchant Banking Fund III	Buyouts	08 / 14 / 01	85,000,000	94,969,463	113,269,545
34. Elevation Partners	Private Equity	11 / 10 / 05	35,000,000	13,696,601	114,075
35. Energy Spectrum Partners IV	Mid Mkt. Buyouts	12 / 15 / 04	50,000,000	43,046,546	14,567,985
Energy Spectrum Partners V	Mid Mkt. Buyouts	07 / 09 / 07	30,000,000	672,594	0
36. Eureka II	Mid Mkt. Buyouts	01 / 30 / 06	20,000,000	4,422,461	291,601
37. Excelsior Capital Asia Partners III	Middle / Later Stage	08 / 17 / 06	25,000,000	6,179,465	40,602
38. First Reserve Fund X	Buyouts	10 / 28 / 04	30,000,000	28,010,045	26,782,907
First Reserve Fund XI	Buyouts	12 / 14 / 06	60,000,000	7,350,005	0
39. Francisco Partners	Buyouts	07 / 27 / 00	50,000,000	46,875,000	29,195,343
Francisco Partners II	Buyouts	07 / 10 / 06	30,000,000	13,050,000	0
40. Frontenac VII	Buyouts	09 / 30 / 97	40,000,000	40,000,000	54,738,396
41. Great Hill Equity Partners	Buyouts	04 / 12 / 99	30,000,000	30,000,000	28,221,438
Great Hill Equity Partners II	Buyouts	03 / 28 / 01	35,000,000	35,063,336	44,268,235
Great Hill Equity Partners III	Mid Mkt. Buyouts	03 / 07 / 06	35,000,000	16,791,250	0
42. Gryphon Partners II	Buyouts	11 / 03 / 99	35,000,000	35,881,393	30,772,309
Gryphon Partners III	Buyouts	09 / 08 / 04	30,000,000	17,294,291	4,312,655
43. GTC&R V	Buyouts	03 / 31 / 97	11,400,000	11,400,000	19,475,171
GTC&R VI	Buyouts	09 / 30 / 98	50,000,000	50,854,013	41,819,443
GTC&R VII	Buyouts	03 / 15 / 00	55,000,000	48,046,546	86,731,469
GTCR VIII	Buyouts	07 / 07 / 03	75,000,000	69,393,599	57,067,322
GTCR IX	Early Stage	12 / 01 / 06	50,000,000	6,666,013	3,161,153
44. Hancock IPEP II (Harbourvest II)	Fund of Funds	06 / 30 / 97	25,000,000	24,357,775	30,812,435
HarbourVest IPEP lll	Fund of Funds	06 / 30 / 98	40,000,000	38,400,000	31,668,683
Harbourvest IPEP IV	Fund of Funds	04 / 09 / 01	40,000,000	32,400,000	20,583,264
HIPEP V-Asia Pacifc & RoW	Buyouts	05 / 09 / 06	30,000,000	7,395,316	0
45. Hellman Friedman III	Buyouts	06 / 30 / 95	50,000,000	40,308,123	91,811,279
Hellman Friedman IV	Buyouts	02 / 14 / 00	75,000,000	66,540,777	140,778,980
Hellman Friedman V	Buyouts	12 / 20 / 04	80,000,000	68,267,655	11,558,233
Hellman & Friedman Capital Partners VI	Buyouts	06 / 05 / 07	125,000,000	30,038,253	0
46. Insight Venture Partners VI	Buyouts	08 / 21 / 07	30,000,000	960,000	0
47. InterMedia Partners VII	Diversified	01 / 05 / 07	15,000,000	7,941,763	142,200
48. Invemed Catalyst Fund	Mid Market Buyouts	10 / 19 / 99	16,754,888	13,376,510	4,929,794

SERS Private Equity Investments Committed, Drawn and Distributed (continued)

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
49. J.H. Whitney V	Later Stage	03 / 29 / 01	$20,000,000	21,858,315	32,598,724
J.H. Whitney VI	Buyouts	01 / 05 / 06	50,000,000	25,378,548	8,221,368
50. JP Morgan US Corp Finance Investors II	Fund of Funds	01 / 14 / 03	50,000,000	37,967,707	12,831,889
51. J.W. Childs Equity Partners III	Mid Mkt. Buyouts	08 / 20 / 02	40,000,000	37,432,049	28,222,308
52. Kelso Investment Associates V	Buyouts	12 / 31 / 93	40,000,000	54,411,479	152,923,297
Kelso VI	Buyouts	09 / 30 / 98	75,000,000	69,057,922	80,127,191
Kelso VII	Buyouts	10 / 18 / 04	40,000,000	30,745,767	9,826,377
Kelso VIII	Buyouts	*	150,000,000	0	0
53. Landmark Equity IV	Secondaries	03 / 31 / 95	14,923,291	12,880,353	18,474,353
Landmark Equity Partners V	Secondaries	12 / 31 / 95	19,624,113	19,434,947	23,132,550
54. Leeds Equity Partners IV	Mid Mkt. Buyouts	11 / 12 / 04	20,000,000	15,154,807	0
55. Lexington Capital Partners II	Secondaries	06 / 30 / 98	40,000,000	39,538,000	44,204,264
Lexington Capital Partners III	Secondaries	01 / 26 / 99	35,000,000	34,169,949	35,603,195
Lexington Capital Partners V	Secondaries	01 / 17 / 02	75,000,000	69,570,753	68,851,975
Lexington Capital Partners VI	Secondaries	10 / 21 / 05	50,000,000	17,798,899	3,072,554
56. Lime Rock Partners III	Later Stage	03 / 07 / 05	15,000,000	10,301,107	2,239,042
Lime Rock Partners IV	Later Stage	11 / 16 / 06	25,000,000	5,190,438	0
Lime Rock Resources	Diversified	12 / 28 / 05	20,000,000	6,014,486	120,778
57. LLR Equity Partners	Mid Mkt. Buyouts	02 / 04 / 00	25,000,000	24,341,235	38,531,299
LLR Equity Partners II	Mid Mkt. Buyouts	01 / 29 / 04	25,000,000	15,237,377	4,513,889
58. Madison Dearborn Capital Partners	Buyouts	03 / 31 / 93	15,000,000	14,538,849	44,936,487
Madison Dearborn Capital Partners II	Buyouts	03 / 31 / 97	40,000,000	40,152,017	90,363,219
Madison Dearborn Capital Partners III	Buyouts	04 / 06 / 99	75,000,000	76,195,099	96,508,584
Madison Dearborn Capital Partners IV	Buyouts	04 / 02 / 01	90,000,000	83,492,915	38,743,729
Madison Dearborn Capital Partners V	Buyouts	12 / 14 / 06	75,000,000	47,839,214	0
59. MatlinPatterson GOP	Distressed Debt	05 / 31 / 01	35,000,000	34,251,484	53,723,890
Matlin Patterson GOP II	Distressed Debt	06 / 30 / 04	30,000,000	30,949,780	13,201,968
60. Media / Communication III	Buyouts	06 / 30 / 97	25,000,000	23,750,000	35,057,571
Media / Communications IV	Buyouts	03 / 31 / 99	25,000,000	23,125,000	5,010,893
Media / Communications Ventures Fund V	Buyouts	09 / 27 / 00	35,000,000	33,150,341	14,935,375
61. Meridian Venture Partners II	Buyouts	02 / 11 / 05	10,000,000	10,000,000	823,344
62. New York Life Capital Partners III	Secondaries	06 / 30 / 06	50,000,000	29,977,053	933,658
New York Life Capital Partners IV	Secondaries	*	100,000,000	0	0
63. Newbridge Asia III	Buyouts	02 / 15 / 01	15,000,000	15,123,450	7,070,976
Newbridge Asia IV	Buyouts	09 / 27 / 05	40,000,000	21,000,943	2,721,435
64. Nordic Capital V	Buyouts	05 / 07 / 04	40,000,000	43,871,777	19,921,452
Nordic Capital VI	Buyouts	07 / 25 / 06	54,441,000	39,492,719	1,128,843
Nordic Capital VII	Buyouts	*	100,237,900	0	0
65. Oakhill Capital Partners	Buyouts	05 / 17 / 99	50,000,000	53,092,280	64,592,965

SERS Private Equity Investments Committed, Drawn and Distributed (continued)

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
66. Oaktree Capital Management	Diversified	05/28/04	$40,000,000	40,577,048	22,662,091
OCM Opportunities Fund	Distressed Debt	01/31/96	24,000,000	24,000,000	38,706,715
OCM Opportunities Fund II	Distressed Debt	03/31/98	40,000,000	40,000,000	59,655,678
OCM Opportunities Fund III	Distressed Debt	01/20/00	60,000,000	60,007,890	87,331,393
OCM Opportunities Fund IV	Distressed Debt	09/26/01	70,000,000	68,250,000	113,156,990
OCM Opportunities Fund V	Distressed Debt	08/12/04	40,000,000	40,003,507	43,836
OCM Opportunities Fund VI	Distressed Debt	09/28/05	40,000,000	40,000,000	0
OCM Opportunities Fund VII	Distressed Debt	05/16/07	40,000,000	10,000,000	0
OCM Opportunities Fund VIIb	Distressed Debt	*	40,000,000	0	0
OCM Principal Opportunities	Distressed Debt	12/31/96	25,000,000	25,000,000	30,026,606
OCM Principal Opportunities II	Distressed Debt	04/24/01	25,000,000	25,000,000	34,191,421
OCM Principal Opportunities Fund IV	Distressed Debt	01/24/07	20,000,000	7,000,000	38,751
OCM/GFI Power Opportunities Fund II	Buyouts	05/09/05	25,000,000	2,133,174	29,205
67. Palamon European Equity	Buyouts	07/23/99	31,499,291	33,308,696	26,639,661
Palamon European Equity II	Diversified	10/25/05	40,114,200	14,175,684	0
68. Parthenon Investors II	Mid Mkt. Buyouts	08/09/01	20,000,000	18,981,604	13,713,886
69. Permira European Fund	Buyouts	09/30/97	33,789,023	32,159,947	83,708,331
Permira European Fund II	Buyouts	06/07/00	47,979,751	43,846,362	78,101,935
Permira European Fund III	Buyouts	01/12/04	112,640,170	97,612,820	77,764,408
Permira IV	Buyouts	12/14/06	126,870,000	34,451,930	0
Permira UK Venture Fund III	Middle/Later Stage	03/31/91	9,063,438	8,946,988	26,106,191
Permira UK Venture Fund IV	Middle/Later Stage	12/31/95	15,000,000	15,993,572	22,721,533
70. Pitango Venture Capital Fund IV	Diversified	07/19/04	20,000,000	12,001,534	199,335
Pitango Venture Capital Fund V	Seed/Early Stage	08/22/07	30,000,000	600,000	0
71. PNC Equity Partners II	Mid Mkt. Buyouts	08/30/07	15,000,000	2,331,340	0
72. Providence Equity Partners IV	Mid Mkt. Buyouts	11/27/00	25,000,000	27,336,438	32,929,207
Providence Equity Partners V	Mid Mkt. Buyouts	04/04/05	50,000,000	42,439,406	342,918
Providence Equity Partners VI	Buyouts	03/16/07	50,000,000	12,451,654	0
73. Sankaty Credit Opportunities III	Distressed Debt	03/08/07	50,000,000	30,000,000	0
74. S.B. Energy Partners I	Buyouts	07/27/07	25,000,000	1,090,867	0
75. SCP Private Equity Partners II	Buyouts	06/15/00	25,000,000	23,831,313	4,864,740
76. Segulah IV	Mid Mkt. Buyouts	*	15,688,890	0	0
77. ShoreView Capital Partners	Buyouts	06/16/03	38,000,000	27,311,618	32,517,614
ShoreView Capital Partners II	Buyouts	*	50,000,000	0	0
78. Siguler Guff BRIC Opportunities Fund	Fund of Funds	05/08/06	10,000,000	3,858,299	335,077
79. Sterling Capital Partners	Buyouts	10/31/02	15,000,000	13,380,637	4,398,878
Sterling Capital Partners II	Buyouts	08/18/05	30,000,000	19,409,937	1,726,778
Sterling Capital Partners III	Buyouts	08/13/07	32,000,000	3,968,473	0
80. Summit Ventures VI	Later Stage	03/23/01	62,000,000	62,087,469	41,963,606
Summit Partners Private Equity Fund VII	Buyouts	02/09/06	97,134,500	29,626,022	1,384,412

SERS Private Equity Investments Committed, Drawn and Distributed (continued)

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed	Capital Drawn	Distributions
81. TA / Advent IX	Later Stage	09 / 20 / 00	$45,000,000	43,650,000	44,648,248
TA / Advent X	Middle / Later Stage	04 / 25 / 06	70,000,000	34,650,000	0
82. Thomas H. Lee Equity Fund IV	Buyouts	06 / 30 / 98	70,000,000	63,950,100	52,462,423
Thomas H Lee Equity Fund V	Buyouts	07 / 03 / 01	100,000,000	101,587,292	83,430,869
Thomas H. Lee Equity Fund VI	Mid Mkt. Buyouts	11 / 14 / 06	50,000,000	14,438,840	252,171
83. TPG Partners II	Buyouts	06 / 30 / 97	75,000,000	76,286,247	111,455,282
TPG Partners III	Buyouts	01 / 13 / 00	75,000,000	69,088,279	119,714,435
TPG Partners IV	Buyouts	12 / 29 / 03	30,000,000	30,941,853	16,398,735
TPG Partners V	Buyouts	06 / 27 / 06	100,000,000	36,952,999	133,294
TPG Asia V	Buyouts	*	25,000,000	0	0
84. UMS Partners Fund I	Distressed Debt	02 / 15 / 05	5,000,000	5,000,000	164,250
85. Versa Capital Partners	Distressed Debt	10 / 16 / 05	20,000,000	11,011,753	4,567,251
86. Vestar Capital Partners III	Buyouts	06 / 30 / 97	25,000,000	23,258,343	22,540,868
Vestar Capital Partners IV	Mid Mkt. Buyouts	01 / 25 / 00	100,000,000	94,743,119	80,821,638
Vestar Capital Partners V	Mid Mkt. Buyouts	01 / 25 / 06	50,000,000	21,430,926	2,443,654
87. W Capital Partners II	Secondaries	08 / 08 / 07	40,000,000	4,937,824	0
Total Active Private Equity Commitments			**$9,027,394,856**	**5,949,466,094**	**5,452,828,575**

**Not funded as of 9/30/07*
Cash flows as of 9/30/07

Inactive Private Equity Funds

Limited Partnership	Committed	Drawn	Distributions
Total Inactive Private Equity	**$123,830,323**	**127,105,590**	**192,520,148**

Inflation Protection is one of eight major asset classes that SERS uses for investments of the Fund. The objective of this asset class is to reduce the deleterious affects of inflation by investing in strategies that specifically respond to expected and unexpected inflation. SERS contracts with external investment advisors to manage portfolios.

Investment Objective: Inflation Protection investments are employed by the Fund to provide diversification within the total portfolio and to act as a hedge against inflation. The asset class is composed of a combination of commodities; TIPS; and a diversified inflation protection portfolio that includes commodities, inflation–sensitive stocks, and bonds. The strategies that make up the asset class were chosen for their inflation protection properties; commodities historically have the highest correlation to inflation and TIPS are adjusted periodically for actual changes in inflation. The Inflation Protection strategies also provide diversification and low correlation to other assets in the portfolio, and are expected to outperform stocks and bonds during rising inflationary periods, but may underperform when inflation is stable or falling.

SERS' long term investment objective in the inflation protection asset class is to achieve a total return, net of fees, that exceeds the total return of the Customized Inflation Protection Benchmark.

At the March 14, 2007 Board meeting, the Board approved a proposal to reallocate a portion of the passively–managed commodity assets to actively–managed commodity strategies. In conjunction with that proposal, the Board approved the addition of an active multi–manager commodity fund to the asset class. The allocation to the diversified inflation protection portfolio was also increased modestly. The Inflation Protection program structure as of December 31, 2007 included both indexed and actively–managed commodity portfolios, TIPS, and the diversified inflation protection portfolio. The passive commodity and TIPS portfolio had a long term target of 2.0% of Fund assets, the active multi–manager commodity portfolio had a long–term target of 2.5% of Fund assets, and the active diversified inflation protection portfolio had a long term target of 2.5% of Fund assets.

Market Exposure as of December 31, 2007: Inflation protection strategies had a $2,624.4 million market exposure, 7.4% of the total Fund's $35,542.2 million fair value on December 31, 2007.

Number of Investment Advisors: SERS had contracts with 3 external investment advisors to manage the Inflation Protection portfolios.

Number of Investment Portfolios: SERS had Inflation Protection portfolios managed by the 3 investment advisors.

Types of Investment Portfolios: As of December 31, 2007, 27% of SERS' Inflation Protection allocation was in a passive commodity portfolio that achieves the commodity index return by employing swap agreements. The underlying cash for the swaps was invested in intermediate–duration TIPS that generate higher incremental return above typical cash instruments. Another 38% of the Inflation Protection allocation was in the actively–managed diversified inflation protection portfolio which invests in commodities, inflation–sensitive global equity and TIPS. The remaining 35% was in the multi–manager commodity product, which employs seven underlying commodities managers across the various commodity sectors (energy, precious metals, industrial metals and agriculture).

SERS Inflation Protection Investments

	Inflation Protection Investment Advisor	Investment Style	Market Exposure* As of 12/31/07 ($ Millions)
1.	NISA Investment Advisors	Indexed commodities and TIPS	$705.7
2.	Wellington Management Company	Diversified inflation protection portfolio	996.4
3.	Blackstone Alternative Asset Management	Commodity fund of funds	922.3
	Total Inflation Protection		**$2,624.4**

**Includes securities and cash that the manager had available for investment. Numbers may not add due to rounding.*

Actuarial Section

Hay Group. Inc.
Suite 600
4301 North Fairfax Drive
Arlington, VA 22203
USA

April 30, 2008

Mr. Leonard M. Knepp
Executive Director
State Employees' Retirement System
30 North Third Street
Suite 150
Harrisburg, PA 17101-1716

HayGroup®

Dear Mr. Knepp:

The purpose of this letter is to certify the actuarial adequacy of the contributions being made by the Commonwealth of Pennsylvania and other participating agencies to the Pennsylvania State Employees' Retirement System (SERS), and to discuss the approach currently being taken toward meeting the financing objectives of the plan. The results provided herein are based upon the December 31, 2007 annual actuarial valuation.

The funding objective of the plan is set forth in the SERS code. The annual employer contribution is equal to the sum of the following for the fiscal year beginning July 1, 2008:

(1) The employer share of the normal cost.
(2) The amortization of the December 31, 2001 liability for Act 2001-9 benefits over a 30-year period beginning July 1, 2002 and ending on June 30, 2032.
(3) The amortization of the remaining unfunded liabilities as of December 31, 2001 over a ten-year period beginning July 1, 2002 and ending on June 30, 2012.
(4) The amortization of all unfunded liabilities due to supplemental annuities (COLAs) after 2001, or other legislated benefit improvements after June 30, 2003, over ten-year periods beginning with the July first following the effective date of the change.
(5) The amortization of changes in liability due to actual experience differing from assumed experience after December 31, 2001 over 30-year periods beginning with the July first following the actuarial valuation determining such changes.

The amortization payments are level amounts over the applicable amortization periods. The employer cost is determined as a percent of payroll, and the employer contributes that percent of the payroll of all covered members during each fiscal year.

All costs and liabilities have been determined in conformance with generally accepted actuarial principles and procedures in accordance with the principles of practice prescribed by the American Academy of Actuaries. The calculations were performed on the basis of actuarial assumptions and methods, which are internally consistent, and reasonable (taking into account past experience under the SERS and reasonable expectations) and which in combination represent the best estimate of anticipated experience under the plan.

The actuarial valuation is based on financial and participant data, which is prepared by SERS staff. The data are reviewed for internal and year-to-year consistency as well as general reasonableness prior to their use in the actuarial valuation.

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Mr. Leonard M. Knepp
April 30, 2008
Page 2

The actuarial valuation uses assumptions regarding future rates of investment return and rates of retirement, withdrawal, death, and disability among SERS members and their beneficiaries. The current set of assumptions used in the December 31, 2007 actuarial valuation was adopted by the Board and was based on actual experience of SERS during the years 2001 through 2005. The actuarial value of assets is developed by recognizing the difference between the expected actuarial value of assets and the market value of assets over a five-year period.

Governmental Accounting Standards Board (GASB) Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* establishes a range of actuarial cost and amortization methods for the Unfunded Actuarial Accrued Liability. The scheduled payments since July 1, 2005 have been below the minimum amount required to meet the GASB #25 minimum. This is a temporary result of financing changes implemented by Act 2003-40 in December 2003. After June 30, 2009, we expect the SERS contribution to exceed the GASB #25 minimum.

The "Schedule of Funding Progress" and "Schedule of Employer Contributions" included in the Financial Section are provided as part of the accounting disclosure statements in accordance with GASB #25. These two schedules were derived from the December 31, 2007 actuarial valuation.

With the exception of the "Schedule of Retirees and Beneficiaries Added to and Removed from Rolls" and the "Summary of Plan Provisions", the schedules appearing in the Actuarial Section were derived from the December 31, 2007 actuarial valuation.

Based upon the valuation results, it is our opinion that the Pennsylvania State Employees' Retirement System is in sound condition in accordance with generally accepted actuarial principles and procedures. The employer contribution has been below the GASB #25 minimum since July 1, 2005 and will likely remain below the minimum through June 30, 2009. However, we project that the employer payments scheduled after that time are above the GASB minimum and that the plan is in sound condition over the long run.

Respectfully submitted,
Hay Group

By Brent M. Mowery
Brent M. Mowery, F.S.A.
Member American Academy of Actuaries
Enrolled Actuary No. 08-3885

By Adam J. Reese
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- The investment rate of return is 8.5% per year based on an underlying rate of inflation of 3.0% per year.

- The Plan uses a five–year smoothed market approach to value plan assets for actuarial purposes.

- Actuarial methods are specified by statute. Actuarial assumptions are recommended by the plan's actuary and approved by the SERS Board of Trustees.

- For current and future non-disabled retirees, beneficiaries, and survivors, the plan uses the RP-2000 Healthy Annuitant Mortality Table projected to 2008. For current and future disabled retirees, the plan uses the RP-2000 Disabled Retiree Annuitant Mortality Table projected to 2008. For all pre-retirement active employees, the mortality is based on actual SERS experience.

- The rates for probability of retirement and the probabilities of withdrawal from active service, including death, before age and service retirements are presented in the Schedule of Active Member Valuation Data.

- The projected average salary increase is 7.1% with a range of 4.9% to 20.2%. This increase includes an underlying assumption of 3.0% for inflation. The annual rate of salary increase for promotions and longevity for members is presented in the Schedule of Active Member Valuation Data.

- The Plan uses a variation of the entry-age normal actuarial cost method to determine the liabilities and costs related to the System's benefits. The method is based on the benefits and contributions for new employees rather than for all current employees from their date of entry. This variation should produce approximately the same results as the typical method over the long run. The Plan uses amortization periods of 10 years and 30 years as follows.

    (1) The amortization of the December 31, 2001 liability for Act 2001-9 benefits over a 30-year period beginning July 1, 2002 and ending on June 30, 2032.

    (2) The amortization of the remaining unfunded liabilities as of December 31, 2001 over a ten-year period beginning July 1, 2002 and ending on June 30, 2012.

    (3) The amortization of all unfunded liabilities due to supplemental annuities (COLAs) after 2001, or other legislated benefit improvements after June 30, 2003, over ten-year periods beginning with the July first following the effective date of the change.

    (4) The amortization of changes in liability due to actual experience differing from assumed experience after December 31, 2001 over 30-year periods beginning with the July first following the actuarial valuation determining such changes.

- The Plan does not use an assumption for cost-of-living adjustments in the determination of actuarial valuations.

- The Plan periodically prepares a study using actual experience in order to develop assumptions to be used in its actuarial valuations. The latest study was completed March 15, 2006, for the period January 1, 2001, through December 31, 2005.

- The most recent valuation was based on members of the Plan as of December 31, 2007. All census data was supplied by the Plan and was subject to reasonable consistency checks. Asset data was also supplied by the Plan.

- The actuarial computations were prepared by, or made under the supervision, of a Member of the American Academy of Actuaries (M.A.A.A.).

Table A[a.]
Withdrawal From Active Employment Before Age & Service Retirement
Annual Rate of Active Members Separating Within the Next Year

Sample Age	Male Withdrawal Years of Service 0	5	9	14+	Male Death	Male Disability	Female Withdrawal Years of Service 0	5	9	14+	Female Death	Female Disability
20	11.85%	-	-	-	0.02	-	11.19%	-	-	-	0.02	-
25	11.60	1.97	1.97	-	0.02	0.03	10.24	2.68	2.12	-	0.02	0.07
30	11.11	1.97	1.48	1.54	0.03	0.09	10.24	2.68	1.88	2.03	0.02	0.17
35	10.86	1.83	1.00	1.05	0.05	0.16	10.24	2.21	1.41	1.55	0.03	0.29
40	10.86	1.28	1.00	1.05	0.06	0.25	10.01	2.21	0.85	0.61	0.05	0.38
45	10.49	1.28	0.49	0.56	0.12	0.44	9.77	1.98	0.85	0.61	0.07	0.60
50	10.24	1.14	0.49	0.56	0.21	0.61	9.77	1.98	0.47	0.61	0.12	0.91
55	10.24	1.48	1.48	1.54	0.33	0.80	9.77	1.65	1.41	1.55	0.18	1.15
60	-	-	-	-	0.48	-	-	-	-	-	0.30	-

Table B[a.]
Annual Rate of Retirement

Sample Age	Full Benefits Male	Full Benefits Female
45-59	30.0%	30.0
60-61	25.0	25.0
62	33.0	33.0
63-64	22.0	22.0
65	33.0	33.0
66 - 79	22.0	22.0
80	100.0	100.0

Table C
Annual Rate of Salary Increase

Completed Years of Service	Increase
1	16.9%
2	8.3
3	5.9
4	4.6
5	4.2
6-10	3.2
11-15	2.8
16-20	2.4
21-25	1.8
26+	1.6

Table D
Reduced Benefits

Sample Age	5 - 14 Years of Service Male	5 - 14 Years of Service Female	15 or More Years of Service Male	15 or More Years of Service Female
20	-	-	-	-
25	3.0%	3.9	-	-
30	2.5	3.5	-	-
35	1.9	2.8	2.6	2.7
40	1.7	1.7	2.6	2.7
45	1.1	1.6	2.6	2.7
50	1.0	1.3	2.6	2.7
55	2.3	2.3	3.9	3.9

[a.] *The assumptions presented in Table A and Table B on this page were based on a review of SERS' experience from 2001 through 2005. The rates are the probabilities that an event will occur in the year after the valuation. For instance, the male retirement rate of 33% at age 62 means that 330 of every 1,000 male employees age 62 and eligible for full benefits are expected to retire before they reach age 63.*

Active Members by Age and Years of Service - Male

	Years of Service								
Age Group	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 Plus	Total	Average Salary
< 20	36	-	-	-	-	-	-	36	$22,567
20 - 24	1,192	11	-	-	-	-	-	1,203	29,121
25 - 29	3,339	576	5	-	-	-	-	3,920	36,811
30 - 34	2,522	1,868	466	6	-	-	-	4,862	42,337
35 - 39	2,232	2,174	2,393	1,026	33	-	-	7,858	50,292
40 - 44	1,939	1,719	1,867	2,521	1,008	32	-	9,086	53,451
45 - 49	1,869	1,543	1,347	1,843	2,128	1,080	34	9,844	53,561
50 - 54	1,719	1,466	1,301	1,536	1,677	1,690	934	10,323	54,452
55 - 59	1,527	1,239	1,196	1,335	1,269	1,296	1,673	9,535	55,979
60 - 64	912	701	701	695	529	351	643	4,532	56,176
65+	326	305	300	202	132	89	281	1,635	62,167
Total	**17,613**	**11,602**	**9,576**	**9,164**	**6,776**	**4,538**	**3,565**	**62,834**	**$51,663**

Average Age: 46.11

Average Service: 12.22

Active Members by Age and Years of Service - Female

	Years of Service								
Age Group	0 - 4	5 - 9	10 - 14	15 - 19	20 - 24	25 - 29	30 Plus	Total	Average Salary
< 20	50	-	-	-	-	-	-	50	$22,612
20 - 24	1,171	22	-	-	-	-	-	1,193	27,528
25 - 29	2,515	664	25	-	-	-	-	3,204	34,003
30 - 34	1,929	1,287	359	30	-	-	-	3,605	38,133
35 - 39	1,870	1,397	989	604	64	-	-	4,924	41,000
40 - 44	1,808	1,225	880	1,099	721	75	-	5,808	42,993
45 - 49	1,942	1,434	995	1,166	1,146	1,115	99	7,897	45,679
50 - 54	1,800	1,350	1,082	1,320	1,102	1,348	1,217	9,219	47,520
55 - 59	1,175	1,012	832	1,120	1,044	943	1,175	7,301	48,502
60 - 64	463	498	464	431	362	240	256	2,714	47,421
65+	124	185	186	129	84	47	106	861	45,670
Total	**14,847**	**9,074**	**5,812**	**5,899**	**4,523**	**3,768**	**2,853**	**46,776**	**$43,888**

Average Age: 45.95

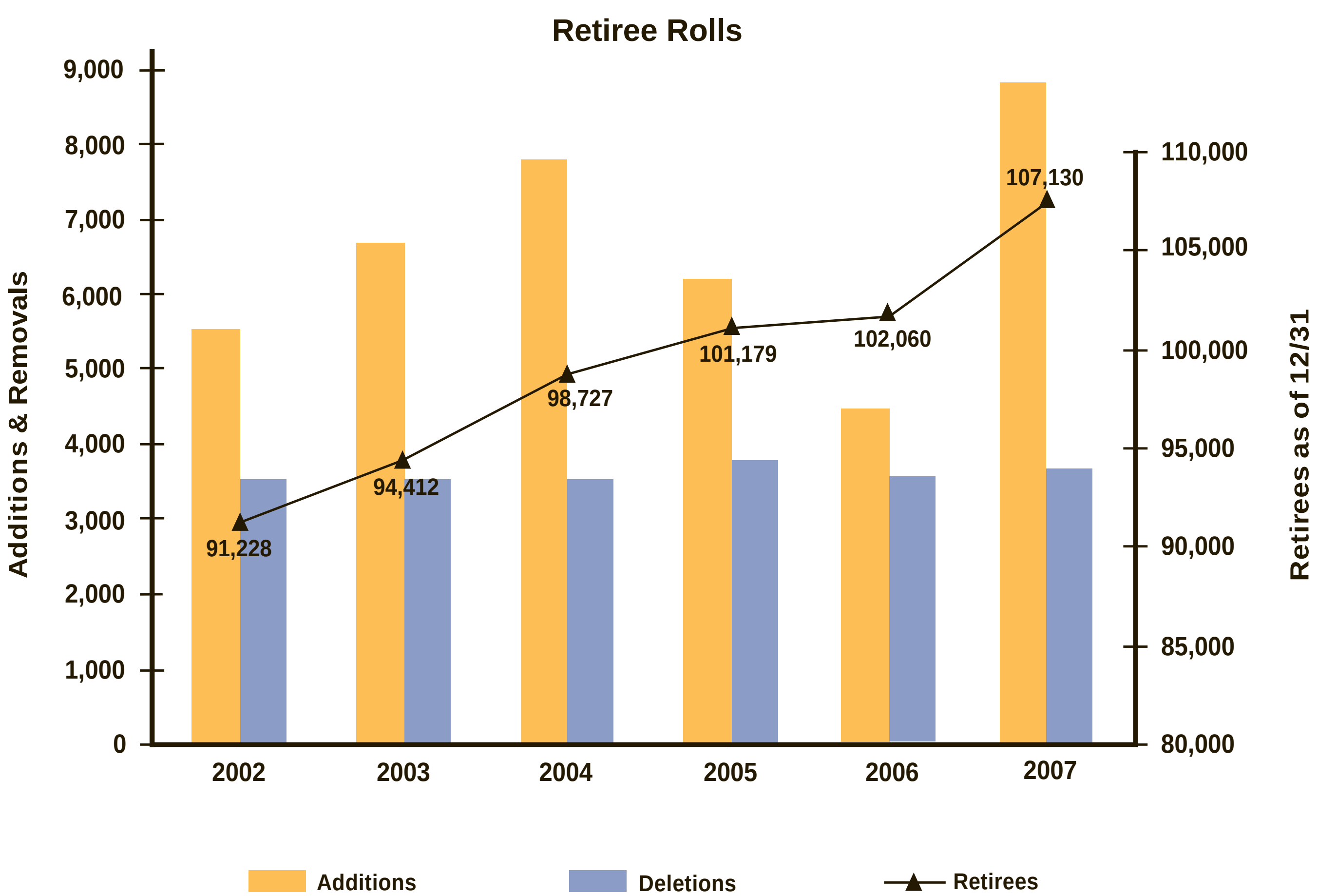
Average Service: 11.76

Aggregate Active Member Valuation Data

Valuation Date	Number Employers	Number Active Members	Annual Payroll	Annual Average Pay	% Increase /(Decrease) in Average Pay
31-Dec-07	108	109,610	$5,299,000,000	48,345	4.8%
31-Dec-06	108	110,972	5,118,000,000	46,118	2.9
31-Dec-05	108	109,981	4,929,000,000	44,815	(1.2)
31-Dec-04	108	108,405	4,920,000,000	45,382	1.9
31-Dec-03	106	109,018	4,853,000,000	44,519	2.0
31-Dec-02	105	111,059	4,846,000,000	43,631	3.5

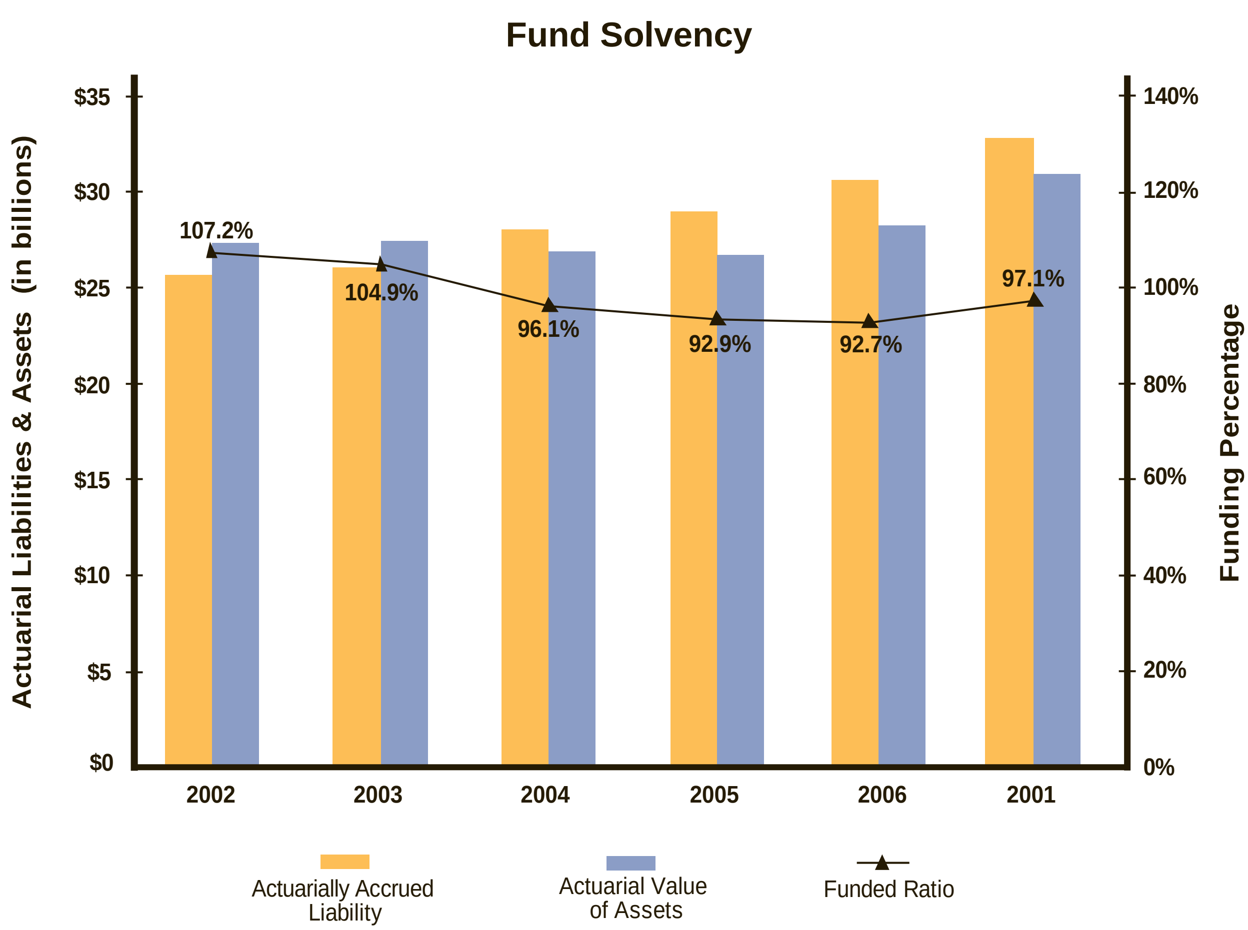
Schedule of Retirees and Beneficiaries Added To and Removed From Rolls
Six Years Ended December 31, 2007

	Added to Rolls		Removed From Rolls		Rolls-End of Year		Percentage Change	
Year	No.	Annual Allowances	No.	Annual Allowances	No.	Annual Allowances	No.	Annual Allowance
2007	8,761	$234,585,550	3,691	$42,238,843	107,130	$1,847,681,816	4.97%	11.58
2006	4,514	96,324,336	3,633	40,351,097	102,060	1,655,881,296	0.87	3.44
2005	6,298	149,935,613	3,846	40,984,887	101,179	1,600,772,520	2.48	7.22
2004	7,905	198,252,778	3,590	37,279,580	98,727	1,492,913,832	4.57	12.04
2003	6,769	161,875,423	3,585	36,430,746	94,412	1,332,443,772	3.49	14.28
2002	5,605	126,087,119	3,594	31,408,470	91,228	1,165,985,640	2.25	12.92



Solvency Test
Six Years Ended December 31, 2007
Dollar Amounts in Thousands

	Aggregate Accrued Liabilities For					Portion of Accrued Liabilities Covered by Reported Assets			
	(1)	(2)	(3)						
Valuation Date	Active Member Contributions	Retirees & Beneficiaries	Active Members (Employer Financed Portion)	Total Actuarial Accrued Liability (AAL)	Actuarial Valuation of Assets	(1)	(2)	(3)	Funded Ratio
31-Dec-07	$3,849,293	16,255,843	11,648,835	**31,753,971**	30,839,877	100.0%	100.0	92.2	97.1
31-Dec-06	3,916,841	14,474,525	11,973,631	**30,364,997**	28,148,834	100.0	100.0	81.5	92.7
31-Dec-05	3,696,477	14,000,196	11,155,043	**28,851,716**	26,793,782	100.0	100.0	81.6	92.9
31-Dec-04	3,593,576	12,779,570	11,625,880	**27,999,026**	26,900,027	100.0	100.0	90.5	96.1
31-Dec-03	3,588,664	11,296,520	11,294,577	**26,179,761**	27,465,615	100.0	100.0	100.0	104.9
31-Dec-02	3,498,672	10,129,669	12,022,048	**25,650,389**	27,497,464	100.0	100.0	100.0	107.2



Gains & Losses in Accrued Liabilities Resulting From Differences Between Assumed Experience and Actual Experience
(Dollar Amounts in Thousands)

Type of Activity	2007	2006	2005	2004
Gain(Loss) from Investment Earnings	$2,158,662	568,176	(815,133)	(1,372,930)
Demographic Assumptions	(355,062)[a.]	(92,597)	4,931	15,539
Pay Increases	43,448	(213,715)	23,806	(156,133)
Other	-	73,112	42,858	(179,410)
Gain(Loss) During Year From Financial Experience	1,847,048	334,976	(743,538)	(1,692,934)
Non Recurring Items:				
Changes in Actuarial Methods and Assumptions	-	6,546	248,873[b.]	(249,607)
Composite Gain(Loss)	**$1,847,048**	**341,522**	**(494,665)**	**(1,942,541)**

a. 2007 demographic assumptions include a $113 million increase from the change in demographics of new entrants, which was offset by a $468 million decrease resulting from greater than expected retirements and other demographic changes.

b. Adoption of the assumptions from the 2005 experience study reduced the liability and employer contribution. The change in the salary increase assumptions from an age-based to service-based schedule reduced the unfunded liability by $874 million. Other experience study changes increased the unfunded liability by $536 million so the net effect of the experience study was to reduce the unfunded liability by $338 million. Changes resulting from the actuarial audit increased the unfunded liability by $89 million.

Benefit and Contribution Provisions
as of December 31, 2007

The State Employees' Retirement System makes provisions for retirement, disability, and death benefits for all State employees and certain other eligible groups. The major provisions may be summarized as follows:

Eligible Employees

Class A

All regular State employees and employees of certain Commissions and Authorities and employees of state-owned educational institutions and the Pennsylvania State University (unless such employees have joined the Public School Employees' Retirement System (PSERS), TIAA-CREF, or Alternative Retirement Program (ARP)) hired before July 1, 2001 who did not elect into the Class AA membership as of December 31, 2001. This excludes Judges and Magisterial District Judges who have elected Class E-1 or Class E-2.

Class AA

All regular State employees who are hired after July 1, 2001, and former Class A State employees hired before July 1, 2001 who elected into Class AA as of December 31, 2001. This includes employees of certain Commissions and Authorities, and employees of state-owned educational institutions and the Pennsylvania State University (unless such employees have joined PSERS, TIAA-CREF or ARP), but excludes State Police Troopers, Judges, Magisterial District Judges and Legislators with Class D-3 or D-4.

Class C

Liquor Law enforcement officers, other officers and certain employees of the State Police who have been members and employees continuously since prior to March 1, 1974.

Class D-3

Members of the General Assembly who have been members and employees continuously since prior to March 1, 1974.

Class D-4

Legislators who are elected after July 1, 2001, and legislators hired before July 1, 2001 who elected into this class, excluding Class D-3 members.

Class E-1

Judges

Class E-2

Magisterial District Justices

Age and Service Requirements for Superannuation (Full Formula Benefits)

Class AA/A

Age 60 with three years of service; except for members of the General Assembly, enforcement officers, correction officers, psychiatric security aids and officers of the Delaware River Port Authority for whom the requirement is age 50 with three years of service. Members of Class AA/A with 35 years of credited service are entitled to full formula benefits regardless of age. State Police Officers can retire on full benefits after age 50 or with 20 years of service. Capitol Police and Park Rangers can retire on full benefits at age 50 with 20 years of Capitol Police or Park Ranger service.

Class C

Age 50, with three years of service.

Class D-3

Age 50, with three years of service.

Class D-4

Age 50, with three years of service.

Class E-1

Age 60, with three years of service; or 35 or more years of credited service, regardless of age.

Class E-2

Age 60, with three years of service; or 35 or more years of credited service, regardless of age.

Formula for Superannuation Annuity

The standard single-life annuity for most members is 2% of the high three-year average salary of the member multiplied by years and fractions of credited service multiplied by the Multiplier of the Class of membership.

The annuity paid to a member shall not exceed the member's highest salary during any period of 12 consecutive months of creditable service.

The multipier for each of the major classes are as follows:

Multipier for Major Classes

Class	Multiplier	
A	1.00	For State Police with years of service between 20 and 25, the minimum annuity is 50% of highest annual salary. With more than 25 years of service the benefit is a minimum of 75% of highest annual salary.
AA	1.25	
C	1.00	For State Police with years of service between 20 and 25, the minimum annuity is 50% of highest annual salary. With more than 25 years of service the benefit is a minimum of 75% of highest annual salary.
D-3	3.75	
D-4	1.50	
E-1	2.00	For each of the first 10 years of judicial service dropping to 1.5 for each subsequent year of judicial service.
E-2	1.50	For each year of judicial service.

NOTE: *There are conditions under which long-service members or members retiring at advanced ages may receive somewhat larger benefits than those described above. Further, benefit limitations exist for most members of SERS.*

Statistical Section

The Statistical Section of the Commonwealth of Pennsylvania State Employees' Retirement System's Comprehensive Annual Financial Report presents detailed information related to the financial statements, as well as highlights of actuarial valuations. The schedules within the Statistical Section are classified into the following four categories: Financial Trends, Revenue Capacity, Demographic and Economic Information, and Operating Information.

Financial Trends

The **Schedule of Trend Data** provides key financial, actuarial, and demographic data for ten years ending December 31, 2007. This data includes items such as employer and member contribution rates, contributions received by the System and benefits paid, fair value and actuarial value of assets, and the number of annuitants, beneficiaries, and active participants.

The **Schedule of Additions to Plan Net Assets** presents the member and employer contributions, as well as the net investment income / loss for the ten years ending December 31, 2007. The System's investment returns have the most significant impact on the additions to plan net assets.

The **Schedule of Deductions from Plan Net Assets** presents the benefits, refunds of contributions, and administrative expenses for the ten years ending December 31, 2007. The System's benefit payments have the most significant impact on the total deductions from plan net assets.

The **Schedule of Benefit and Refund Deductions from Net Assets by Type** presents the amount of benefit payments and refunds by type for the ten years ended December 31, 2007. Most benefit types are either superannuated or early which is determined by the number of years of service and / or age at retirement.

The **Schedule of Total Changes in Plan Net Assets** is a schedule combining the additions to and deductions from plan net assets from the Schedule of Additions to Plan Net Assets and Schedule of Deductions from Plan Net Assets to arrive at net increase / decrease of changes in plan net assets for the ten years ended December 31, 2007.

Revenue Capacity

The **Schedule of Investment Income** presents the details of the total net investment gain / loss for the ten years ended December 31, 2007. The System has two outside sources of revenue and one own-source (internal) of revenue. Employer contributions and member contributions, which information is provided for in the Schedule of Additions to Plan Net Assets and Schedule of Deductions from Plan Net Assets, are the two outside sources of revenue, and investment income is the System's own-source revenue. Since investment income is the largest source of revenue to the System, this schedule provides more detail on the major components of the investment income, which is also disclosed in total on the Schedule of Additions to Plan Net Assets.

Demographic and Economic Information

The **Schedule of Active Member Statistics** provides the total number of active members, as well as the average age, average service and average salary by gender.

Operating Information

The **Schedule of Retired Members by Type of Benefit** presents, for given benefit ranges, the total number of retirees, total monthly benefits and total number of retirees by retirement type as of December 31, 2007.

The **Schedule of Retired Members by Option** presents, for given benefit ranges, the total number of retirees, total monthly benefits and total number of retirees by retirement option as of December 31, 2007.

The **Schedule of Average Monthly Benefit Payments** presents, in five-year increments of credited service, the average monthly benefit, average final average salary and number of retired members for the ten years ended December 31, 2007.

The **Schedule of Average Annual Benefit Payments** presents, in five-year age increments and by gender, average annual benefit for each major retirement type as of December 31, 2007.

The **Schedule of SERS Agency Participation** provides the number of covered employees and the corresponding percentage of participation for the 20 largest employers for the ten years ended December 31, 2007, as well as a listing of additional employers participating with SERS as of December 31, 2007.

Sources: Unless otherwise noted, the information of these schedules is derived from the Financial Section and Actuarial Section of the Comprehensive Annual Financial Report for the relevant year.

Schedule of Trend Data[a.]
Ten Years Ended December 31, 2007

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Contribution Rates										
Employer [b.]	4.04%[e.]	4.02[d.]	3.02[d.]	2.03[d.]	1.07	0.00	0.00	1.39	5.00	6.70
Member	6.25%	6.25	6.25	6.25	6.25	6.25	5.00	5.00	5.00	5.00
Contributions:										
Employer	$243,936	196,420	148,375	106,703	68,604	50,831	76,710	168,002	270,718	310,501
Member	$333,818	317,790	305,624	309,923	308,014	304,233	240,528	231,666	224,928	221,618
Average Annual Compensation	$48,345	46,118	44,815	45,382	44,519	43,631	42,172	41,110	39,698	38,898
Market Value of Assets	$35,516,198	32,052,830	28,751,871	26,641,399	24,535,949	20,879,559	24,706,063	27,880,467	28,093,181	24,123,358
Actuarial Value of Assets	$30,839,877	28,148,834	26,793,782	26,900,027	27,465,615	27,497,464	27,505,494	26,094,306	23,624,267	20,670,711
Accrued Actuarial Liability	$31,753,971	30,364,997	28,851,716	27,999,026	26,179,761	25,650,389	23,658,757	19,702,278	19,091,840	18,357,899
Funded Ratio	97.1%	92.7	92.9	96.1	104.9	107.2	116.3	132.4	123.7	112.6
Total Benefits and Refunds	$2,336,368	1,919,426	1,943,643	1,859,255	1,632,281	1,430,417	1,245,129	1,176,785	1,229,348	1,062,155
Average Pension [c.]	$21,326	20,025	19,372	18,414	17,192	15,445	13,656	12,935	12,520	12,027
Annuitants and Beneficiaries	107,130	102,060	101,179	98,727	94,412	91,228	89,217	88,392	88,043	85,834
Active Participants	109,610	110,972	109,981	108,405	109,018	111,059	109,716	109,469	108,035	108,893

[a.] *All dollar amounts are in thousands, except Average Pension and Average Annual Compensation.*
[b.] *Employer rate represents total contributions as a percent of covered payroll as of 12/31.*
[c.] *Average pension amount represents average annual pension only for members who have reached superannuation through age or service credits.*
[d.] *Act 40 of 2003 established a minimum employer contribution rate of 2%, 3%, and 4% effective July 1, 2004, 2005 and 2006 respectively.*
[e.] *Act 2007-8 established a permanent minimum employer contribution rate floor of 4%.*

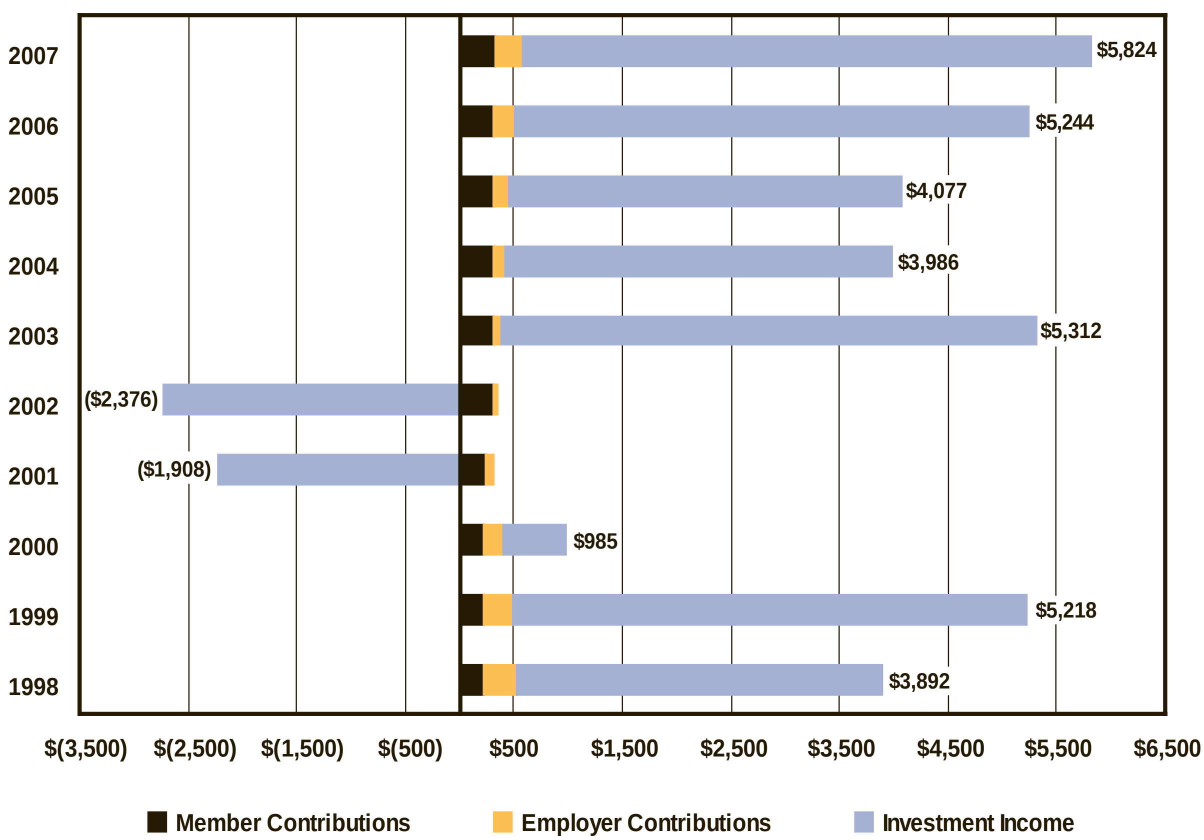
Source: State Employees' Retirement System

Schedule of Additions to Plan Net Assets
Ten Years Ended December 31, 2007
(Dollar Amounts in Thousands)

Year Ending	Member Contributions	Employer Contributions: Dollar Amount	Employer Contributions: % of Annual Covered Payroll	Net Investment Gain/(Loss)	Total
2007	$333,818	243,936	4.6%	$5,246,730	5,824,484
2006	317,790	196,420	3.8	4,730,043	5,244,253
2005	305,624	148,375	3.0	3,622,820	4,076,819
2004	309,923	106,703	2.2	3,569,323	3,985,949
2003	308,014	68,604	1.4	4,935,699	5,312,317
2002	304,233[a]	50,831	1.0	(2,731,295)	(2,376,231)
2001	240,528	76,710	1.7	(2,225,627)	(1,908,389)
2000	231,666	168,002	3.7	585,712	985,380
1999	224,928	270,718	6.3	4,722,671	5,218,317
1998	221,618	310,501	7.3	3,359,844	3,891,963

[a] *Effective January 1, 2002, most members' contributions increased to 6.25% from 5.00% of salary as a result of Act 9 of 2001.*

Additions to Plan Net Assets
(Dollar Amounts in Millions)



Source: State Employees' Retirement System

Schedule of Deductions From Plan Net Assets
Ten Years Ended December 31, 2007
(Dollar Amounts in Thousands)

Year	Benefits	Refund of Contributions	Administrative	Total
2007	$2,328,185 [e.]	8,183	24,748	2,361,116
2006	1,911,330	8,096	23,868	1,943,294
2005	1,936,428	7,215	22,704	1,966,347
2004	1,853,117	6,138	21,244	1,880,499
2003	1,627,166 [a.]	5,115	23,646	1,655,927
2002	1,426,257 [b.]	4,160	19,856	1,450,273
2001	1,237,953 [c.]	7,176 [d.]	20,887	1,266,016
2000	1,166,897	9,888	21,309	1,198,094
1999	1,218,133	11,215	19,146	1,248,494
1998	1,050,870	11,285	18,221	1,080,376

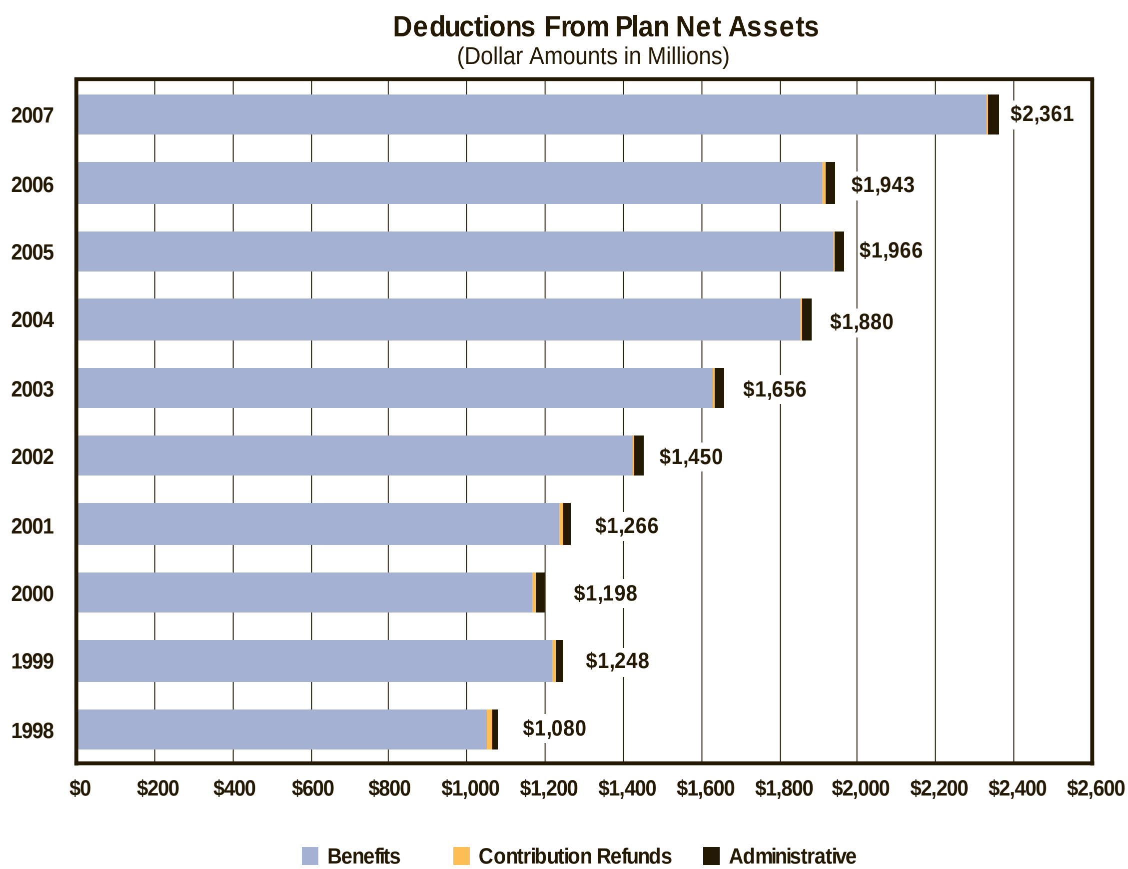
[a.] *Phase two of Cost of Living Adjustment (COLA) for members who retired between July 2, 1990 and July 1, 2002 became effective July 2, 2003.*

[b.] *Phase one of two-phase COLA for members who retired before July 2, 1990 became effective July 1, 2002.*

[c.] *For most members who retired after July 1, 2001, the benefit multiplier increased by 25% as a result of Act 9 of 2001.*

[d.] *Act 9 of 2001 also lowered the amount of years required to vest benefits from 10 years to 5 years.*

[e.] *22% increase from prior year is due to large number of employees retiring as a result of changes in health care benefits.*



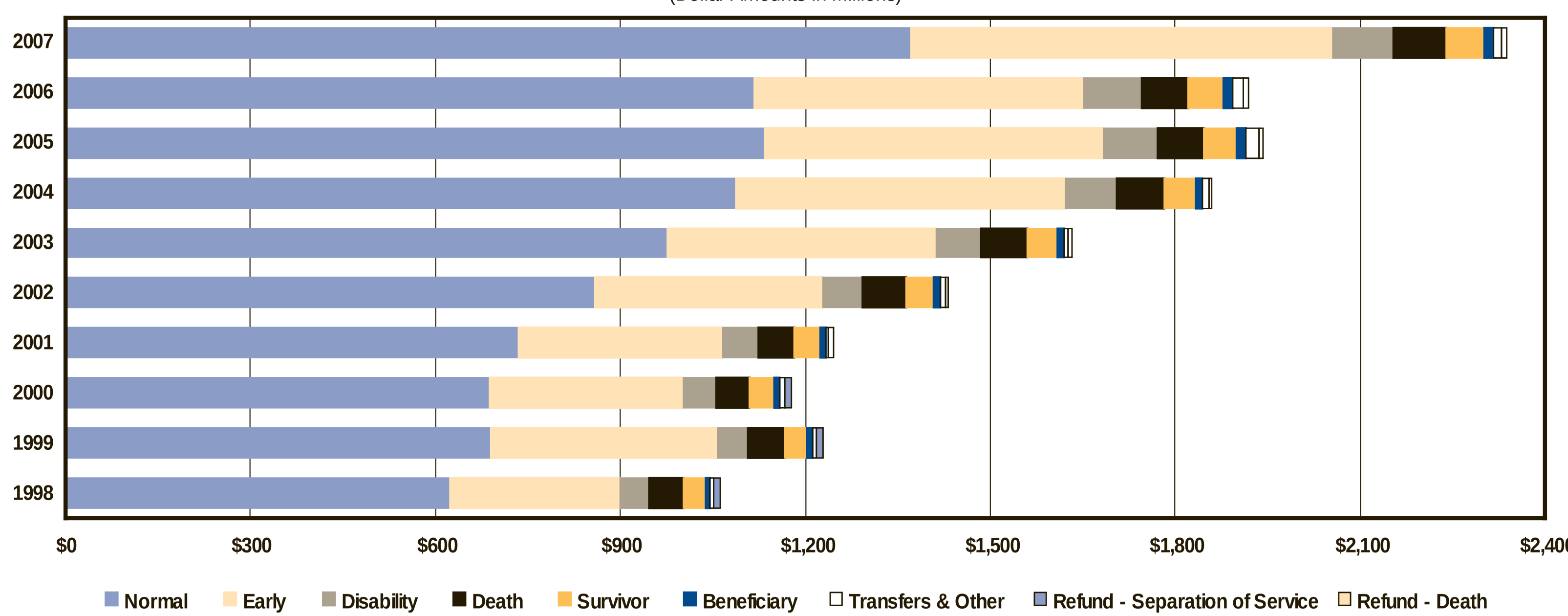
Source: State Employees' Retirement System

Schedule of Benefit and Refund Deductions From Plan Net Assets by Type
Ten Years Ended December 31, 2007
(Dollar Amounts in Thousands)

	Retirement								Refunds		
Year	Normal	Early	Disability	Death	Survivor	Beneficiary	Transfers & Other	Total Benefit Deductions	Separation of Service	Death	Total Refunds
2007	$1,372,909	683,467	98,605	83,687	62,726	13,949	12,842	2,328,185 [a]	8,007	176	8,183
2006	1,117,801	535,156	93,358	73,885	58,038	14,988	18,104	1,911,330	7,971	125	8,096
2005	1,133,694	550,437	88,250	74,312	53,873	14,650	21,212	1,936,428	7,086	129	7,215
2004	1,088,129	534,674	82,515	76,216	51,946	10,818	8,819	1,853,117	6,013	125	6,138
2003	976,102	436,325	72,880	75,368	48,687	9,876	7,928	1,627,166	4,994	121	5,115
2002	859,078	368,778	64,789	70,703	45,439	8,902	8,568	1,426,257	4,024	136	4,160
2001	735,919	331,445	57,254	57,744	42,689	8,115	4,787	1,237,953	6,753	423	7,176
2000	688,410	314,014	54,112	53,785	40,037	7,948	8,591	1,166,897	9,548	340	9,888
1999	690,840	366,515	50,496	58,675	36,830	7,283	7,494	1,218,133	10,788	427	11,215
1998	623,980	276,428	45,691	57,465	34,681	7,527	5,098	1,050,870	11,034	251	11,285

[a] *For most members who retired after July 1, 2007, member must contribute to medical insurance premiums as a result of AFSCME agreement dated July 1, 2007.*

Benefit and Refund Deductions From Plan Net Assets by Type
(Dollar Amounts in Millions)



Source: State Employees' Retirement System

Schedule of Total Changes in Plan Net Assets
Ten Years Ended December 31, 2007
(Dollar Amounts in Thousands)

	Additions to Plan Net Assets				Deductions from Plan Net Assets				
Year Ending	Member Contributions	Employer Contributions	Net Investment Income	Total Additions	Benefits	Refund of Contributions	Administrative	Total Deductions	Net Increase / (Decrease)
2007	$333,818	243,936	5,246,730	**5,824,484**	2,328,185	8,183	24,748	**2,361,116**	**3,463,368**
2006	317,790	196,420	4,730,043	**5,244,253**	1,911,330	8,096	23,868	**1,943,294**	**3,300,959**
2005	305,624	148,375	3,622,820	**4,076,819**	1,936,428	7,215	22,704	**1,966,347**	**2,110,472**
2004	309,923	106,703	3,569,323	**3,985,949**	1,853,117	6,138	21,244	**1,880,499**	**2,105,450**
2003	308,014	68,604	4,935,699	**5,312,317**	1,627,166	5,115	23,646	**1,655,927**	**3,656,390**
2002	304,233	50,831	(2,731,295)	**(2,376,231)**	1,426,257	4,160	19,856	**1,450,273**	**(3,826,504)**
2001	240,528	76,710	(2,225,627)	**(1,908,389)**	1,237,953	7,176	20,887	**1,266,016**	**(3,174,405)**
2000	231,667	168,002	585,712	**985,381**	1,166,897	9,888	21,309	**1,198,094**	**(212,713)**
1999	224,928	270,718	4,722,671	**5,218,317**	1,218,133	11,215	19,146	**1,248,494**	**3,969,823**
1998	221,618	310,501	3,359,844	**3,891,963**	1,050,870	11,285	18,221	**1,080,376**	**2,811,587**

Source: State Employees' Retirement System

Schedule of Investment Income
Ten Years Ended December 31, 2007
(Dollar Amounts in Thousands)

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Investment gain/(loss):										
Net appreciation/(depreciation) in fair value of investments	$4,164,231	3,723,160	2,811,470	2,807,290	3,423,081	(1,915,634)	(1,790,575)	774,998	2,676,745	1,212,355
Collective trust fund appreciation/(depreciation) and income	798,941	641,718	420,888	391,248	1,165,463	(1,310,044)	(1,014,578)	(825,600)	1,453,724	1,568,761
Interest	347,507	350,783	368,610	280,221	237,786	303,421	388,626	412,933	371,062	357,708
Dividends	149,488	152,690	128,480	124,099	113,634	112,015	106,253	113,293	127,330	118,502
Real estate	112,148	145,871	112,057	148,133	168,427	193,719	182,423	203,308	164,893	153,611
Miscellaneous	6,149	3,519	3,537	6,722	7,138	30,035	41,111	37,377	35,981	25,954
	5,578,464	5,017,741	3,845,042	3,757,713	5,115,529	(2,586,488)	(2,086,740)	716,309	4,829,735	3,436,891
Investment expenses	(344,707)	(298,204)	(234,760)	(196,859)	(187,139)	(153,211)	(148,778)	(140,526)	(115,538)	(82,369)
Net gain/(loss) from investing activities	5,233,757	4,719,537	3,610,282	3,560,854	4,928,390	(2,739,699)	(2,235,518)	575,783	4,714,197	3,354,522
From securities lending activities:										
Securities lending income	155,067	170,675	116,477	40,854	16,163	26,696	54,813	87,874	54,530	71,736
Securities lending expenses	(142,094)	(160,169)	(103,939)	(32,385)	(8,854)	(18,292)	(44,922)	(77,945)	(46,056)	(66,414)
Net income from securities lending activities	12,973	10,506	12,538	8,469	7,309	8,404	9,891	9,929	8,474	5,322
Total net investment gain/(loss)	**$5,246,730**	**4,730,043**	**3,622,820**	**3,569,323**	**4,935,699**	**(2,731,295)**	**(2,225,627)**	**585,712**	**4,722,671**	**3,359,844**

Source: State Employees' Retirement System

Schedule of Active Member Statistics
Ten Years Ended December 31, 2007

	Male			Female			Total Number of Active Members
	Average Age	Average Service	Average Salary	Average Age	Average Service	Average Salary	
2007	46.11	12.22	$51,663	45.95	11.76	$43,888	109,610
2006	46.39	12.80	49,455	46.20	12.49	41,616	110,972
2005	46.12	12.71	48,129	45.91	12.46	40,331	109,981
2004	46.14	13.03	48,801	46.01	12.88	40,716	108,405
2003	46.25	13.42	47,717	46.12	13.39	40,120	109,018
2002	46.16	13.55	46,857	45.98	13.48	39,198	111,059
2001	46.08	13.68	45,386	45.88	13.65	37,737	109,716
2000	45.86	13.53	44,316	45.70	13.65	36,630	109,469
1999	45.55	13.38	42,799	45.41	13.54	35,374	108,035
1998	45.42	13.42	41,853	45.28	13.56	34,757	108,893

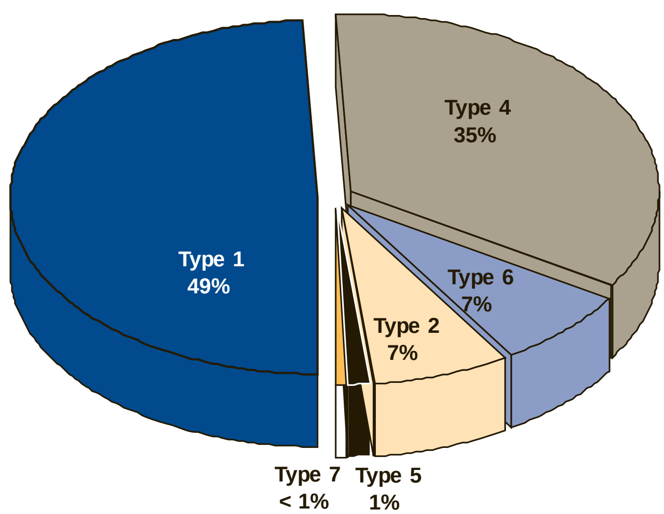
Source: State Employees' Retirement System

Schedule of Retired Members by Type of Benefit
As of December 31, 2007

Amount of Monthly Benefit	Total Monthly Benefits	Total Number of Retirees	Type of Retirement					
			1	2	4	5	6	7
$1 to 500	$7,238,962	28,828	7,798	724	15,437	573	4,035	261
> 500 to 1,000	17,477,247	23,768	12,447	3,751	5,036	287	2,045	202
> 1,000 to 1,500	19,558,143	15,865	8,960	1,551	4,301	120	831	102
> 1,500 to 2,000	19,393,255	11,149	5,945	751	4,014	44	353	42
> 2,000 to 2,500	18,495,309	8,268	4,612	353	3,039	29	224	11
> 2,500 to 3,000	15,705,654	5,736	3,448	203	1,967	25	90	3
> 3,000	56,104,914	13,516	9,531	155	3,634	42	150	4
Totals	**$153,973,484**	**107,130**	**52,741**	**7,488**	**37,428**	**1,120**	**7,728**	**625**

Type of Retirement
1 - Superannuation
2 - Disabled
4 - Early
5 - Beneficiary
6 - Survivor
7 - Alternate Payee

Retired Members by Type of Benefit



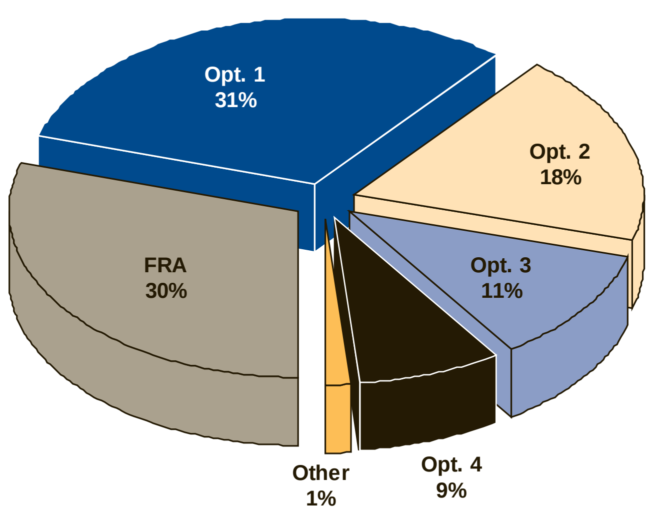
Source: State Employees' Retirement System

Schedule of Retired Members by Option
As of December 31, 2007

			Option Selected					
Amount of Monthly Benefit	Total Monthly Benefits	Total Number of Retirees	FRA	1	2	3	4	Other
$1 to 500	$7,238,962	28,828	6,960	11,323	6,515	2,419	1,004	607
> 500 to 1,000	17,477,247	23,768	8,017	7,161	4,400	2,340	1,519	331
> 1,000 to 1,500	19,558,143	15,865	4,632	4,717	3,002	1,761	1,607	146
> 1,500 to 2,000	19,393,255	11,149	3,305	3,123	1,864	1,442	1,353	62
> 2,000 to 2,500	18,495,309	8,268	2,381	2,149	1,328	1,163	1,212	35
> 2,500 to 3,000	15,705,654	5,736	1,731	1,402	874	822	875	32
> 3,000	56,104,914	13,516	4,590	2,944	1,567	2,021	2,344	50
Totals	**$153,973,484**	**107,130**	**31,616**	**32,819**	**19,550**	**11,968**	**9,914**	**1,263**

Options
FRA - Full Retirement Allowance
Opt. 1 - Annuity for Life with beneficiary receiving remainder of Present Value when member dies
Opt. 2 - Annuity for Life with beneficiary receiving same annuity when member dies
Opt. 3 - Annuity for Life with beneficiary receiving one half the members annuity amount when member dies
Opt. 4 - Member designs a different plan approved by SERS not covered under the above option
Other - Death Benefit and Domestic Relation Order

Retired Members by Option



Source: State Employees' Retirement System

Schedule of Average Monthly Benefit Payments[a.]
Ten Years Ended December 31, 2007

	Years Credited Service						
Retirement Effective Dates	**< 5**	**5-9**	**10-14**	**15-19**	**20-24**	**25-29**	**30+**
Period 1/1/2007 to 12/31/2007							
Average monthly benefit	$219	322	674	1,214	1,883	2,538	3,464
Average final average salary	$31,359	37,629	42,759	45,817	53,241	58,974	60,726
Number of retired members	53	637	476	1,057	759	1,258	3,384
Period 1/1/2006 to 12/31/2006							
Average monthly benefit	$174	316	690	1,171	1,878	2,487	3,489
Average final average salary	$27,898	35,283	42,358	45,225	53,513	58,031	60,582
Number of retired members	51	584	491	667	471	627	1,205
Period 1/1/2005 to 12/31/2005							
Average monthly benefit	$197	335	695	1,161	1,844	2,409	3,464
Average final average salary	$31,822	34,767	40,577	45,052	51,985	55,391	60,758
Number of retired members	57	579	544	785	588	885	2,034
Period 1/1/2004 to 12/31/2004							
Average monthly benefit	$170	355	674	1,171	1,820	2,255	3,230
Average final average salary	$26,332	34,645	39,343	44,095	49,960	53,306	56,940
Number of retired members	53	550	558	878	686	1,130	3,100
Period 1/1/2003 to 12/31/2003							
Average monthly benefit	$201	370	661	1,126	1,721	2,201	3,179
Average final average salary	$30,920	34,935	37,342	41,727	47,340	51,372	55,947
Number of retired members	33	514	538	851	701	984	2,633
Period 1/1/2002 to 12/31/2002							
Average monthly benefit	$201	355	631	1,073	1,683	2,150	3,264
Average final average salary	$25,626	33,588	37,370	41,421	45,974	49,743	56,880
Number of retired members	29	492	525	627	615	799	1,826
Period 1/1/2001 to 12/31/2001							
Average monthly benefit	$166	413	542	967	1,445	1,874	2,959
Average final average salary	$27,851	32,700	35,821	40,773	43,815	47,066	55,470
Number of retired members	25	399	476	594	536	805	1,332
Period 1/1/2000 to 12/31/2000							
Average monthly benefit	$160	469	448	771	1,205	1,645	2,487
Average final average salary	$28,373	31,567	35,508	39,153	41,765	45,709	53,923
Number of retired members	33	252	639	594	458	712	678
Period 1/1/1999 to 12/31/1999							
Average monthly benefit	$149	453	425	798	1,132	1,567	2,235
Average final average salary	$27,246	29,670	34,691	38,970	40,447	43,931	49,742
Number of retired members	55	268	618	613	517	776	2,140
Period 1/1/1998 to 12/31/1998							
Average monthly benefit	$124	424	423	762	1,110	1,690	2,410
Average final average salary	$24,114	28,296	34,841	37,288	39,524	44,937	51,200
Number of retired members	44	271	621	587	476	791	914

[a.] *Includes Normal Retirement, Early Retirement and Disability Benefits for new retirees in the years listed.*

Source: State Employees' Retirement System

Schedule of Average Annual Benefit Payments
As of December 31, 2007

	Superannuation		Early Retirement		Disability		Beneficiary and Survivor	
Age	**Male**	**Female**	**Male**	**Female**	**Male**	**Female**	**Male**	**Female**
Under 25	-	-	-	363	-	-	10,567	8,078
25-29	-	-	637	568	-	8,748	9,259	16,326
30-34	-	-	951	864	10,220	10,950	15,909	8,870
35-39	-	-	2,002	1,684	12,582	10,758	13,476	9,868
40-44	-	-	4,468	2,284	13,569	10,454	5,542	10,050
45-49	-	-	11,236	4,651	15,611	14,095	7,992	8,720
50-54	$34,109	31,281	14,513	10,781	16,735	15,116	6,057	8,659
55-59	36,424	36,159	20,091	14,630	16,403	14,928	6,919	10,915
60-64	34,628	26,544	22,649	15,629	13,809	13,448	10,571	12,695
65-69	29,003	20,492	16,984	11,820	10,893	9,882	7,992	11,938
70-74	23,258	15,707	14,146	9,225	9,201	8,763	7,862	10,430
75-79	19,757	11,948	14,395	9,202	9,852	7,575	8,186	9,072
80-84	16,544	10,264	12,553	7,762	9,556	7,057	6,382	7,701
85-89	13,770	8,571	12,306	8,003	8,907	6,498	5,638	6,216
90 and over	12,209	8,012	11,247	9,139	11,260	6,939	4,129	5,452
Total Average	**$24,994**	**16,434**	**17,375**	**11,519**	**13,718**	**12,387**	**7,844**	**8,742**

	Superannuation	Early Retirement	Disability	Beneficiary and Survivor
Average Pension	$21,326	14,563	13,026	8,654
Average Age Male & Female	72.8	61.4	60.5	75.0

Source: State Employees' Retirement System

Schedule of SERS Agency Participation - Twenty Largest Employers
Ten Years Ended December 31, 2007

\# - Number of Active Employees
% - Percentage of Total Active Members

	2007		2006		2005		2004		2003		2002		2001		2000		1999		1998	
Employer Name	#	%	#	%	#	%	#	%	#	%	#	%	#	%	#	%	#	%	#	%
Dept of Public Welfare	18,761	17.12	19,355	17.44	19,781	17.99	20,175	18.61	20,417	18.73	21,242	19.13	21,507	19.60	21,766	19.88	22,290	20.63	23,378	21.47
Dept of Corrections	15,523	14.16	15,151	13.65	15,126	13.75	14,463	13.34	14,267	13.09	14,839	13.36	14,416	13.14	14,123	12.90	13,284	12.30	12,765	11.72
Dept of Transportation	12,264	11.19	12,484	11.25	12,388	11.26	12,428	11.46	12,603	11.56	12,768	11.50	12,623	11.51	12,748	11.65	12,590	11.65	12,556	11.53
Pennsylvania State Police	6,266	5.72	6,172	5.56	6,127	5.57	5,885	5.43	5,803	5.32	5,807	5.23	5,650	5.15	5,632	5.14	5,597	5.18	5,406	4.96
Pennsylvania State University	6,210	5.67	6,265	5.65	6,210	5.65	6,085	5.61	6,102	5.60	6,071	5.47	6,099	5.56	6,117	5.59	6,174	5.71	6,408	5.88
State System of Higher Education	5,316	4.85	5,344	4.82	5,240	4.76	5,248	4.84	5,432	4.98	5,565	5.01	5,697	5.19	5,897	5.39	5,989	5.54	6,331	5.81
Dept of Labor and Industry	5,234	4.78	5,692	5.13	5,608	5.10	5,648	5.21	5,823	5.34	5,938	5.35	5,416	4.94	5,467	4.99	5,624	5.21	5,762	5.29
Liquor Control Board	3,969	3.62	4,102	3.70	3,994	3.63	3,840	3.54	3,686	3.38	3,672	3.31	3,523	3.21	3,576	3.27	3,463	3.21	3,421	3.14
Dept of Environmental Protection	2,767	2.52	2,921	2.63	2,836	2.58	2,854	2.63	2,916	2.67	2,973	2.68	3,016	2.75	3,004	2.74	2,922	2.70	2,896	2.66
Dept of Military and Veterans Affairs	2,545	2.32	2,540	2.29	2,492	2.27	2,402	2.22	2,291	2.10	2,220	2.00	2,127	1.94	2,057	1.88	1,919	1.78	1,846	1.70
PA Higher Education Assistance Agency	2,494	2.28	2,524	2.27	2,378	2.16	1,968	1.82	1,957	1.80	1,908	1.72	1,811	1.65	1,544	1.41	1,482	1.37	1,303	1.20
Dept of Revenue	2,289	2.09	2,319	2.09	2,322	2.11	2,238	2.06	2,312	2.12	2,462	2.22	2,493	2.27	2,431	2.22	2,326	2.15	2,301	2.11
PA Turnpike Commission	2,232	2.04	2,276	2.05	2,227	2.02	2,282	2.11	2,354	2.16	2,330	2.10	2,404	2.19	2,406	2.20	2,228	2.06	2,316	2.13
Executive Offices	2,201	2.01	2,247	2.02	2,246	2.04	2,237	2.06	2,351	2.16	2,349	2.12	2,374	2.16	2,335	2.13	2,233	2.07	2,194	2.01
Dept of Conservation & Natural Resources	2,080	1.90	2,093	1.89	1,971	1.79	1,927	1.78	2,009	1.84	2,079	1.87	2,045	1.86	2,019	1.84	1,748	1.62	1,658	1.52
Administrative Office of PA Courts	1,988	1.81	1,989	1.79	1,953	1.78	1,957	1.81	1,884	1.73	1,883	1.70	1,834	1.67	1,836	1.68	1,621	1.50	1,630	1.50
House of Representatives	1,758	1.60	1,701	1.53	1,706	1.55	1,662	1.53	1,619	1.49	1,568	1.41	1,544	1.41	1,496	1.37	1,493	1.38	1,474	1.35
Dept of Health	1,433	1.31	1,479	1.33	1,435	1.30	1,386	1.28	1,393	1.28	1,378	1.24	1,330	1.21	1,271	1.16	1,213	1.12	1,216	1.12
Dept of General Services	1,267	1.16	1,340	1.21	1,306	1.19	1,230	1.13	1,281	1.18	1,357	1.22	1,350	1.23	1,333	1.22	1,270	1.18	1,261	1.16
Board of Probation and Parole	1,009	0.92	974	0.88	1,010	0.92	998	0.92	986	0.90	989	0.89	944	0.86	940	0.86	913	0.85	892	0.82
Active Employees for Twenty Largest Employers	**97,606**	**89.05**	**98,968**	**89.18**	**98,356**	**89.43**	**96,913**	**89.40**	**97,486**	**89.42**	**99,398**	**89.50**	**98,203**	**89.51**	**97,998**	**89.52**	**96,379**	**89.21**	**97,014**	**89.09**
Total Number of Active Employees	109,610		110,972		109,981		108,405		109,018		111,059		109,716		109,469		108,035		108,893	

Source: State Employees' Retirement System

Bloomsburg University Community Activities
Bucks County Community College
Bucks County Health Department
Bucks County Intermediate Unit
California University Student Association
Capitol Preservation Committee
Center for Rural Pennsylvania
Central Susquehanna Intermediate Unit
Chester County Health Department
Civil Service Commission
Clarion University Student Association
Community College of Allegheny County
Community College of Philadelphia
Delaware County Community College
Delaware River Joint Toll Bridge
Delaware River Port Authority
Delaware Valley Regional Planning Commission
Department of Aging
Department of Agriculture
Department of Banking
Department of Community & Economic Development
Department of Education
Department of State
Department of the Auditor General
East Stroudsburg University Student Association
Edinboro University Services Inc.
Environmental Hearing Board
Erie County Health Department
Fish and Boat Commission
Game Commission
Governor's Office
Harrisburg Area Community College
Historical and Museum Commission
House Appropriations Committee(D)
House Appropriations Committee(R)
Independent Regulatory Review Commission
Indiana University Student Co-op
Insurance Department
Intergovernmental Cooperation Authority
Joint Legislative Conservation Committee
Joint State Government Commission
Kutztown University Student Services
Lancaster-Lebanon Intermediate Unit
Legislative Budget & Finance Committee
Legislative Data Processing Center
Legislative Reference Bureau
Lehigh Carbon Community College
Lieutenant Governor's Office
Local Government Commission
Lock Haven University Student Co-op
Luzerne County Community College
Luzerne Intermediate Unit
Mansfield University Community Services
Milk Marketing Board
Millersville Student Services
Montgomery County Community College
Northampton Community College
Office of Attorney General
Office of Liquidations
Pennsylvania College of Technology
Pennsylvania Convention Center Authority
Pennsylvania Emergency Management Agency
Pennsylvania Gaming Control Board
Pennsylvania Health Care Cost Containment Council
Pennsylvania Highlands Community College
Pennsylvania Housing Finance Agency
Pennsylvania Infrastructure Investment Authority
Pennsylvania Municipal Retirement System
Pennsylvania Port Authority
Pennsylvania Public Television Network Commission
Port Authority Transit Corporation
Public School Employees' Retirement System
Public Utility Commission
Reading Area Community College
Securities Commission
Senate of Pennsylvania
Shippensburg Student Association
Slippery Rock Student Government
State Employees' Retirement System
State Ethics Commission
State Public School Building Authority
State Tax Equalization Board
Susquehanna River Basin Commission
Thaddeus Stevens College of Technology
Treasury Department
U.S. Property & Fiscal Office for Pennsylvania
West Chester University Student Services
Westmoreland County Community College

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