

# 2012 Supplemental Budget Information

Prepared for the House Appropriations Committee





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Chairman

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February 8, 2012

The Honorable William F. Adolph Jr.  
Chairman, Appropriations Committee  
Pennsylvania House of Representatives  
245 Main Capitol Building  
Harrisburg, PA 17120-2165

The Honorable Joseph F. Markosek  
Democratic Chairman, Appropriations Committee  
Pennsylvania House of Representatives  
512E Main Capitol Building  
Harrisburg, PA 17120-2025

Gentlemen and Members of the Appropriations Committee:

On behalf of the State Employee's Retirement System (SERS), I am pleased to share this detailed information about SERS' operations, investments and appropriations request. I trust that this data will be useful in your careful deliberation of the Commonwealth's FY 2012/13 budget.

In reviewing and transmitting this information, I am proud of the men and women who work so hard every day to serve Pennsylvania's public employees by administering their retirement benefit. Every person who works at SERS understands that our vigilant stewardship of employee and taxpayer dollars ultimately provides financial security for more than one hundred thousand Commonwealth retirees – our communities' volunteers, our neighbors, our friends, our parents.

The "looming pension crisis" has once again been the subject of extensive media coverage over the past year. Rather than rely on press or academic reports that paint this important issue with a broad brush, I call your attention to some facts – some favorable, some less so – associated specifically with our plan:

- Far from the media hype of "bloated" or "exorbitant" public pensions, the average SERS pension for someone who worked to full retirement age is about \$24,000 per year. And only about half of SERS retirees work to full retirement age. Those who retire early, retire as a result of a disability, or survive a retiree receive considerably less, between \$10,000 and \$16,000 per year.
- Pennsylvania enacted significant state pension reform in 2010. As a result of Act 2010-120, the Commonwealth's pension costs were cut approximately in half. It now costs just 4% of payroll to provide retirement benefits to SERS-covered employees hired on or after January 1, 2011.
- Most employees contribute 6.25% of their own paychecks toward their state retirement.
- As of December 31, 2011 the market value of the SERS Fund (Fund) was \$24.2 billion. Despite this year's economic turbulence, the Fund achieved an estimated return of 2.6%, which places it in the top 80% of similarly situated public pension funds. Nonetheless, the Fund is \$1.7 billion less than it was at this time in 2010.
- The system has more retired members than active members and is paying out approximately \$166 million more each month than it is taking in from employer and employee contributions. SERS' increasing maturity raises the liquidity needs of the Fund and will require that assets be rebalanced.
- For a variety of reasons – employer contributions below normal costs, losses that neutralized investment gains used to justify lower employer contributions, benefit increases without corresponding funding, changes to extend time to pay down liabilities – SERS has an unfunded liability of about \$12.5 billion, which is a debt that has already been incurred and is owed to current and retired employees.

- Act 2010-120 allows for employer contributions to increase at predictable, measured intervals over time: 8.0% in FY 2011, 11.5% in FY 2012, and increases of not more than 4.5% each fiscal year thereafter. Such contributions, however, remain below the actuarial annual contribution rate until at least 2015 and result in an ongoing deficit.
- When the General Assembly meets the increases scheduled in Act 2010-120 and as the Fund continues to achieve its assumed rate of return over time, SERS will again approach full funding in roughly 30 years. Given the current fiscal climate, honoring the commitment and meeting return assumptions may very well be difficult, however, they are essential.

In referencing the current fiscal climate, I would be remiss if I neglected to spotlight the Fund's importance to the Commonwealth's economy. Tab 10 of this book details the roughly \$960 million in Pennsylvania-based investments which clearly align with SERS' fiduciary obligation to its members.

And, of course, we know that pension payments are a primary source of income, safety and stability for the more than 115,000 people who receive SERS checks each month. Studies suggest that a single taxpayer dollar – when augmented by the employee's own contributions and the overwhelming power of the billions in SERS investment earnings over decades – generates significant economic activity.

The 107 participating SERS employers paid \$399 million to the system in 2011 while the system paid \$2.4 billion in payments to Pennsylvania-based retirees. These payments directly stimulate economic activity in communities throughout Pennsylvania. According to the National Institute on Retirement Security, the Commonwealth's real estate, finance, insurance, retail and health care sectors are particularly influenced by retiree spending.

The information in this book provides a great deal of detail on SERS' operations and investments. I, along with Acting Executive Director, David Durbin, and Chief Investment Officer, Anthony Clark, am prepared to answer any questions you may have during our February 23 hearing. If you have questions, comments, or concerns before then – or if there's any issue you would like to be sure we are fully prepared to discuss with specificity – please contact Mr. Durbin at (717) 787-9657.

Thank you for your time and consideration. You have extremely challenging work ahead of you; if there is any way SERS or its professionals can help you, please don't hesitate to call.

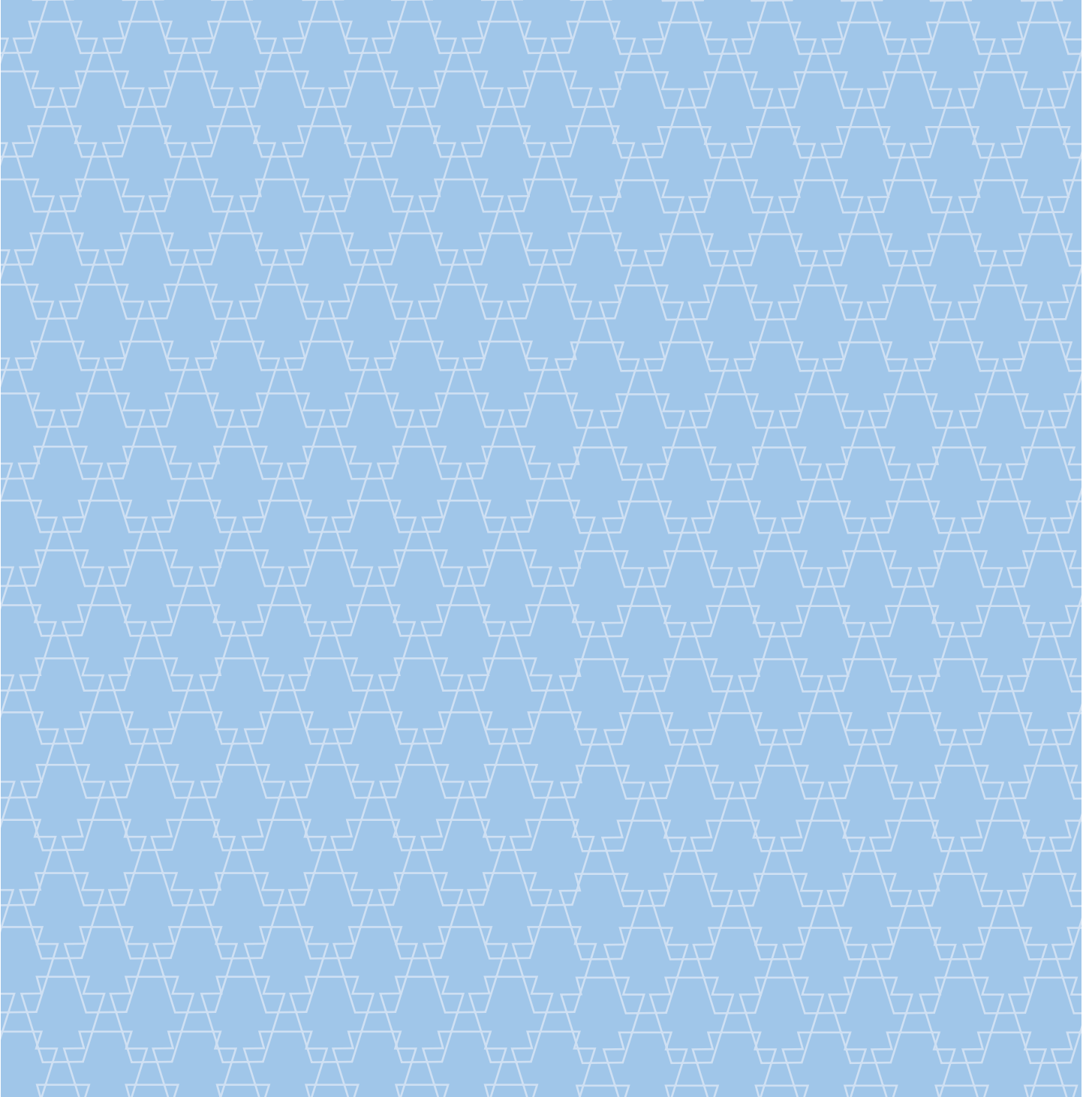
Sincerely,



Nicholas J. Maiale  
Chairman

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# Mission, Vision & Guiding Principles

Established in 1923, SERS is one of the nation's oldest and largest statewide retirement plans for public employees, with more than 227,000 members. SERS is among the largest of public and corporate pension funds, with assets of approximately \$24.2 billion as of December 31, 2011.

SERS is responsible for administering the State Employees' Retirement Code in accordance with the expressed intent of the General Assembly and bears a fiduciary obligation to the state employees and retirees who are the plan beneficiaries.

State law provides that the administration of the SERS Fund and the fiduciary responsibility for its management be vested in an 11-member Board. The management of SERS is the responsibility of the Executive Director who, with the approval of the Board, contracts for professional services and employs the staff needed to operate the System.

## **Mission**

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

## **Vision**

To navigate the fiscal storm in such a way that SERS emerges with a positive cash flow and enhanced member services.

## **Guiding Principles**

- Demonstrate Integrity
- Think Strategically
- Lead Innovation and Improvement
- Develop and Empower Employees
- Share Knowledge
- Focus on Customer Service
- Learn from Mistakes
- Safeguard Information, Facilities and Staff
- Fulfill Fiduciary Obligations

# Organization & Operations

The agency's various program functions are administered by staff in SERS' Harrisburg Central Office and through a statewide network of seven Regional Retirement Counseling Centers. Assignment of major agency functions is as follows:

**Executive Office:** Supports the Executive Director who is the agency's senior staff administrator. Provides direct service to the Chairman of the Board and Board members. Makes arrangements for and conducts administrative functions for all Board meetings. Conducts research and provides agency direction on organizational development, strategic planning, pending retirement issues and actuarial considerations. Includes the Communications and Policy Office, which serves a variety of support functions related to communications and legislation. These include preparation and dissemination of retirement-related information and publications, tracking and reporting on retirement legislation, serving as the agency's legislative liaison and handling inquiries from the media, state Legislature and the public.

**Office of Member Services:** Provides individualized counseling and retirement-related seminars through SERS' statewide system of seven Regional Retirement Counseling Centers. Processes member and member-survivor benefit payments and provides membership account services. Researches issues in public pension programs, recommends adoption of new strategies, and performs special retirement-related functions.

**Investment Office:** Works closely with the Board to recommend and establish asset allocation, investment policy and investment managers for review and approval by the Board. The office works in tandem with the consultants monitoring the compliance and performance of the outside managers and undertaking research on investment products and investment managers.

**Office of Finance and Administration:** Provides the accounting structure for SERS' \$24.2 billion Fund; oversees all transactions, including payment of member benefits, purchase and sale of investment securities, receipt of employer and employee contributions and investment income, and administration of the agency operational budget. The office also manages agency operations and disaster recovery planning, while reporting to the Board on management of the approximately \$2.2 billion Commonwealth Deferred Compensation Program.

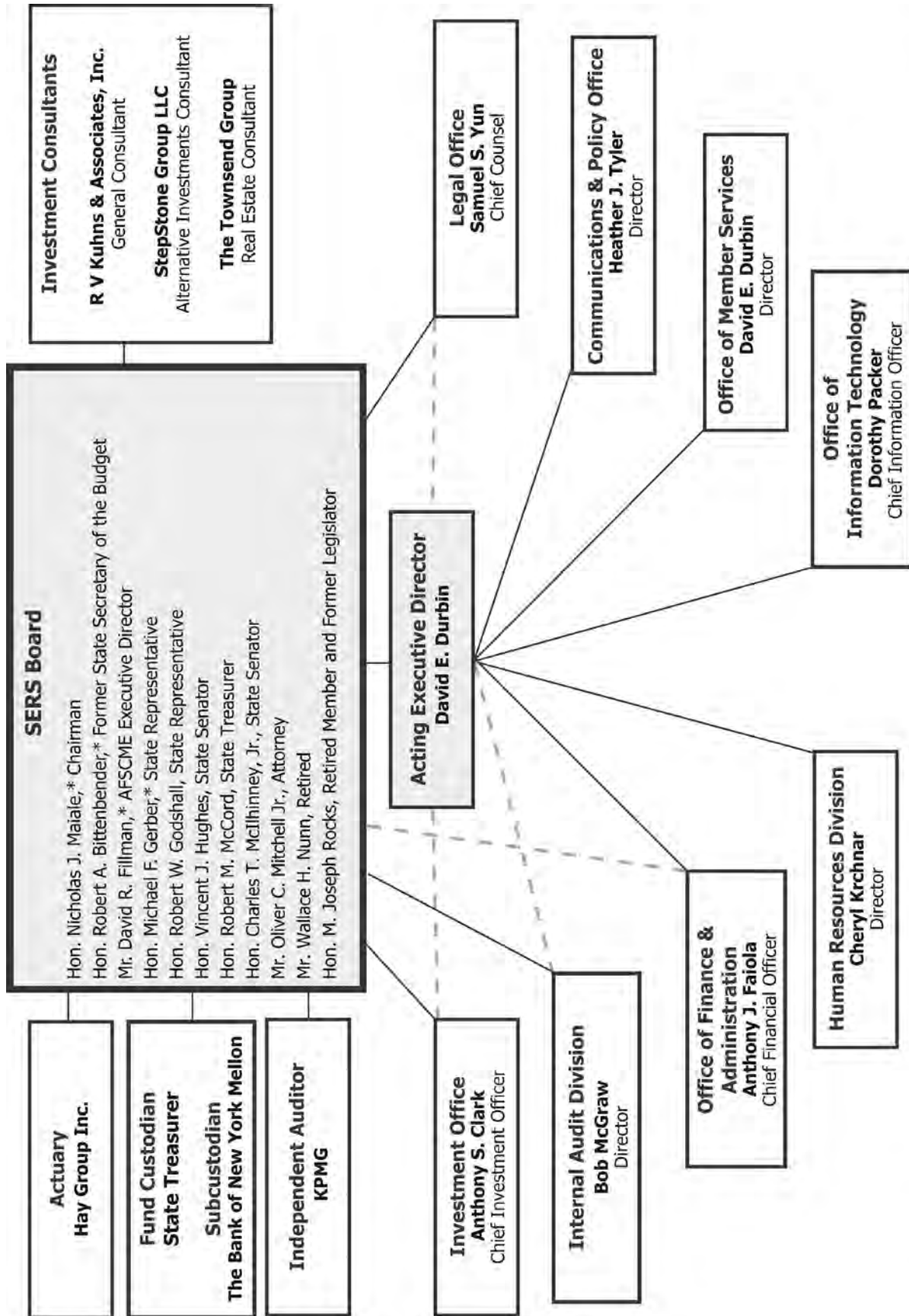
**Legal Office:** Provides counsel to the Board and the agency, including handling administrative hearings involving SERS members, reviewing investment and non-investment-related contracts, and providing legal advice.

**Office of Information Technology:** Provides all computer and technical support for SERS operations, including a Wide Area Network linking the agency's seven Regional Retirement Counseling Centers.

**Internal Audit Division:** Provides the Board with the assurance that internal controls are adequate and operating as designed through internal audits of business processes. Coordinates audits performed at SERS by external agencies and auditors.

**Human Resources Division:** Implements programs and provides direction for all aspects of organizational change and employee needs including, but not limited to, recruitment, classification, compensation, staff development, workforce planning, and labor relations.

# SERS Organizational Chart



01-26-12

\* Audit Committee Member





**2012-2013 Budget - Board Submission 2**

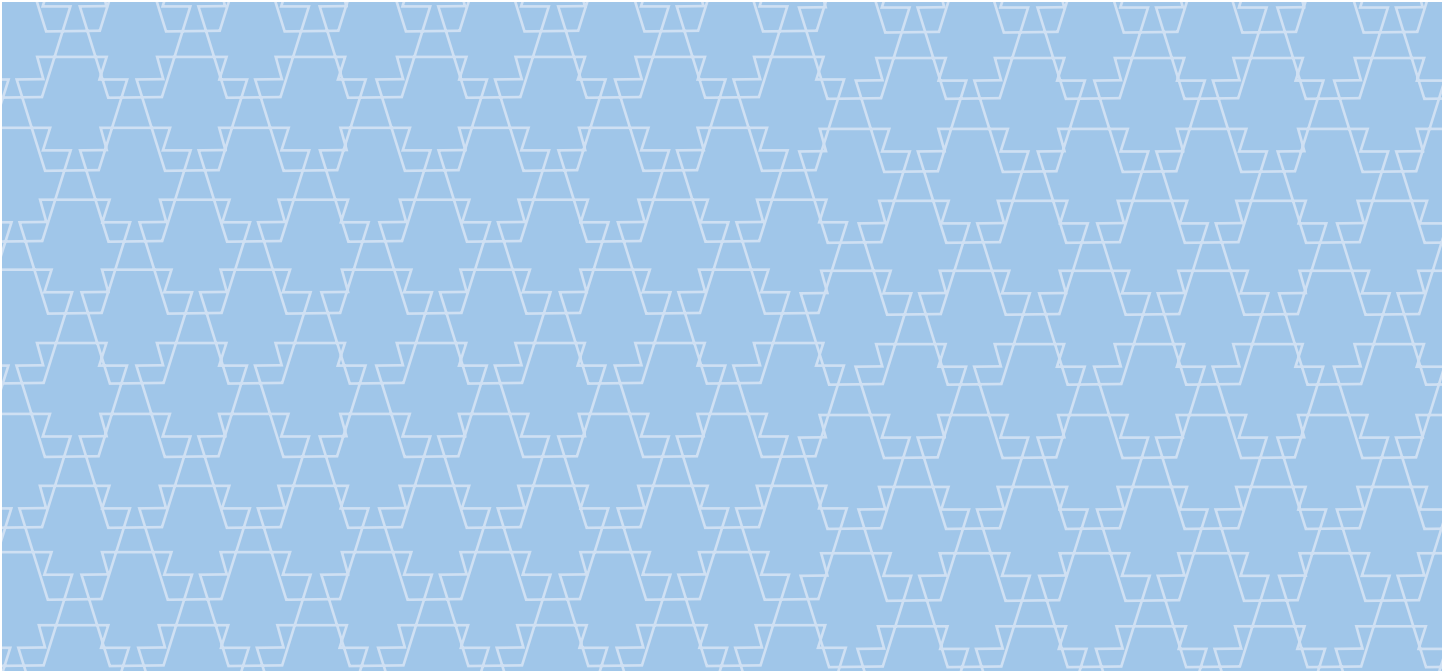


# SERS Budget 2012-2013

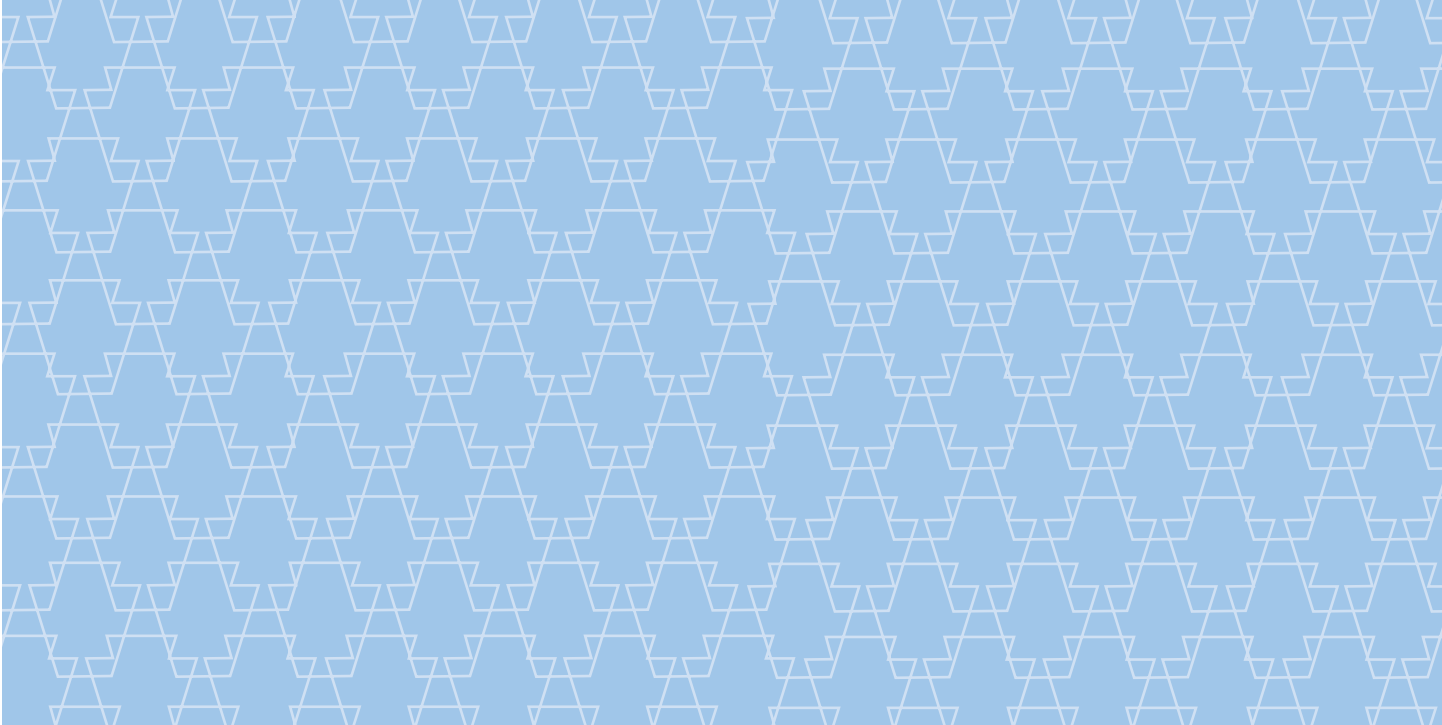
	Rebudget 2008-09	Rebudget 2009-10	Rebudget 2010-11	Rebudget 2011-12	Budget Request**
<b>Personnel Services</b>	\$16,913,000	\$16,628,031	\$16,142,200	\$16,218,000	\$17,081,100
<b>Operational:</b>					
Travel	205,000	249,700	224,600	141,800	183,600
Training	165,000	200,050	164,900	97,400	90,500
Communication Services	395,000	389,400	385,800	299,900	371,000
Telephone/Equipment	9,000	0	0	0	7,500
Consultant	3,863,000	4,439,000	4,874,000	4,799,000	396,500*
Legal Services/Fees	52,000	52,000	188,000	100,500	175,500
Specialized Services	781,000	711,300	677,400	620,100	421,700
Advertising	5,000	5,000	5,000	10,000	20,000
IT Consulting	1,038,000	755,000	1,385,000	1,728,500	947,500
Contracted Maintenance & Repairs-Non-EDP	48,000	74,200	70,700	43,100	52,800
Hardware/Software and Maintenance	862,000	1,076,900	765,000	339,100	614,800*
Real Estate	1,611,000	1,630,000	1,690,000	1,725,000	1,730,800
Vehicles	54,000	54,000	32,900	34,100	44,900
Office Equipment	215,000	179,300	95,900	90,000	59,100
Other Rentals/Leases	142,000	146,700	135,500	82,500	18,600
Office Supplies	48,000	48,500	87,300	80,000	84,900
Educational Supplies	1,000	1,000	1,000	2,400	1,700
Other Computer Equipment	609,000	619,500	400,000	0	470,000
Motorized Equipment Maintenance	16,000	19,900	18,100	14,800	10,900
Postage	320,000	320,000	210,000	203,100	294,700
Freight	8,000	8,800	8,800	4,500	3,200
Printing	210,000	225,500	197,600	172,400	226,200
Subscriptions & Investment Licensing	80,000	319,300	637,500	430,800	115,000*
Membership Dues	60,000	141,900	70,400	61,200	59,500
Conference Expenses	8,000	23,150	12,800	8,300	7,400
Purchasing Card Purchases	236,000	0	0	0	0
Insurance, Surety, & Fidelity Bonds	8,000	10,000	12,000	13,500	13,000
Other Operational	861,000	904,869	1,082,800	1,200,000	1,237,100
<b>Total Operational</b>	11,910,000	12,604,969	13,433,000	12,302,000	7,658,400
<b>Fixed Assets</b>	25,000	0	0	0	120,000
<b>Less Directed Commissions</b>	1,500,000	1,500,000	1,500,000	1,200,000	1,200,000
<b>Total Annual Budget</b>	\$27,348,000	\$27,733,000	\$28,075,200	\$27,320,000	\$23,659,500

\*Investment-related expenditures that were previously included in these line items will be accounted for as non-budgeted appropriated expenditures and reported in the same manner as other investment expenditures in FY 12-13.

\*\*This budget has been approved by SERS' Board but is subject to change by the Governor's Executive Budget Committee.



**Investment Advisory and Consultant Fees 3**



# Investment Advisory & Consultant Fees

(Unaudited)

## 2011 Advisory Fees

Assets	Fees	Fees <sup>1/</sup> (in basis points)
Stocks	\$20,494,638	29.0
Fixed Income	15,286,428	37.5
Absolute Return	25,335,477	87.6
Real Estate	25,434,371	104.7
Alternative Investments	99,650,909	152.2
Inflation Protection	8,729,578	78.8
<b>Total Advisory Fees</b>	<b>\$194,931,401</b>	<b>76.4</b>

<sup>1/</sup>The fees were divided by SERS' total fund and asset class quarterly average values during calendar year 2011 to arrive at the basis point calculations.

## Average Basis Points Calendar Years Ended 2007-2011

Calendar Year	Fees (\$ millions)	Basis Points
2007	\$330.8	86.7
2008	303.8	89.1
2009	252.1	97.0
2010	231.0	94.0
2011	194.9	76.4

## 2011 Consultant Fees

Firm	Service Type	Fees
Cambridge Associates	Alternative Investments	\$2,225,000
Rocaton Investment Advisors	General Investment	490,994
StepStone Group <sup>1/</sup>	Alternative Investments	487,694
The Hay Group	Actuary	339,080
The Townsend Group	Real Estate	284,000
RV Kuhns & Associates <sup>2/</sup>	General Investment	130,973

<sup>1/</sup>Assumed duties as the Fund's alternative investment consultant in October 2011.

<sup>2/</sup>Assumed duties as the Fund's general investment consultant in October 2011.

# Fees to Managers (Non-Budget Appropriation)

(Unaudited)

SERS employs outside investment managers because of their investment expertise. The managers of the SERS' investment portfolio are paid through the non-budget appropriation. Their fees are treated as a reduction of the investment revenue of the Fund, rather than as a direct administrative expense. Thus, when investment performance is reported elsewhere in this book, the numbers are reported net of fees - that is, performance after all investment management fees have been paid.

## 2011 Fees to Managers

	City	State/Country	Fees
<b>U.S. Stocks</b>			
BlackRock Alpha Tilt	San Francisco	CA	\$198,878
BlackRock Russell 3000 NL	San Francisco	CA	165,876
BlackRock S&P 500 Index NL	San Francisco	CA	189,015
Emerald Advisors	Lancaster	PA	1,411,146
Iridian Asset Management	Westport	CT	1,194,180
Mellon Capital Management Russell 1000 Index	Pittsburgh	PA	21,594
Mellon Capital Management Custom U.S. Equity	Pittsburgh	PA	236,319
Turner Investment Partners	Berwyn	PA	136,754
<b>Absolute Return</b>			
Arden Capital Management	New York	NY	1,946,450
BAAM - Stable Alpha	New York	NY	9,141,455
Mesirow Advanced Strategies Fund	Chicago	IL	6,748,307
Morgan Stanley Alternative Investments Partners	West Conshohocken	PA	1,364,609
Pacific Alternative Asset Management Company	Irvine	CA	3,745,976
Rock Creek	Washington	DC	2,388,680
<b>Inflation Protection</b>			
Blackstone SERS Customized Commodities Fund	New York	NY	4,764,132
Wellington Management Company	Boston	MA	3,965,446
<b>Non-U.S. Stocks</b>			
Artisan Partners	Milwaukee	WI	1,923,135
BlackRock ACWI ex-U.S. NL	San Francisco	CA	807,496
BlackRock Emerging Markets NL	San Francisco	CA	555,041
Harris Associates	Chicago	IL	1,864,275
Mellon Capital Management MSCI World ex-U.S. Index	Pittsburgh	PA	10,633
Morgan Stanley - EAFE	London	United Kingdom	1,382,451
Pictet International Management - Small Capital	London	United Kingdom	607,066
Pictet International Management - Emerging Markets	London	United Kingdom	702,949
Rexiter Capital Management	Boston	MA	1,116,344
Templeton Investment Counsel	Fort Lauderdale	FL	1,315,187
Templeton Strategic Emerging Markets Fund III	Fort Lauderdale	FL	1,749,996
<b>Global Stocks</b>			
Marathon London Global Fund	London	United Kingdom	2,895,124
Walter Scott & Partners	Edinburgh	United Kingdom	2,011,179

# Fees to Managers

	City	State/Country	Fees
<b>Fixed Income</b>			
Ashmore Emerging Markets Debt Fund	London	United Kingdom	\$1,177,696
Ashmore Emerging Markets Local Currency Fund	London	United Kingdom	1,685,746
Berwind Financial Group	Philadelphia	PA	69,932
BNY Mellon Cash Investment Strategies	Pittsburgh	PA	121,196
Brandywine	Philadelphia	PA	586,789
Franklin Templeton Global Fixed Core Income	San Mateo	CA	279,923
Gramercy Advisors	Greenwich	CT	119
Greylock Capital Management	New York	NY	151,165
NISA Custom TIPS Intermediate Income	St. Louis	MO	1,332,935
Oaktree Cap Mgmt Mezzanine Fund	Los Angeles	CA	106,100
PIMCO Emerging Market Debt	Newport Beach	CA	1,013,259
PIMCO Global TIPS	Newport Beach	CA	6,385
PIMCO U.S. Treasuries	Newport Beach	CA	41,510
Pyramis Global Advisors Trust Company	Smithfield	RI	2,012,973
Ramius	New York	NY	732,305
SEI Structured Credit Fund	Oaks	PA	1,132,221
Stone Harbor Investment Partners - Emerging Market Debt	New York	NY	1,106,767
Stone Harbor Investment Partners - High Yield	New York	NY	2,165,373
Taplin, Canida & Habacht	Miami	FL	417,815
Waterfall Asset Management	New York	NY	1,104,065
Wellington U.S. Treasuries	Boston	MA	28,623
W.R. Huff Asset Management Company	Morristown	NJ	13,531
<b>Real Estate</b>			
AG Asia Realty Fund	New York	NY	221,438
Blackstone Real Estate Partners IV	New York	NY	264,403
Blackstone Real Estate Partners V	New York	NY	610,691
Blackstone Real Estate Partners VI	New York	NY	1,094,751
Blackstone Real Estate Partners VII	New York	NY	5,000
BPG Investment Partnership V	Yardley	PA	71,104
BPG Investment Partnership VI	Yardley	PA	123,106
BPG Investment Partnership VII	Yardley	PA	240,000
BPG Investment Partnership VIII	Yardley	PA	197,127
Clerestory Small Cap Real Estate Fund I	New York	NY	254,205
Colony Investors VIII	Los Angeles	CA	207,640
Fidelity Real Estate Opportunistic Income Fund	Smithfield	RI	334,483
Fillmore East Fund	San Francisco	CA	270,196
Fillmore West Fund	San Francisco	CA	201,015
Forest Investment Associates	Atlanta	GA	1,142,587
Goldman Sachs/Whitehall VII & VIII	New York	NY	2,834
Grosvenor Investment Management	Philadelphia	PA	3,199,133
Grosvenor Residential Investment Partners I	Philadelphia	PA	232,036
Hawkeye Scout Fund I	Dallas	TX	568,059
Heitman America Real Estate Trust	Chicago	IL	574,160

# Fees to Managers

(Real Estate, continued)

	City	State/Country	Fees
Heitman Capital Management	Chicago	IL	\$1,165,210
ING Clarion Real Estate Securities	Radnor	PA	1,080,228
LaSalle Investment Management	Baltimore	MD	2,197,376
Lowe Enterprises Investment Management	Los Angeles	CA	2,912,178
Lubert Adler Real Estate Fund II	Philadelphia	PA	8,902
Lubert Adler Real Estate Fund IV	Philadelphia	PA	61,095
Lubert Adler Real Estate Fund V	Philadelphia	PA	37,243
Lubert Adler Real Estate Fund VI	Philadelphia	PA	373,843
Oaktree Cap Mgmt Real Estate Opportunities Fund III	New York	NY	11,929
Oxford Fund	Pittsburgh	PA	315,979
Prudential Latin America Retail Fund I	Parsippany	NJ	374,052
Prudential Latin America Residential Fund III	Parsippany	NJ	345,827
Prudential Senior Housing Partners II	Parsippany	NJ	4,183
Prudential Senior Housing Partners III	Parsippany	NJ	349,065
Prudential Senior Housing Partners IV	Parsippany	NJ	8,000
Rockpoint Finance Fund I	Dallas	TX	21,824
Rockpoint Real Estate Fund I	Dallas	TX	52,622
Rockpoint Real Estate Fund II	Dallas	TX	289,806
Rockpoint Real Estate Fund III	Dallas	TX	424,631
Sentinel Real Estate Corporation	New York	NY	478,918
Starwood Global Opportunity Fund VI	Greenwich	CT	421,759
Starwood Global Opportunity Fund VII	Greenwich	CT	413,053
Starwood Global Opportunity Fund VIII	Greenwich	CT	791,646
UBS Trumbull Property Income Fund	Hartford	CT	525,335
UBS Trumbull Property Fund	Hartford	CT	773,510
Urdang Securities Management	Plymouth Meeting	PA	281,136
Westbrook Real Estate Fund II	Dallas	TX	1,232
Westbrook Real Estate Fund III	Dallas	TX	5,787
Westbrook Real Estate Fund IV	Dallas	TX	61,204
Westbrook Real Estate Fund V	Dallas	TX	102,990
Westbrook Real Estate Fund VI	Dallas	TX	333,477
Westbrook Real Estate Fund VII	Dallas	TX	646,363
Westbrook Real Estate Fund VIII	Dallas	TX	750,000

## Venture Capital

Abingworth Bioventures IV	London	United Kingdom	400,000
Abingworth Bioventures V	London	United Kingdom	428,614
ABS Capital Partners VI	Baltimore	MD	833,367
Adams Capital Management III	Sewickley	PA	467,875
Advanced Technology Ventures VI	Waltham	MA	136,747
Advanced Technology Ventures VII	Waltham	MA	193,033
Alloy Ventures 2000	Palo Alto	CA	186,260
Alloy Ventures 2002	Palo Alto	CA	132,918
Alloy Ventures 2005	Palo Alto	CA	529,384
APAX Excelsior VI	New York	NY	157,721

# Fees to Managers

(Venture Capital, continued)

	City	State/Country	Fees
Apex Investment Partners Fund V	Chicago	IL	\$3,700
Artiman Ventures II	Palo Alto	CA	531,149
Artiman Ventures III	Palo Alto	CA	457,704
Atlas Venture Fund V	Waltham	MA	27,821
Atlas Venture Fund VI	Waltham	MA	156,001
Austin Ventures VIII	Austin	TX	178,302
Austin Ventures IX	Austin	TX	291,538
Battery Ventures VIII	Waltham	MA	574,313
Battery Ventures VIII Side Fund	Waltham	MA	162,522
Birchmere Ventures Fund III	Pittsburgh	PA	88,098
Care Capital Investments III	Princeton	NJ	457,255
Charles River Partnership XI	Waltham	MA	214,399
CID Greater China Venture Capital Fund II	Taipei	Taiwan	283,857
Clearstone Venture Partners III	Santa Monica	CA	400,000
Cross Atlantic Technology I	Radnor	PA	38,170
Cross Atlantic Technology II	Radnor	PA	106,142
Devon Park Bioventures	Wayne	PA	224,705
Draper Fisher Jurveston VII	Menlo Park	CA	7,337
Draper Triangle Ventures I	Pittsburgh	PA	125,435
Draper Triangle Ventures II	Pittsburgh	PA	180,000
Frazier Healthcare IV	Seattle	WA	172,091
Frazier Healthcare V	Seattle	WA	354,838
Guggenheim Technology Ventures I	King of Prussia	PA	40,512
Halpern Denny Fund III	Boston	MA	29,026
HarbourVest Partners VI	Boston	MA	1,385,150
HarbourVest Partners VII	Boston	MA	750,000
HarbourVest Partners VIII	Boston	MA	1,000,000
Healthcare Ventures VII	Princeton	NJ	694,960
Healthcare Ventures VIII	Princeton	NJ	477,697
Highland Capital Partners VI	Lexington	MA	377,237
Highland Capital Partners VII	Lexington	MA	875,940
Highland Consumer Fund I	Lexington	MA	624,932
I.P. - Fund II	Bellevue	WA	52,508
I.P. - Fund III	Bellevue	WA	79,993
I.P. - Fund IV	Bellevue	WA	85,738
Insight Venture Partners VII	New York	NY	249,900
InterWest Partners IX	Menlo Park	CA	495,768
InterWest Partners X	Menlo Park	CA	750,000
J.P. Morgan Venture Capital Institutional Investors I	New York	NY	626,275
J.P. Morgan Venture Capital Institutional Investors II	New York	NY	745,991
J.P. Morgan Venture Capital Institutional Investors III	New York	NY	1,065,736
JMI Equity Fund V	Baltimore	MD	232,339
JMI Equity Fund VI	Baltimore	MD	748,548
JMI Equity Fund VII	Baltimore	MD	175,844
Kline Hawkes Pacific	Los Angeles	CA	69,257
Knightsbridge Venture Capital VI	Bartlesville	OK	140,000



# Fees to Managers

(Venture Capital, continued)

	City	State/Country	Fees
Lightspeed Venture Partners VII	Menlo Park	CA	\$546,922
Lightspeed Venture Partners VIII	Menlo Park	CA	364,620
Meritech Capital Partners III	Palo Alto	CA	708,725
Meritech Capital Partners IV	Palo Alto	CA	390,822
Mid-Atlantic Venture Fund IV	Bethlehem	PA	67,448
Morgenthaler Venture Partners VII	Menlo Park	CA	414,899
Morgenthaler Venture Partners VIII	Menlo Park	CA	731,981
Morgenthaler Venture Partners IX	Menlo Park	CA	360,406
New Enterprise Associates IX	Baltimore	MD	176,681
New Enterprise Associates X	Baltimore	MD	201,227
New Enterprise Associates 11	Baltimore	MD	155,860
New Enterprise Associates 12	Baltimore	MD	402,924
Newspring Ventures II	King of Prussia	PA	200,000
Novitas III	King of Prussia	PA	85,068
Oak Investment Partners XI	Westport	CT	702,937
Oak Investment Partners XII	Westport	CT	892,701
Pitango Venture Capital Fund IV	Herzliya	Israel	275,142
Pitango Venture Capital Fund V	Herzliya	Israel	675,123
Polaris Venture Partners III	Waltham	MA	56
Polaris Venture Partners IV	Waltham	MA	1,364,858
Polaris Venture Partners V	Waltham	MA	1,250,000
Quaker BioVentures I	Philadelphia	PA	393,414
Quaker BioVentures II	Philadelphia	PA	562,897
Sofinnova Venture Partners VII	San Francisco	CA	764,907
Summit Accelerator	Boston	MA	17,443
Summit Partners Venture Capital Fund II	Boston	MA	334,513
T Rowe Price	Baltimore	MD	366,081
Technology Leaders IV	Wayne	PA	64,297
Technology Leaders V	Wayne	PA	271,756
Three Arch Capital Partners I	Portola Valley	CA	144,270
Three Arch Capital Partners IV	Portola Valley	CA	399,336
Weathergage Venture Capital	Redwood City	CA	250,000
Weathergage Venture Capital II	Redwood City	CA	250,000
Weston Presidio Capital IV	Boston	MA	74,306
Weston Presidio Capital V	Boston	MA	304,183
Worldview Technology Partners IV	San Mateo	CA	136,369

## Private Equity

ABRY Advanced Securities Fund I	Boston	MA	494,393
ABRY Broadcast Partners III	Boston	MA	35,088
ABRY Broadcast Partners IV	Boston	MA	75,594
ABRY Broadcast Partners V	Boston	MA	180,242
ABRY Mezzanine Partners	Boston	MA	27,937
ABRY Partners VI	Boston	MA	464,582
ABRY Partners VII	Boston	MA	289,865

# Fees to Managers

(Private Equity, continued)

	City	State/Country	Fees
ABRY Senior Equity II	Boston	MA	\$367,882
ABS Capital Partners III	Baltimore	MD	520
ABS Capital Partners IV	Baltimore	MD	199,258
ABS Capital Partners V	Baltimore	MD	259,407
Accel Europe	London	United Kingdom	348,727
Advent International Global Private Equity VI	Boston	MA	478,947
Advent Latin American Private Equity Fund IV	Boston	MA	415,290
Advent Latin American Private Equity Fund V	Boston	MA	253,056
AG Capital Recovery Partners IV	New York	NY	8,391
AG Capital Recovery Partners V	New York	NY	101,937
Alpha Private Equity Fund 4	Paris	France	78,578
Alpha Private Equity Fund 5	Paris	France	1,053,861
APAX Europe Fund V	London	United Kingdom	198,351
APAX Europe VI-A	London	United Kingdom	418,708
APAX Europe VII-A	London	United Kingdom	826,894
Asia Alternative Capital Partners	San Francisco	CA	118,827
Asia Alternative Capital Partners II	San Francisco	CA	202,130
Asia Pacific Associates III	San Francisco	CA	11,216
Audax Private Equity Fund II	Boston	MA	18,720
Audax Private Equity Fund III	Boston	MA	499,899
Avenue Asia Special Situations Fund IV	New York	NY	69,827
Avenue Europe Special Situations Fund	New York	NY	583,100
Avenue Special Situations Fund IV	New York	NY	36,832
Avenue Special Situations Fund V	New York	NY	622,689
Avenue Special Situations Fund VI	New York	NY	71,178
AXA Secondary Fund III-1	Paris	France	60,366
AXA Secondary Fund III-2	Paris	France	31,389
AXA Secondary Fund IV	Jersey	Channel Islands	775,714
Bain Capital Asia Fund	Boston	MA	234,780
Bain Capital Europe Fund III	Boston	MA	1,137,891
Bain Capital Fund VII	Boston	MA	79,885
Bain Capital Fund VIII	Boston	MA	252,947
Bain Capital Fund IX	Boston	MA	1,669,999
Bain Capital Fund IX Coinvestment Fund	Boston	MA	261,143
Bain Capital Fund X	Boston	MA	1,650,045
Bain Capital Fund X Coinvestment Fund	Boston	MA	14,300
Baring India Private Equity Fund III	Port Lewis	Mauritius	75,070
Baring Vostok Private Equity Fund IV	Guernsey	Channel Islands	324,475
BC European Capital VII	London	United Kingdom	6,025
BC European Capital VIII	London	United Kingdom	361,537
BC European Capital IX	London	United Kingdom	261,535
Berkshire Fund VI	Boston	MA	201,400
Berkshire Fund VII	Boston	MA	497,585
Berkshire Fund VIII	Boston	MA	131,675
Blackstone Capital Partners V	New York	NY	252,443

# Fees to Managers

(Private Equity, continued)

	City	State/Country	Fees
Blackstone Communications Partners I	New York	NY	\$45,278
Brait IV	Grand Cayman	Cayman Islands	475,553
Brynwood Partners V	Greenwich	CT	93,571
Brynwood Partners VI	Greenwich	CT	149,373
Centerbridge Capital Partners	New York	NY	685,885
Cerberus Institutional Partners Series Two	New York	NY	43,387
Cerberus Institutional Partners Series Three	New York	NY	200,204
Cerberus Institutional Partners Series Four	New York	NY	996,563
Charterhouse Capital Partners VII	London	United Kingdom	76,483
Charterhouse Capital Partners VIII	London	United Kingdom	526,136
Charterhouse Capital Partners IX	London	United Kingdom	1,034,873
Chequers Capital XV	Paris	France	548,194
Clessidra Capital Partners II	Milan	Italy	474,841
Code, Hennessy & Simmons V	Chicago	IL	75,582
Cognetas II	London	United Kingdom	590,481
CVI Global Value Fund	Grand Cayman	Cayman Islands	1,054,478
DLJ Merchant Banking III	New York	NY	82,461
Dover Street VII	Boston	MA	315,372
Elevation Partners	Menlo Park	CA	163,351
Energy Spectrum Partners IV	Dallas	TX	828,281
Energy Spectrum Partners V	Dallas	TX	267,068
Eureka II	Yardley	PA	337,308
Excelsior Capital Asia Partners III	Hong Kong	China	500,000
First Reserve Fund X	Greenwich	CT	99,994
First Reserve Fund XI	Greenwich	CT	371,761
First Reserve Fund XII	Greenwich	CT	778,897
Francisco Partners II	San Francisco	CA	51,274
Francisco Partners III	San Francisco	CA	145,775
Great Hill Equity Partners III	Boston	MA	489,973
Great Hill Equity Partners IV	Boston	MA	415,582
Gryphon Partners II	San Francisco	CA	59,205
Gryphon Partners III	San Francisco	CA	188,856
GTCR Fund VII	Chicago	IL	30,696
GTCR Fund VIII	Chicago	IL	589,030
GTCR Fund IX	Chicago	IL	356,564
H.I.G. Bayside Debt & LBO Fund II	Miami	FL	600,000
H.I.G. Growth Buyouts & Equity Fund II	Miami	FL	150,000
HarbourVest International Private Equity III	Boston	MA	191,330
HarbourVest International Private Equity IV	Boston	MA	323,920
HIPEP V-Asia Pacific and Rest of World Partnership Fund	Boston	MA	300,000
Hellman & Friedman Capital Partners V	San Francisco	CA	66,895
Hellman & Friedman Capital Partners VI	San Francisco	CA	1,225,942
Insight Venture Partners VI	New York	NY	605,599
InterMedia Partners VII	New York	NY	224,906
Invemed Catalyst Fund	New York	NY	11,647

# Fees to Managers

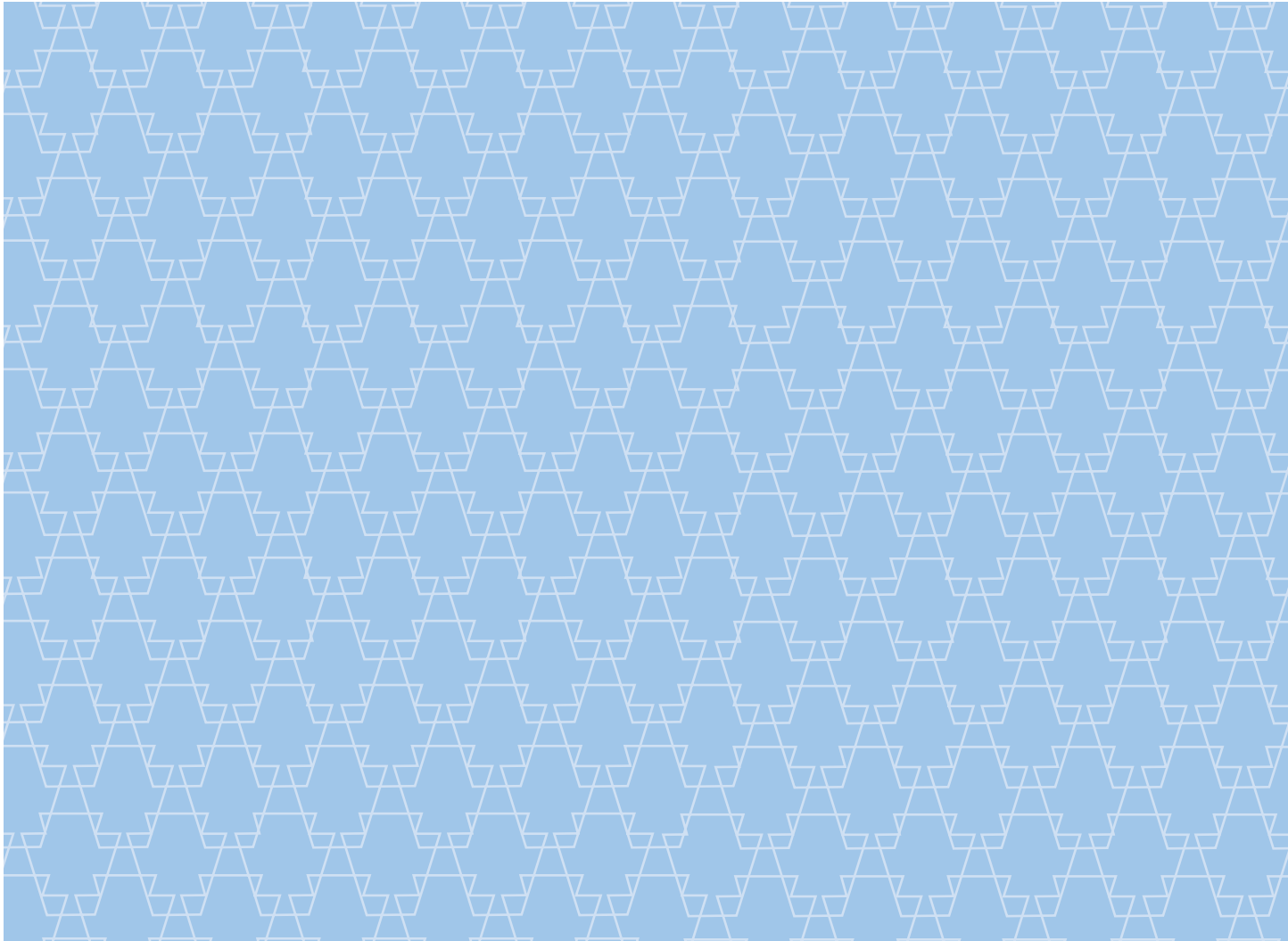
(Private Equity, continued)

	City	State/Country	Fees
J.H. Whitney Fund V	Stamford	CT	\$2,155
J.H. Whitney Fund VI	Stamford	CT	145,707
J.H. Whitney Fund VII	Stamford	CT	708,739
J.P. Morgan U. S. Corporate Financial Institutional Investors II	New York	NY	372,307
J.W. Childs Equity Partners III	Boston	MA	340,093
Kelso Investment Associates VII	New York	NY	281,058
Kelso Investment Associates VIII	New York	NY	2,250,000
Leeds Weld Equity Partners IV	New York	NY	131,581
Lexington Capital Partners III	New York	NY	1,105
Lexington Capital Partners V	New York	NY	283,221
Lexington Capital Partners VI	New York	NY	319,569
Lime Rock Partners III	Westport	CT	152,369
Lime Rock Partners IV	Westport	CT	406,678
Lime Rock Partners V	Westport	CT	846,905
Lime Rock Resources C	Westport	CT	273,756
LLR Equity Partners	Philadelphia	PA	89,324
LLR Equity Partners II	Philadelphia	PA	294,277
LLR Equity Partners III	Philadelphia	PA	600,000
Madison Dearborn Capital Partners IV	Chicago	IL	34,300
Madison Dearborn Capital Partners V	Chicago	IL	333,710
Madison Dearborn Capital Partners VI	Chicago	IL	653,394
Matlin Patterson Global Opportunities Partners	New York	NY	10,442
Media Communications Partners V	Boston	MA	131,148
Meridian Venture Partners II	Radnor	PA	377,690
New York Life Capital Partners III	New York	NY	374,923
New York Life Capital Partners IV	New York	NY	500,000
Newbridge Asia IV	San Francisco	CA	191,260
Nordic Capital V	Stockholm	Sweden	199,762
Nordic Capital VI	Stockholm	Sweden	408,559
Nordic Capital VII	Stockholm	Sweden	1,423,246
Oak Hill Capital Partners I	Menlo Park	CA	10,343
Oaktree Cap Mgmt Opportunities Fund I	Los Angeles	CA	2,241
Oaktree Cap Mgmt Opportunities Fund IV	Los Angeles	CA	10,722
Oaktree Cap Mgmt Opportunities Fund V	Los Angeles	CA	232,180
Oaktree Cap Mgmt Opportunities Fund VI	Los Angeles	CA	375,432
Oaktree Cap Mgmt Opportunities Fund VII	Los Angeles	CA	463,978
Oaktree Cap Mgmt Opportunities Fund VIIb	Los Angeles	CA	505,075
Oaktree Cap Mgmt Opportunities Fund VIII	Los Angeles	CA	333,090
Oaktree Cap Mgmt Opportunities Fund VIIIb	Los Angeles	CA	65,449
Oaktree Cap Mgmt Principal Opportunities Fund IV	Los Angeles	CA	330,612
Oaktree Cap Mgmt/GFI Power Opportunities Fund II	Los Angeles	CA	49,063
Oaktree Cap Mgmt/GFI Power Opportunities Fund III	Los Angeles	CA	650,069
Palamon Partners I	London	United Kingdom	160,512
Palamon European Equity II	London	United Kingdom	569,252
Parthenon Investors II	Boston	MA	154,121

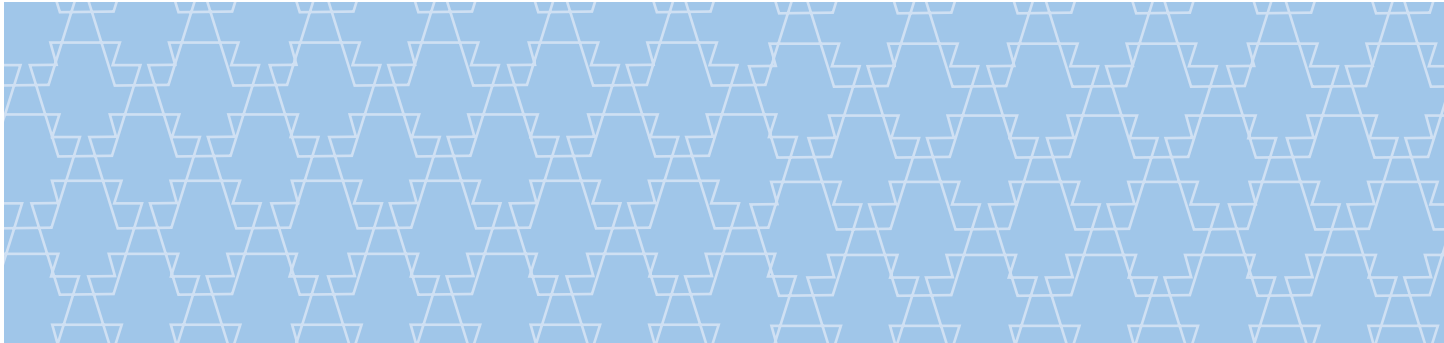
# Fees to Managers

(Private Equity, continued)

	City	State/Country	Fees
Patriot Financial Partners	Philadelphia	PA	\$518,980
Permira European Fund III	London	United Kingdom	598,823
PNC Equity Partners II	Pittsburgh	PA	113,153
Providence Equity Offshore Partners V	Providence	RI	387,021
Providence Equity Partners VI	Providence	RI	262,138
Sankaty Credit Opportunities III	Boston	MA	996,045
Sankaty Credit Opportunities IV	Boston	MA	729,101
SFC Energy Partners I	Denver	CO	544,060
SFC Energy Partners II	Denver	CO	124,996
SCP Private Equity Partners II	Wayne	PA	198,449
Segulah IV	Jersey	Channel Islands	148,262
ShoreView Capital Partners	Minneapolis	MN	41,160
ShoreView Capital Partners II	Minneapolis	MN	713,062
Siguler Guff BRIC Opportunities Fund	New York	NY	81,515
Siguler Guff BRIC Opportunities Fund II	New York	NY	210,060
Sterling Capital Partners	Northbrook	IL	123,497
Sterling Capital Partners II	Northbrook	IL	260,572
Sterling Capital Partners III	Northbrook	IL	679,322
Summit Partners Private Equity Fund VI	Boston	MA	477,700
Summit Partners Private Equity Fund VII	Boston	MA	2,112,526
TA IX	Boston	MA	112,145
TA X	Boston	MA	1,588,522
Thomas H. Lee Equity Fund V	Boston	MA	70,420
Thomas H. Lee Equity Fund VI	Boston	MA	856,329
TPG Asia V	Fort Worth	TX	301,750
TPG Partners V	Fort Worth	TX	332,787
TPG Partners VI	Fort Worth	TX	281,305
Trust Company of the West - Special Credits V	Los Angeles	CA	6,103
Versa Capital Management	Philadelphia	PA	273,247
Versa Capital Fund II	Philadelphia	PA	58,381
Vestar Capital Partners IV	New York	NY	355,354
Vestar Capital Partners V	New York	NY	420,853
W Capital Partners II	New York	NY	798,963
Yucaipa American Alliance Fund II	Los Angeles	CA	313,373
<b>Total Fees to Managers</b>			<b>\$194,931,401</b>



**Directed Commissions 4**

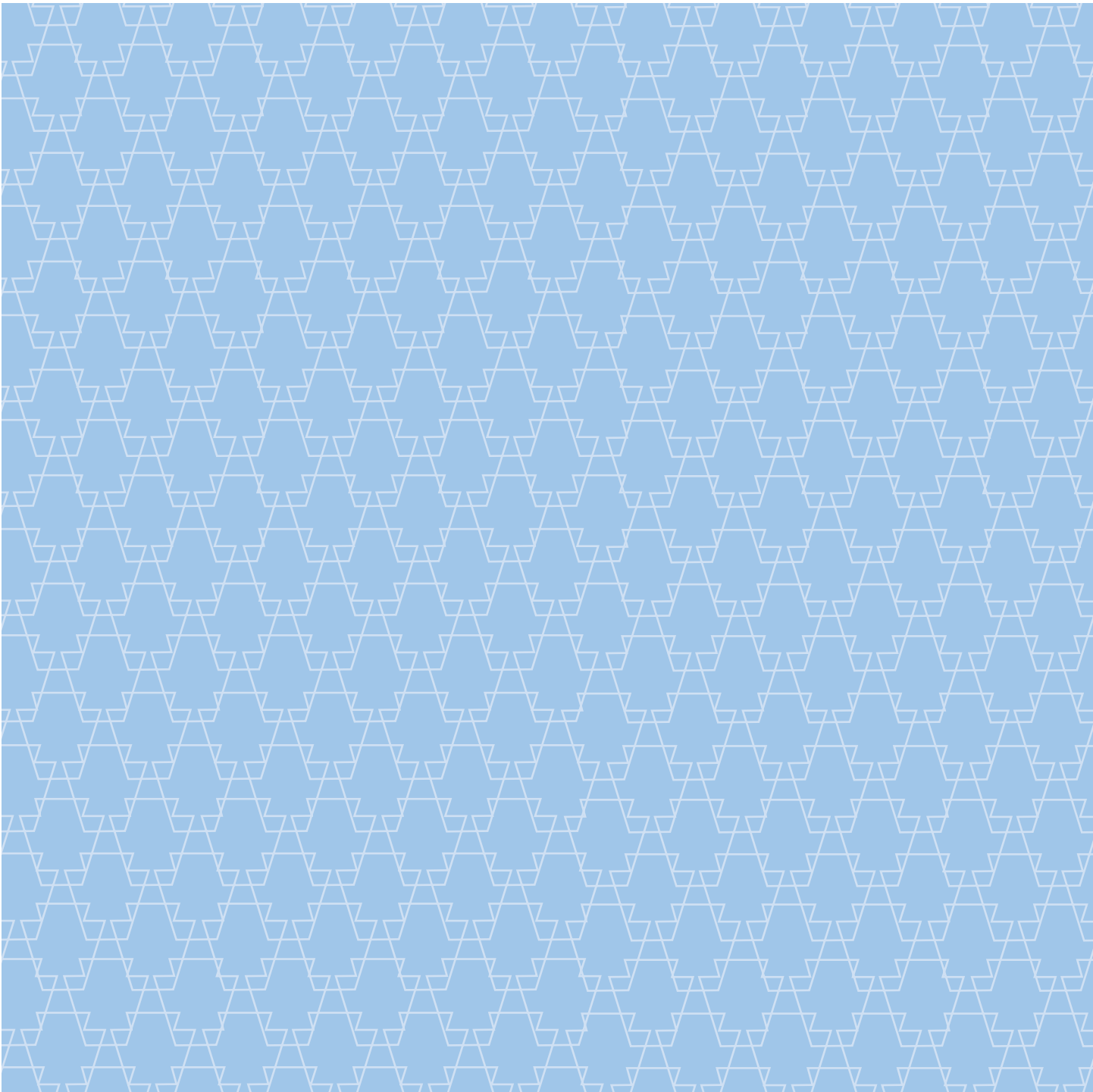


# Directed Commissions

## Directed Commissions\*

	FY 2011-12 Budget	FY 2012-13 Budget
Beginning Balance	\$3,861,059	\$2,761,059
Directed Commission Revenue	100,000	100,000
<b>Total Available</b>	<b>3,961,059</b>	<b>2,861,059</b>
Directed Commission Expense	1,200,000	1,200,000
<b>Ending Balance</b>	<b>\$2,761,059</b>	<b>\$1,661,059</b>

*\*Directed commissions are reimbursements to the System for a portion of the fee paid to a broker for executing a trade.*





# Member Services

The Office of Member Services provides a variety of services to SERS Active Members and Annuitants. Following are lists of services provided through the seven Regional Retirement Counseling Centers.

## Services to Active Members

- Calculate regular retirement, Disability Retirement and vesting estimates upon request.
- Provide one-on-one counseling for any member who is considering retiring or terminating service.
- Provide Active Members with an annual *Member Statement of Account*.
- Provide counseling to deceased members' Beneficiaries or Survivor Annuitants.
- Conduct group information sessions (Question & Answer Sessions, Pre-Retirement and Vestee Seminars).
- Provide resource speakers for various agency or association information sessions.
- Provide estimates and counsel members on the purchase of creditable State and nonstate service.
- Provide information on members' eligibility for retiree health benefits.

## Services to Retired Members

- Provide direct deposit forms, federal income tax withholding forms, and change of address forms upon request; and provide information and assistance to complete the forms.
- Provide Beneficiary forms and assist members in completing the forms.
- Provide all Annuitants with an annual *Personal Statement of Retirement Benefits*.
- Provide all Annuitants with a *1099-R* federal tax form each tax year.
- Take information and process change of dependent information on the retiree's Retired Employees Health Program (REHP) coverage.
- Investigate and place stop payment transactions on checks not received by Annuitants after ten working days.
- Provide resource speakers for group or association informational seminars.
- Receive and process notifications of death and serve as a contact for Beneficiaries and Survivors.
- Provide option change counseling for members when their Designated Survivor predeceases them, the retiree obtains a divorce, or when the retiree marries after the date of their retirement.
- Provide counseling on any change of monthly Annuity payment, when applicable.

## Regional Retirement Counseling Centers

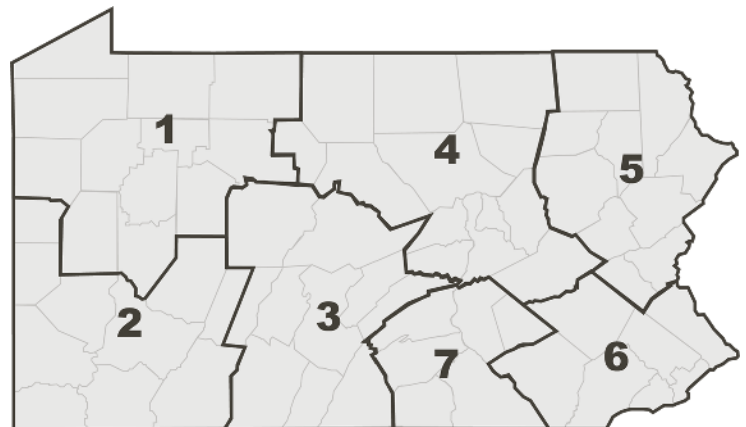
**Region 1 Seneca Office** Serving Armstrong, Butler, Clarion, Crawford, Elk, Erie, Forest, Jefferson, McKean, Mercer, Venango and Warren counties.

**Region 2 Pittsburgh Office** Serving Allegheny, Beaver, Cambria (Western), Fayette, Greene, Indiana, Lawrence, Somerset, Washington and Westmoreland counties.

**Region 3 State College Office** Serving Bedford, Blair, Cambria (Eastern), Centre, Clearfield, Franklin, Fulton, Huntingdon, Juniata and Mifflin counties.

**Region 4 Montoursville Office** Serving Bradford, Cameron, Clinton, Columbia, Lycoming, Montour, Northumberland, Potter, Schuylkill, Snyder, Sullivan, Tioga and Union counties.

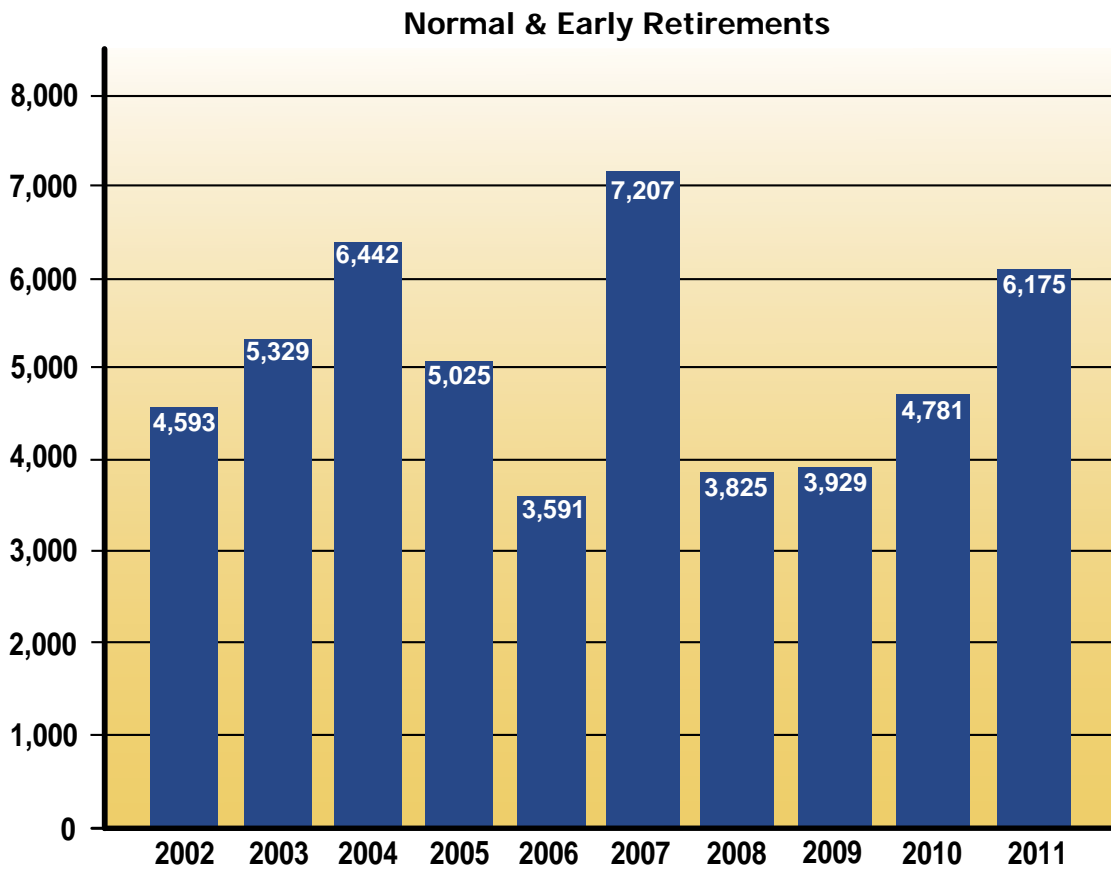
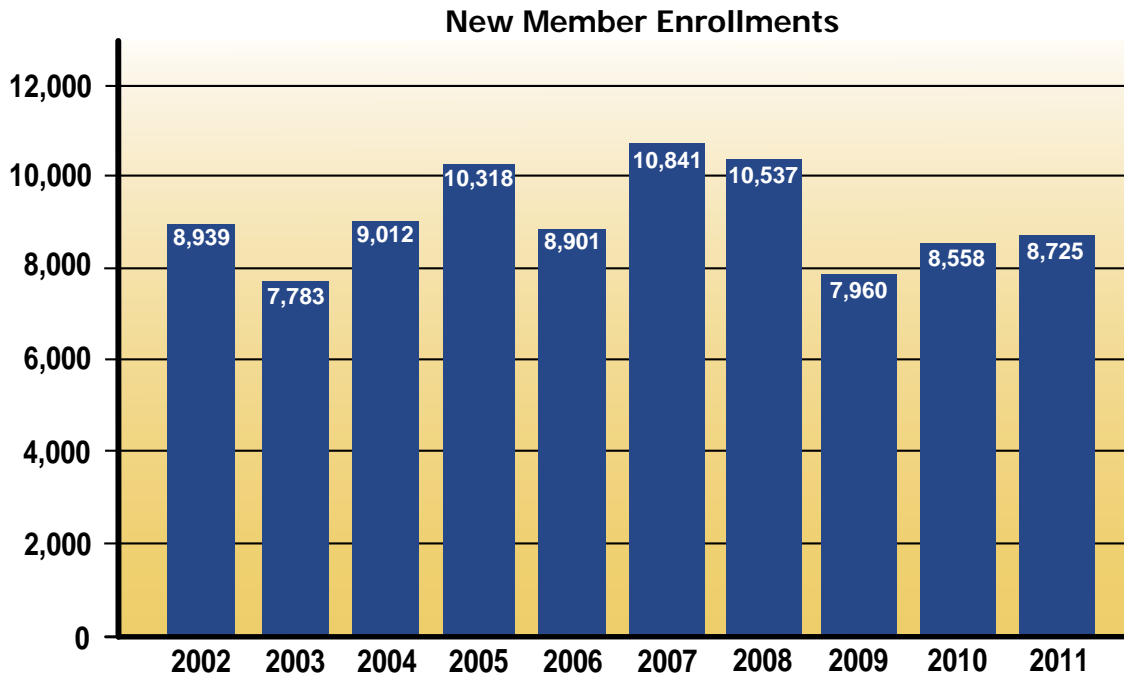
**Region 5 Hazleton Office** Serving Carbon, Lackawanna, Lehigh, Luzerne, Monroe, Northampton, Pike, Susquehanna, Wayne and Wyoming counties.



**Region 6 Bensalem Office** Serving Berks, Bucks, Chester, Delaware, Lancaster and Montgomery counties and Philadelphia.

**Region 7 Harrisburg Office** Serving Adams, Cumberland, Dauphin, Lebanon, Perry and York counties.

# Benefit Processing



# SERS Member Demographics

Year Ending December 31	Membership		
	Total Members*	Active Members	Annuitants & Beneficiaries
2011	222,581	107,239	115,342
2010	220,968	109,255	111,713
2009	220,097	110,458	109,639
2008	219,012	110,866	108,146
2007	216,740	109,610	107,130
2006	213,032	110,972	102,060
2005	211,160	109,981	101,179
2004	207,132	108,405	98,727
2003	203,430	109,018	94,412
2002	202,287	111,059	91,228

\*These totals do not include inactive members.

Since 2002 Annuitants and Beneficiaries have increased by 26.4% while the number of Active Members has remained relatively steady.

## Active Member Age and Service as of December 31, 2011

Average Age:	46.6
Average Years of Service:	12.2

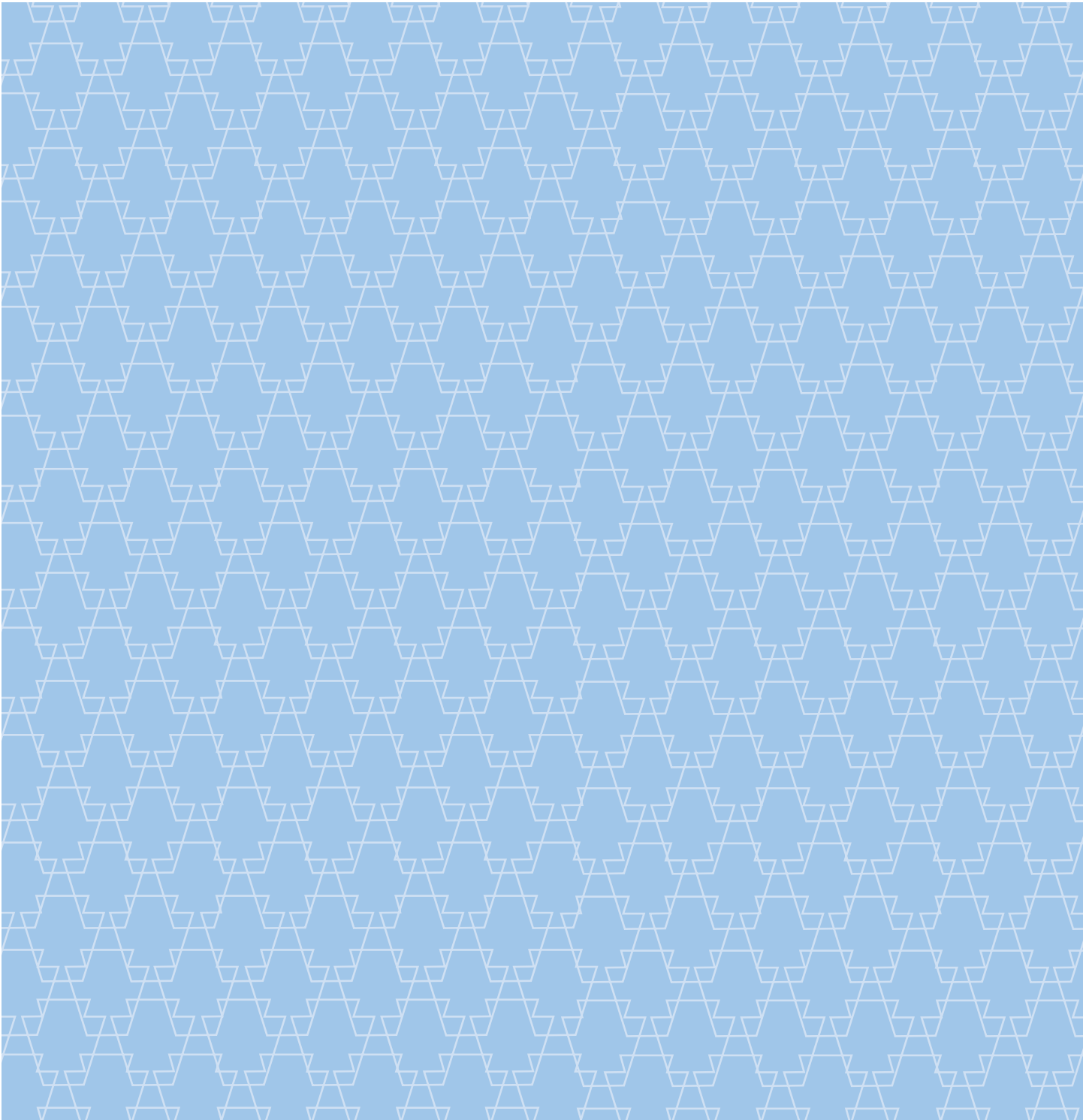
## Total Annuitants and Beneficiaries as of December 31

	2008	2009	2010	2011
Superannuation Annuitants	52,821	53,478	54,659	56,722
Early Retirees	38,069	38,624	39,241	40,483
Disabled Annuitants	7,602	7,674	7,801	7,891
Beneficiary/Survivors	9,654	9,863	10,012	10,246

## Profile of Annuitants, Beneficiaries and Survivor Annuitants as of December 31

	Average Age				Average Annual Pension			
	2008	2009	2010	2011	2008	2009	2010	2011
Superannuation Annuitants	72.8	72.8	72.7	72.4	\$21,965	\$22,695	\$23,491	\$24,448
Early Retirees	61.8	62.2	62.7	62.9	14,668	14,932	15,209	15,770
Disabled Annuitants	60.8	61.1	61.4	61.8	13,251	13,443	13,774	14,027
Beneficiary/Survivors	75.0	74.9	75.0	74.8	9,094	9,481	9,833	10,334

Since 2008 the average annual superannuation pension is up 11.3%.



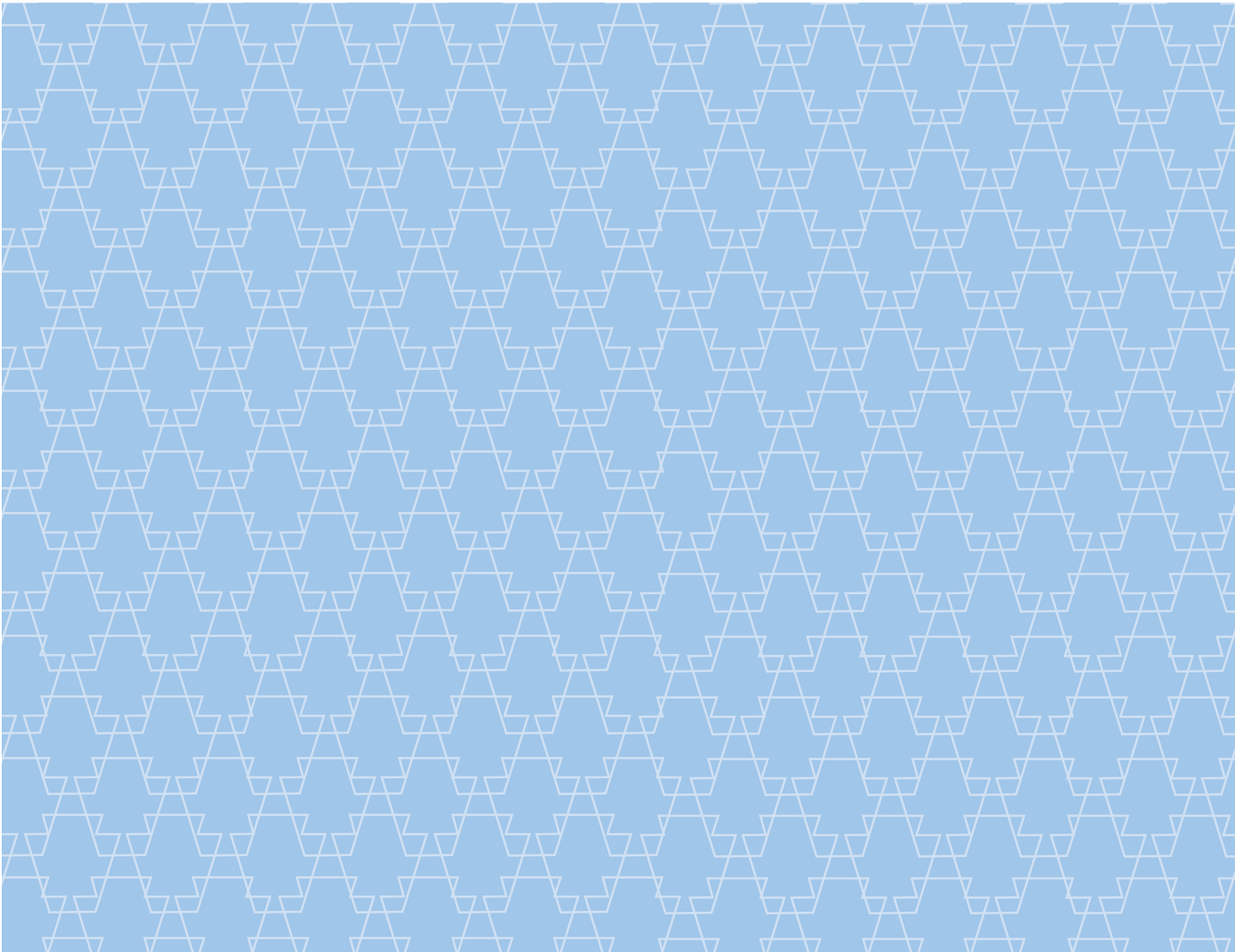
# Legislation

## **Legislation Enacted During 2011**

No amendments to the Retirement Code (Title 71) became law during 2011.



# Funding Process and Actuarial Status 7



# Funding Process & Actuarial Status

(Unaudited)

## Funding Process: Defined Benefit Plan and Deferred Compensation Program

Pennsylvania's State Employees' Retirement System administers two retirement plans to help ensure the financial security of the Commonwealth's public workforce in their retirement years.

### Defined Benefit Plan

Most state employees are required to participate in Pennsylvania's defined benefit plan, which is referred to simply as the "pension plan."

In the defined benefit plan, both the employer and the employee pay a certain percentage of the employee's salary to the SERS Fund for as long as the employee works for the Commonwealth. In FY 2011/12, employers generally are paying 8% and most employees are paying 6.25%. SERS aggregates and invests this money to achieve returns to help ensure sufficient funds are available to make payments to current and future retirees.

When employees meet certain thresholds – working a specific number of years to achieve "vesting," for example – they become eligible to receive monthly retirement payments for the rest of their lives. The payment amount is based on a formula that includes the employee's length of service, their age, their compensation over a period of time, and an "accrual rate" that is determined by the General Assembly.

The rules of this plan are set forth in Pennsylvania law through the State Employees' Retirement Code. Additional details of the defined benefit plan are included in this section.

### Deferred Compensation Program

Commonwealth employees who are eligible to participate in the pension plan may choose to augment their retirement savings by voluntarily participating in the SERS-administered Deferred Compensation Program. This plan is often referred to simply as "deferred comp."

In the deferred comp program, employees elect to have any sum they choose – up to certain limits – withheld from their paychecks on a pre-tax basis. There is no employer contribution. Employees may enroll at any time and change the amount they contribute at their discretion. Employees direct their own savings into an array of investment options and may adjust their allocations and options at any time.

When employees retire, they gain access to the amount they've saved, including the earnings and/or losses on their own investments.

The cost of administering this plan is borne solely by participants, using no Commonwealth funds.

The rules of this plan are set forth in federal law through Section 457(b) of the Internal Revenue Code. Additional details of the Deferred Compensation Program are included in Tab 12 of this book.

## Funding Process: Determining Adequate Funding for a Defined Benefit Plan

A defined benefit plan operates on a sound basis when the funds on hand and expected future contributions plus earnings are sufficient to cover the value of promised benefits.

It is a standard feature that employee and employer contributions invested throughout an employee's working life provide sufficient funding to pay for that particular employee's expected lifetime retirement benefit.

Because a defined benefit plan guarantees a monthly payment to every retiree for life, it is impossible to develop precise, before-the-fact costs and cash flows for the plan.

### What is an "unfunded liability"?

An "unfunded liability" – also commonly called an "unfunded actuarial liability" or "UAL" – is the degree to which the current and projected liabilities exceed the current and projected assets of a pension plan.

In other words, it is the difference between what the Commonwealth's pension plan is legally obligated to pay and what assets have been set aside to make those payments.

# Funding Process & Actuarial Status *(continued)*

The number of people paying into the plan, the amount they earn, how long they work, the number of people retiring, the age at which each person retires, and how long each retiree lives are among the myriad of factors that vary from day-to-day, month-to-month, and year-to-year.

Actuarial science is used to develop accurate predictions. Actuarial science applies available data to a number of interrelated mathematical and statistical methods and uses investment and financial practices to study uncertain future events.

SERS' actuarial firm conducts an in-depth investigation, review, and analysis of economic and demographic data every five years. Economic assumptions include rates of investment return and salary growth, for example, which are significantly impacted by inflation. Demographic assumptions include workforce, disability, and mortality trends.

<p><b>Key Actuarial Assumptions</b></p> <p>8.00% long-term investment return</p> <p>6.20% average salary/career growth</p> <p>2.75% inflation rate</p>	<p>The selection of economic and demographic assumptions used is generally guided by the Actuarial Standards Board via the Actuarial Standard of Practice 35. In SERS' case, some very important assumptions – such as the length of time over which investment gains and losses are recognized on SERS' books – are set by Pennsylvania law.</p> <p>Each year, SERS' actuary performs a valuation of the plan. The valuation uses the most recent employee and retiree demographic data to determine the sum of expected future obligations and compares such obligations to the expected value of the Fund's assets, based on current audited financial statements and future economic assumptions.</p> <p>This calculation is factored with the statutorily set employee contribution rate and the assumed investment rate of return as the basis for calculating how much employers need to contribute in order to fully fund their employees' retirement benefits.</p>
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## Funding Process: Sources and Trends for SERS' Defined Benefit Plan

Defined benefit plans are designed to remain stable by receiving three regular funding streams – employee contributions, investment earnings, and employer contributions.

### Employee Contributions

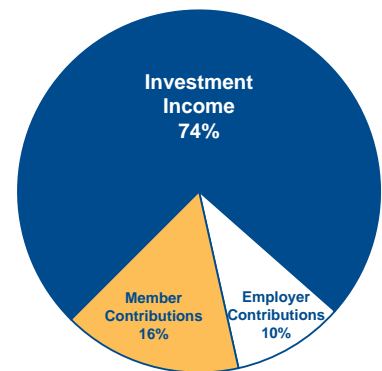
Active employees pay a certain percentage of their salaries toward their retirement benefit. While different classes of employees pay different rates, most employees currently pay 6.25% of their salary with a certain segment who are eligible for and elect higher benefits at 9.3% of pay. Employees' contributions are typically withheld from their paychecks and sent directly from their employer to SERS. The percentage is set by statute and the rate doesn't change from year to year.

In 1981, employee contributions totaled \$116 million; in 2011 employee contributions totaled \$350 million, a more than 200% increase over 30 years.

A significant body of case law establishes that the contract clauses of the United States and Pennsylvania constitutions protect public retirement benefits from being retroactively changed in any way that may be construed as a "net detriment" to employees. "Net detriment" has been interpreted as either any reduction in benefits agreed-to at the time of hire or as any increase in employee contributions required to maintain the same level of agreed-to benefits.

Pennsylvania Act 2010-120 did introduce a "risk sharing" provision that allows for an increase in contributions by employees hired on or after January 1, 2011 if there is a multi-year period of investment returns below the assumed rate. An increased employee "shared risk contribution" would be established every three years beginning in 2014. The additional contribution may not increase by more than 0.5% in any three-year period and may not exceed 2% in total.

**SERS Funding**  
(10-Year History)





# Funding Process & Actuarial Status *(continued)*

## Investment Earnings

SERS' overall investment objective is to assure adequate Fund reserves at the least cost to Commonwealth citizens and to provide some protection against the erosion of principal by inflation. SERS seeks to provide investment earnings that meet, or preferably exceed, the actuarial rate of return assumption over complete economic cycles. SERS strives to meet this objective by applying acceptable risk parameters and allocations to investments that are diversified by type, industry, quality, and geography.

Investment earnings can vary widely from year to year; the SERS Fund, for example, produced a nearly 25% return in 2003 and experienced more than a 25% loss in 2008. In order to minimize volatility, Pennsylvania law requires that the differences between actual performance and an assumed rate of return be recognized on SERS' books over a five-year period at a rate of 20% per year – a concept often referred to as “smoothing.” Thus, 2008's losses will continue to negatively impact SERS' unfunded liability through 2012.

SERS examines and sets its assumed rate of return each year based on global market dynamics, investment performance and other considerations. In 2009 SERS reduced its assumed rate of return from 8.5% to 8%, for example, largely as a result of 2008's global economic collapse.

SERS' assumed rate of return is currently at 8%.

### Public Pension Fund Assumed Rates of Return (2011 Public Fund Survey)

Rate	# of Plans Using Rate
7.00%	5
7.25	2
7.50	12
7.75	20
8.00	57 (SERS)
8.25	16
8.50	11

For 11 of the last 16 years, SERS has exceeded assumed rates of return. Moreover, even factoring in recent losses, the SERS Fund has achieved a 20-year compounded rate of return of 8.2% and a 30-year return of 10.2%.

The “shared risk” provision of Act 2010-120, previously discussed, is designed to moderate the need for future employer rate increases that may be prompted by investment underperformance, should it occur.

As of December 31, 2011 the market value of the SERS Fund was \$24.2 billion. Despite this year's economic turbulence, the Fund achieved an estimated return of 2.6%, which places it in the top 80% of similarly situated public pension funds. Nonetheless – because SERS paid \$2.7 billion in benefits in 2011 – the Fund is \$1.7 billion less than at this time in 2010.

The System has more retired members than active members and is paying out approximately \$166 million more each month than it is taking in through employee and employer contributions. SERS' increasing maturity raises the liquidity needs of the Fund and will require that assets be rebalanced to meet the need.

# Funding Process & Actuarial Status *(continued)*

## Employer Contributions

The “employer normal cost” is the amount employers would contribute if all actuarial assumptions were *precisely* correct and the Fund *exactly* achieved its assumed rate of return year over year. Because it is highly unlikely that such a situation could ever occur, Pennsylvania’s State Employees’ Retirement Code requires SERS to adjust the employer contribution rate—expressed as a percentage of payroll—each year based on actual experience and investment performance.

The employer contribution rate is calculated by an independent actuary, taking into account employee contributions, demographic activity, investment earnings and future liabilities.

Based on the actuary’s recommendation and statutory limitations, the SERS board annually certifies an employer contribution rate. The rate has fluctuated dramatically over the years, in 1981 the rate was approximately 18%, for example, but from 2001-03 the rate was 0%.

### 30-Year Snapshot Contrasting Employer & Employee Contributions

	1981	2011
<b>Employer Rate</b>	17.9%	8.0%
<b>Employer Contributions</b>	\$326 million	\$399 million
<b>Employee Rate</b>	5.00%	6.25%
<b>Employee Contributions</b>	\$116 million	\$350 million
<b>Active Employees</b>	117,000	107,000
<b>Annuityants</b>	53,000	115,000

As one would expect, then, the total dollars contributed by employers has varied from year to year. In 1981, employer contributions totaled \$326 million, in 2011 that figure was \$399 million—a nominal dollar-for-dollar increase that would likely be a decrease if adjusted for inflation. As provided by the Budget Office, SERS employers under the Governor’s jurisdiction paid less than half of the employers’ share—about 46%—from general funds. Approximately 22% came from special funds; approximately 15% came from federal funds; and approximately 17% came from other sources.

The employer contribution rate has two parts: the cost to fund the benefits of new SERS members in the current year (as applied to all active members) and a contribution toward SERS’ unfunded liability. When SERS reduced its assumed rate of return from 8.5% to 8% in 2009, the change increased SERS unfunded liability by approximately \$1.6 billion which, in turn, increased future employer contribution rates. As a simplified “rule of thumb,” every 1% change in the assumed rate of return impacts employer rate contribution projections by approximately 7%.

The fiscal year 2012/13 employer contribution is currently legislated to be 11.5% with increases capped at 4.5% each subsequent year. If the contribution were not legislatively capped, the rate would be 22.5%—about 4.1% to fund the benefits of new SERS members in the current year and about 18.4% to pay toward SERS’ unfunded liability.

Because the employer rate will remain below actual cost until at least 2015, SERS’ deficit will continue to grow in the near term. The deficit will grow more slowly, however, each year that the employer rate rises closer to the actual cost.

# Funding Process & Actuarial Status *(continued)*

## Projected Employer Contributions, Payout, and Funding Status

Assuming 6.2% salary growth, 2.75% inflation, 8% investment return and 6.25% employee contribution

Commonwealth Fiscal Year	Expected FY Payroll (\$ millions)	Employer Contribution		Payout**	Funding Status**	
		Employer Contribution Rate	Expected FY Contribution (\$ millions)	Benefits & Expenses (\$ billions)	Funded Ratio	Unfunded Liability (\$ billions)
2012/13*	\$6,030.2	11.5%	\$693.5	\$2.7	69.0%	\$12.5
2013/14	6,214.1	16.0	994.3	2.7	61.7	15.8
2014/15	6,403.6	20.5	1,312.7	2.8	61.2	16.4
2015/16	6,598.9	25.0	1,649.7	2.9	60.5	17.1
2016/17	6,800.2	28.1	1,909.5	3.1	60.1	17.7
2017/18	7,007.6	27.7	1,938.2	3.2	61.0	17.7
2018/19	7,221.3	27.1	1,954.4	3.3	62.2	17.5
2019/20	7,441.6	26.5	1,970.2	3.4	63.4	17.3
2020/21	7,668.6	25.9	1,985.4	3.6	64.6	17.1
2021/22	7,902.5	25.3	2,000.4	3.7	65.8	16.9
2022/23	8,143.5	24.8	2,015.6	3.8	66.9	16.6
2023/24	8,391.9	24.2	2,031.2	3.9	68.1	16.3
2024/25	8,647.8	23.7	2,047.2	4.0	69.3	16.0
2025/26	8,911.6	23.2	2,063.8	4.1	70.5	15.6
2026/27	9,183.4	22.7	2,080.8	4.3	71.7	15.2
2027/28	9,463.5	22.2	2,098.3	4.4	72.9	14.8
2028/29	9,752.1	21.7	2,116.4	4.5	74.2	14.3
2029/30	10,049.5	21.3	2,135.1	4.6	75.4	13.8
2030/31	10,356.1	20.8	2,154.4	4.7	76.8	13.2
2031/32	10,671.9	20.4	2,174.2	4.8	78.1	12.6
2032/33	10,997.4	20.0	2,194.7	4.9	79.6	12.0
2033/34	11,332.8	19.6	2,215.8	5.0	81.0	11.3
2034/35	11,678.5	19.2	2,237.6	5.1	82.6	10.5
2035/36	12,034.7	18.8	2,260.1	5.1	84.2	9.6
2036/37	12,401.7	18.4	2,283.3	5.2	85.9	8.7
2037/38	12,780.0	18.1	2,307.2	5.3	87.7	7.7
2038/39	13,169.8	17.7	2,331.9	5.4	89.6	6.6
2039/40	13,571.4	17.4	2,357.3	5.5	91.5	5.4
2040/41	13,985.4	13.5	1,886.8	5.6	93.6	4.2
2041/42	14,411.9	10.7	1,541.5	5.7	95.1	3.3

\*Assumes an unaudited 2.6% investment return.

\*\*Figures are based upon previous calendar year's actuarial valuation.

# Funding Process & Actuarial Status *(continued)*

## Actuarial Status: Current Funded Position of SERS' Defined Benefit Plan

The "funded position" of a defined benefit plan is measured by its "funded ratio" which is the actuarially calculated value of assets divided by the actuarially calculated sum of retirement benefits earned by all existing SERS members – more than 227,000 active, vested and retired employees.

At the close of 2011, SERS' estimated funded ratio was 69% (actuarial value) or 61% (market value).

SERS funded ratio has varied significantly over time:

	<b>Actuarial Value</b>	<b>Fair (Market) Value</b>
1991	98.7%	109.2%
1996	105.7	116.0
2001	116.3	104.4
2006	92.7	99.6
2011	69.0	61.3

The unfunded liability associated with the 2011 ratio is \$12.5 billion (actuarial value) or \$16.1 billion (market value). As discussed, SERS unfunded liability will grow in the near term, as 2008 losses are recognized and employer contribution rates are suppressed by Pennsylvania law.

Factors influencing the unfunded liability have been building over time, including but not limited to:

- sustained periods of employer contributions below normal costs
- losses that neutralized past investment gains used to justify the low employer contributions
- benefit increases – including cost of living adjustments and increased "accrual rates," for example – without corresponding funding streams
- legislatively mandated actuarial changes that extended the time over which liabilities be paid
- demographic and salary evolution
- cumulative negative impact of the above on the overall size of the Fund and its investment returns

In 2010 the number of employees drawing from the Fund exceeded the number of employees paying into it. Ten years ago, in 2001, monthly payments from the Fund were \$86.0 million, a sum that had grown to \$186.8 million in 2011.

# Funding Process & Actuarial Status *(continued)*

## Additions and Deductions to Plan Net Assets

Calendar Years  
(\$ millions)

Year	Member Contributions	Investment Earnings	Employer Contributions	Benefits and Expenses	Fair (Market) Value
2011 <sup>1/</sup>	\$350	\$264 <sup>2/</sup>	\$399	\$(2,735)	\$24,164
2010	349	3,076	273	(2,474)	25,886
2009	349	3,561	253	(2,297)	24,662
2008	337	(11,061)	235	(2,231)	22,796
2007	334	5,246	244	(2,361)	35,516
2006	318	4,730	196	(1,943)	32,053
2005	306	3,623	148	(1,966)	28,752
2004	310	3,568	107	(1,880)	26,641
2003	308	4,936	68	(1,656)	24,536
2002	304	(2,731)	51	(1,450)	20,880
<b>10 Year Total</b>	<b>\$3,265</b>	<b>\$15,212</b>	<b>\$1,974</b>	<b>\$(20,993)</b>	<b>*</b>

<sup>1/</sup>2011 figures are unaudited.

<sup>2/</sup>Figure does not include 4th quarter earnings for Alternative Investments and Real Estate. Data was not yet available.

\*Ten year net additions and deductions were \$(542).

As indicated, courts have held that retirement benefits earned by members of public pension systems are protected by the United States and Pennsylvania constitutions. Thus, the sum of benefits earned by existing SERS members is a debt that has already been incurred by the Commonwealth.

The State Employee's Retirement Code, Title 71, Pa.C.S. §5951 sets forth that "Statutory interest charges payable, the maintenance of reserves in the Fund and payment of all annuities and other benefits granted by the board under the provisions of this part are hereby made obligations of the Commonwealth. All income, interest, and dividends derived from deposits and investments authorized by this part shall be used for the payment of the said obligations of the Commonwealth."

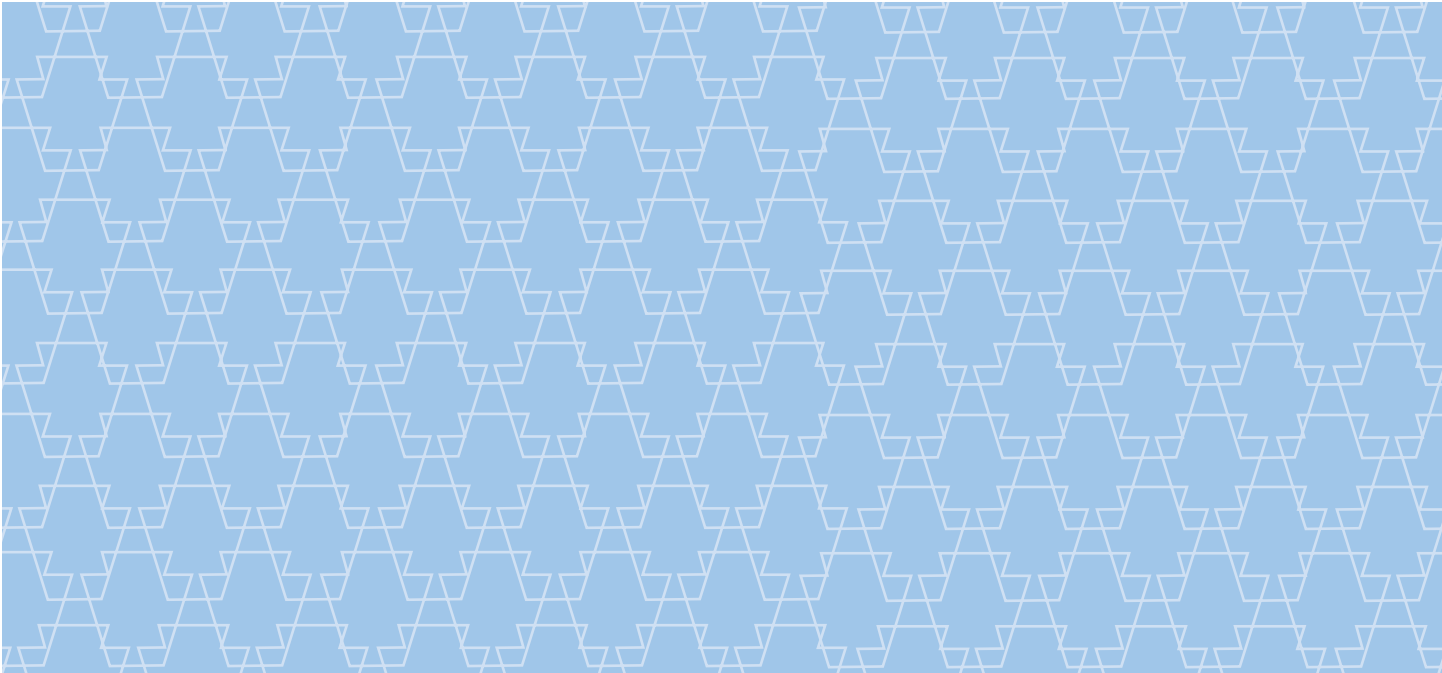
### Actuarial Status: Restoring SERS' Defined Benefit Plan Funding

SERS' unfunded liability is growing more slowly than it otherwise would have been growing because of Act 2010-120 which saves approximately \$1.5 billion over 30 years by reducing the retirement benefit "accrual rate"; increasing the Normal Retirement Age; eliminating the lump sum withdrawal option; extending the vesting period from five years to ten years and other provisions for employees hired on or after January 1, 2011.

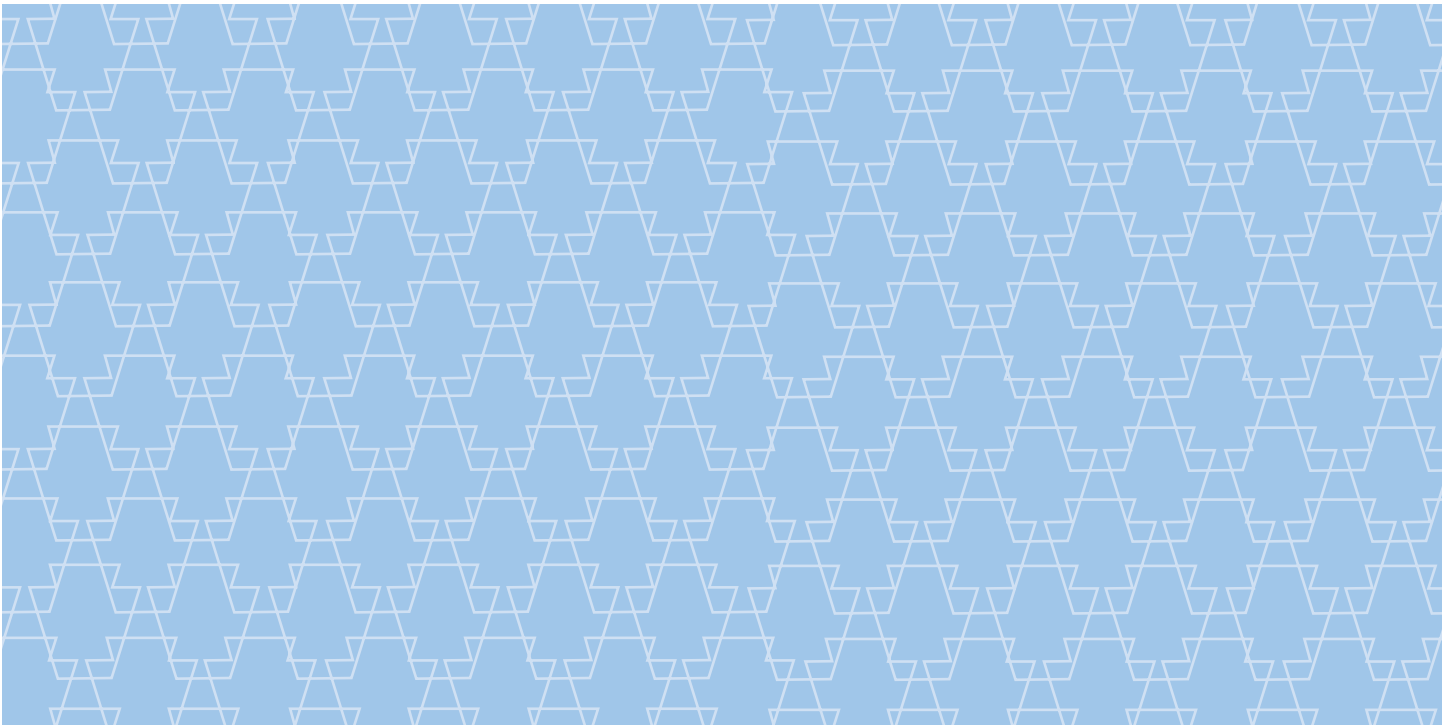
It will, however, take considerable time to realize benefits from the lower costs. SERS' funded ratio will improve as employees hired before January 2011 retire and post-January 2011 hires begin to fill employee ranks in greater proportion.

Act 2010-120 also recognized the need for greater rates of employer funding and does allow employer contributions to increase over time. To ensure predictability and to moderate overall budget impacts, the General Assembly set forth measured intervals for increased employer contribution rates. Often referred to in shorthand as the "Act 120 collars," as previously discussed, the legislation limits future year-to-year increases in employer contributions to 4.5%.

Because the collared employer rate remains below actual cost for a number of years, SERS' deficit will continue to grow in the near term. As the rate increases, however, its impact on paying down the liability is dramatic. Such funding is among the most crucial components of the overall, long-term stability of the pension system. Thus, as Commonwealth employers meet the increases mandated by the General Assembly in Act 2010-120, SERS will again approach full funding in approximately 30 years.



# Investment Policy, Objectives and Performance 8



# Investment Policy

The 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 2009. 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 investors 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 strategic investment plan is prepared to establish the allocation of funds among investment advisors and categories of assets during the year;
- Objectives are established for each category of assets used by the Fund's investment advisors to provide a framework for monitoring quality, diversification and liquidity;
- SERS is committed to promoting and improving good corporate governance practices of companies within the portfolio; 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.

# Investment Objectives

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 for 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 System through investment earnings;
- Achieve in Global Stock a total return that exceeds the total return of the MSCI World Net Dividends Index;
- Achieve in U.S. Stock a total return that exceeds the total return of the Russell 3000 Index;
- Achieve in Non-U.S. Stock a total return that exceeds the total return of the MSCI ACWI ex U.S. IMI Net Index;
- Achieve in the stand alone Absolute Return Strategy a total return that exceeds the 90 Day LIBOR + 300 bps benchmark;
- Achieve in the Fixed Income asset class a total return that exceeds the total return of the SERS Custom Fixed Income Benchmark;
- Achieve in the Real Estate asset class a total return that exceeds the total return of the Townsend Stylized Benchmark;
- Achieve in the Private Equity asset class a total return that exceeds the Russell 3000 Index + 300 bps benchmark;
- Achieve in the Venture Capital asset class a total return that exceeds the Russell 3000 Index + 300 bps benchmark;
- Achieve in Inflation Protection a total return that exceeds the total return of the SERS Custom Inflation Protection Benchmark;
- Achieve in the Cash asset class a total return that exceeds the total return on 3 Month T-bills;

Total return includes income, 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.



# Asset Allocation Trend

## Prudent Investor Investment Standards

The Board's investment authority is governed by the "prudent investor" standard as set forth in Title 71, Pennsylvania Consolidated Statutes, Section 5931(a). Enactment of the "prudent investor" standard in Act 1994-29 and asset/liability studies completed by SERS' general investment consultants and the SERS Investment Staff are the foundation of SERS' investment strategy. With "prudent investor" investment authority, SERS is able to pursue a broader array of investment opportunities that enhance the ability to achieve reasonable rates of return while maintaining risk at acceptable levels.

## Total Fund Asset Allocation

SERS develops an annual strategic investment plan which provides direction for the SERS' investment program. The *2011 Annual Strategic Investment Plan* will be implemented over a period of five years. The Fund's asset allocation strategy will evolve over this timeframe until the long-term targets for each asset category are achieved by the end of the year 2015.

### Asset Allocation (Unaudited)

12/31/2011	Asset Class/Strategy	2015 Long-Term Strategic Asset Allocation
29.1%	Stocks	39.0%
26.2	Alternative Investments	15.0
10.6	Real Estate	8.0
18.5	Fixed Income	26.0
4.2	Inflation Protection	3.0
8.2	Absolute Return	9.0
3.1	Cash	0.0
100.0%		100.0%

*\*Numbers may not add due to rounding.*

# Estimated Investment Performance\*

## Calendar Year Basis

through December 31, 2011 (net of fees)

Asset Class	1 Year Total Return	3 Years Total Return	5 Years Total Return	10 Years Total Return
Global Stock <sup>1/</sup>	-6.4%	15.3%	1.5%	N/A
<i>MSCI World Net Dividends Index</i>	-5.5%	11.1%	-2.4%	N/A
U.S. Stock	-0.3%	14.1%	-2.9%	3.0%
<i>Russell 3000 Index</i>	1.0%	14.9%	0.0%	3.5%
Non-U.S. Stock	-13.8%	11.3%	-5.2%	5.2%
<i>MSCI ACWI ex U.S. IMI Net Index<sup>2/</sup></i>	-14.3%	11.5%	-3.1%	7.3%
Fixed Income	6.1%	16.1%	6.5%	7.2%
<i>SERS Custom Fixed Income Benchmark</i>	7.4%	14.5%	7.1%	7.1%
Absolute Return Strategy <sup>3/</sup>	-1.6%	6.0%	N/A	N/A
<i>90 Day LIBOR + 300 basis points</i>	3.3%	3.5%	N/A	N/A
Cash	0.2%	0.3%	1.9%	2.3%
<i>3 Month T-Bills</i>	0.1%	0.1%	1.5%	2.0%
Real Estate <sup>4/</sup>	10.5%	-7.2%	-2.7%	6.0%
<i>Townsend Stylized Benchmark<sup>5/</sup></i>	13.5%	-6.8%	-1.8%	5.5%
Private Equity <sup>4/</sup>	11.6%	7.6%	10.3%	13.6%
<i>Russell 3000 Index +300 basis points<sup>6/</sup></i>	3.6%	4.5%	2.1%	6.6%
Venture Capital <sup>4/</sup>	18.0%	2.8%	4.8%	-0.9%
<i>Russell 3000 Index +300 basis points<sup>6/</sup></i>	3.6%	4.5%	2.1%	6.6%
Inflation Protection	-6.4%	11.7%	4.8%	10.8%
<i>SERS Custom Inflation Protection Benchmark</i>	-5.2%	9.8%	1.0%	8.6%
<b>Total Fund</b>	<b>2.6%</b>	<b>7.8%</b>	<b>0.9%</b>	<b>6.0%</b>
<b>Total Fund Benchmark</b>	<b>1.0%</b>	<b>10.1%</b>	<b>2.6%</b>	<b>6.5%</b>

\* Returns for periods greater than one year are annualized.

<sup>1/</sup> Global Stock was initially funded in November 2006.

<sup>2/</sup> Represents the current benchmark. Benchmark has changed over time.

<sup>3/</sup> Absolute Return Strategy was initially funded in August 2007.

<sup>4/</sup> Real Estate, Private Equity, Venture Capital and its corresponding benchmark returns are reported on a quarter lag basis.

<sup>5/</sup> The private real estate component of the Townsend Stylized Benchmark is reported net of fees. The public real estate and timber components are reported before fees.

<sup>6/</sup> Interim benchmark recommended by SERS investment consultant and consistent with other comparable state pension plans.

# Estimated Investment Performance\*

## Commonwealth Fiscal Year Basis

through June 30, 2011 (net of fees)

Asset Class	1 Year Total Return	3 Years Total Return	5 Years Total Return	10 Years Total Return
Global Stock <sup>1/</sup>	30.4%	6.0%	N/A	N/A
<i>MSCI World Net Dividends Index</i>	30.5%	0.5%	N/A	N/A
U.S. Stock	32.8%	-2.1%	0.8%	3.1%
<i>Russell 3000 Index</i>	32.4%	4.0%	3.4%	3.4%
Non-U.S. Stock	28.4%	-3.7%	1.5%	6.3%
<i>MSCI ACWI ex U.S. IMI Net Index</i> <sup>2/</sup>	30.3%	0.3%	4.0%	8.0%
Fixed Income	12.9%	9.0%	7.9%	7.5%
<i>SERS Custom Fixed Income Benchmark</i>	8.8%	8.9%	7.9%	7.2%
Absolute Return Strategy <sup>3/</sup>	7.6%	1.3%	N/A	N/A
<i>90 Day LIBOR + 300 basis points</i>	3.3%	3.4%	N/A	N/A
Cash	0.3%	0.9%	2.4%	2.3%
<i>3 Month T-Bills</i>	0.2%	0.4%	2.0%	2.1%
Real Estate <sup>4/</sup>	13.1%	-10.6%	-1.8%	6.1%
<i>Townsend Stylized Benchmark</i> <sup>5/</sup>	18.4%	-9.5%	-1.3%	5.4%
Private Equity <sup>4/</sup>	21.9%	4.4%	12.8%	12.9%
<i>Cambridge Private Equity Index</i>	21.3%	4.3%	10.4%	11.3%
Venture Capital <sup>4/</sup>	18.4%	0.2%	4.2%	-3.4%
<i>Cambridge Venture Capital Index</i>	14.9%	0.3%	4.6%	-3.3%
Inflation Protection <sup>6/</sup>	33.0%	-6.0%	4.0%	N/A
<i>SERS Custom Inflation Protection Benchmark</i>	30.6%	-10.6%	0.0%	N/A
<b>Total Fund</b>	<b>18.8%</b>	<b>-1.4%</b>	<b>3.6%</b>	<b>6.0%</b>
<b>Total Fund Benchmark</b>	<b>18.3%</b>	<b>2.6%</b>	<b>5.6%</b>	<b>6.6%</b>

\* Returns for periods greater than one year are annualized.

<sup>1/</sup> Global Stock was initially funded in November 2006.

<sup>2/</sup> Represents the current benchmark. Benchmark has changed over time.

<sup>3/</sup> Absolute Return Strategy was initially funded in August 2007.

<sup>4/</sup> Real Estate, Private Equity, Venture Capital and its corresponding benchmark returns are reported on a quarter lag basis.

<sup>5/</sup> The private real estate component of the Townsend Stylized Benchmark is reported net of fees. The public real estate and timber components are reported before fees.

<sup>6/</sup> Inflation Protection was initially funded in November of 2001.

# Investment-Related Statistics

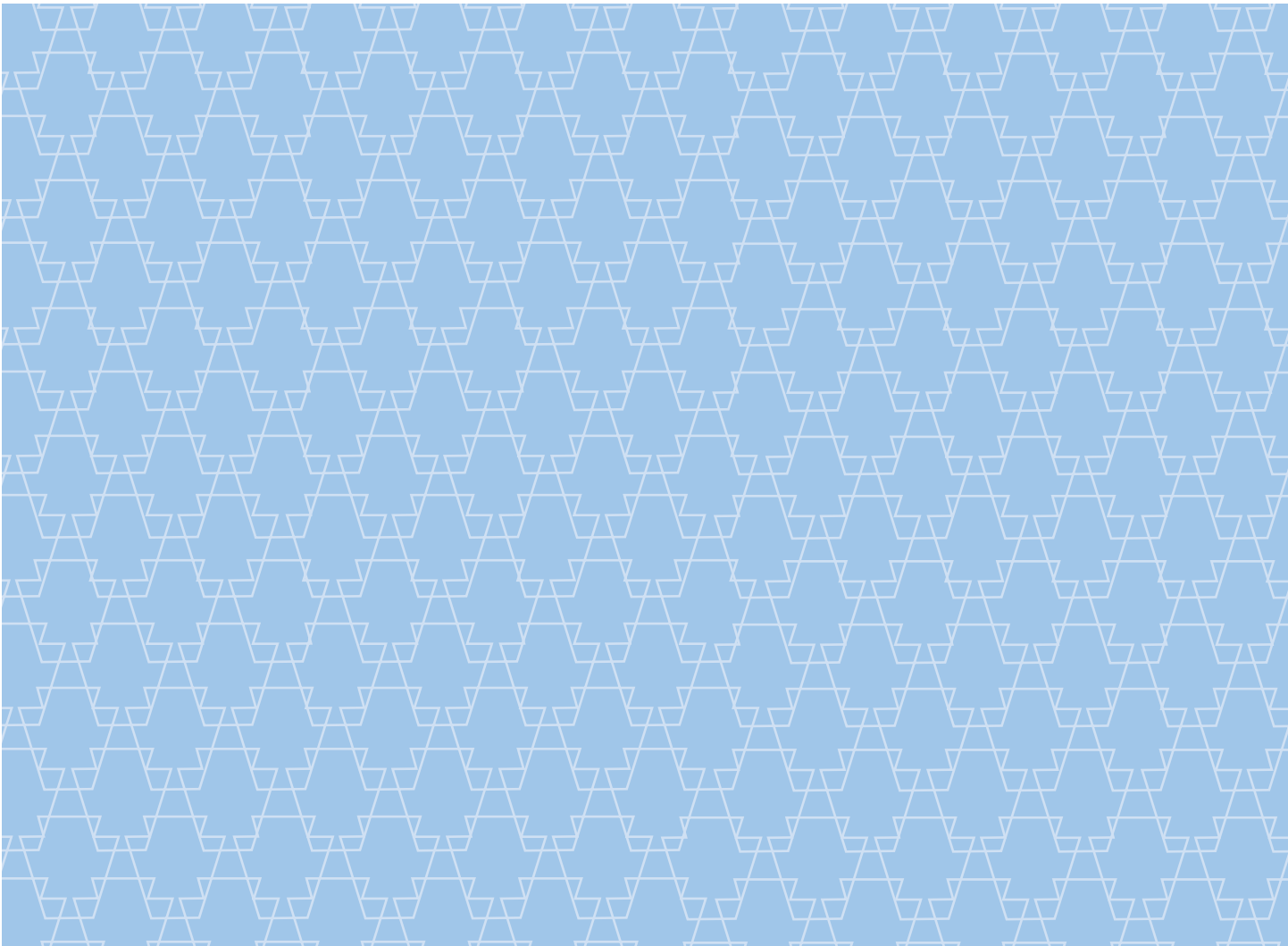
## SERS Investment-Related Statistics Calendar Year 1980 through 2011 (Unaudited)

Year End	SERS Fund Fair Value (\$ millions) <sup>1/</sup>	Annual Total Fund Rate of Return
1980	\$2,689	5.3%
1981	2,817	0.9%
1982	3,730	27.8%
1983	4,396	13.0%
1984	4,922	9.4%
1985	6,157	23.1%
1986	7,120	15.2%
1987	7,367	3.3%
1988	8,312	12.8%
1989	9,785	17.8%
1990	9,886	1.0%
1991	11,940	22.6%
1992	12,453	7.4%
1993	13,701	13.2%
1994	13,330	- 1.1%
1995	16,343	25.2%
1996	18,492	15.9%
1997	21,312	18.0%
1998	24,123	16.3%
1999	28,093	19.9%
2000	27,880	2.2%
2001	24,706	-7.9%
2002	20,880	-10.9%
2003	24,536	24.3%
2004	26,641	15.1%
2005	28,752	14.5%
2006	32,053	16.4%
2007	35,516	17.2%
2008	22,796	-28.7%
2009	24,662	9.1%
2010	25,460	11.9%
2011 <sup>2/</sup>	24,164 <sup>3/</sup>	2.6%

<sup>1/</sup>Fair values for Real Estate and Alternative Investments are lagged by one quarter adjusted for allocations and distributions. Fair values also include non-investment receivables and payables.

<sup>2/</sup>2011 values are estimated.

<sup>3/</sup>Fund fair values for Real Estate and Alternative Investments are lagged by one quarter adjusted for allocations and distributions since 4th quarter values were not available for those asset classes at the time of print.



## Investment Program Summary 9



# Investment Program Summary

as of December 31, 2011 - (Unaudited)

The assets of SERS are administered by the Board. The Board 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. SERS' 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, 2011:** SERS' assets had an unaudited market exposure of approximately \$24.2 billion.

## SERS Asset Allocation

Asset Class/Strategy	Market Exposure* (Unaudited)		2011 Long-Term Target Allocation
	(\$ millions)	%	
Global Stock	\$920.4	3.8%	5.0%
U.S. Stock	3,262.6	13.5	12.5
Non-U.S. Stock	2,846.6	11.8	21.5
Alternative Investments	6,334.0	26.2	15.0
Real Estate	2,561.1	10.6	8.0
Fixed Income	4,469.0	18.5	26.0
Inflation Protection	1,025.5	4.2	3.0
Absolute Return	1,984.6	8.2	9.0
Cash	759.9	3.1	0.0
<b>Total Fund</b>	<b>\$24,163.7</b>	<b>100.0%</b>	<b>100.0%</b>

\*Numbers may not add due to rounding.

**Number of Investment Advisors:** SERS had 212 investment advisors managing multiple portfolios across asset classes.

- 2 Global Stock advisors
- 5 U.S. Stock advisors
- 8 Non-U.S. Stock advisors
- 6 Absolute Return advisors
- 17 Fixed Income advisors
- 1 Cash advisor
- 2 Inflation Protection advisors
- 26 Real Estate advisors
- 56 Venture Capital general partners managing limited partnerships
- 89 Private Equity general partners managing limited partnerships

**Number of Investment Portfolios:** SERS had 458 investment portfolios.

- 2 Global Stock portfolios
- 5 U.S. Stock portfolios and 1 transition manager
- 10 Non-U.S. Stock portfolios
- 6 Absolute Return portfolios
- 21 Fixed Income portfolios
- 1 Cash portfolio
- 2 Inflation Protection portfolios
- 61 Real Estate portfolios
- 121 Venture Capital limited partnership interests
- 229 Private Equity limited partnership interests

# Global Stock Investments Summary

as of December 31, 2011 - (Unaudited)

Global Stock is a component of the stock asset class, one of six 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 Stock 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 Net Dividends Index.

SERS' 2011 Annual Strategic Investment Plan targets a long-term allocation of 5.0% of Fund assets to global stocks.

**Market Exposure as of December 31, 2011:** Global Stock had a \$920.4 million market exposure, 3.8% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with two external investment advisors.

**Type of Investment Portfolios:** As of December 31, 2011, SERS Global Stock allocation was invested in large/mid-capitalization strategies.

## SERS Global Stock Investments

Global Stock Investment Advisor	Investment Style	Market Exposure as of 12/31/11* (\$ millions)
1. Walter Scott & Partners	Growth	\$448.9
2. Marathon-London Global Fund	Contrarian sector relative value	471.5
<b>Total Global Stock Investments</b>		<b>\$920.4</b>

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

# U.S. Stock Investments Summary

as of December 31, 2011 - (Unaudited)

U.S. Stock is a component of the stock asset class, one of six 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 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 for the U.S. Stock component of the stock asset class is to achieve a total return, net of fees, that exceeds the total return of the Russell 3000 Index.

Stock investments may 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).

SERS' 2011 Annual Strategic Investment Plan targets a long-term allocation of 12.5% of assets to U.S. Stock: 10.0% of the Fund to large cap and 2.5% of the Fund to mid/small cap, approximating the composition of the Russell 3000 Index.

The large cap U.S. stocks, benchmarked to the S&P 500 Index, uses index funds and a hedge fund-of-funds investment. The mid/small cap U.S. stocks, benchmarked to the Russell 2500 Index, uses index funds, and active strategies benchmarked to the Russell Midcap Index and the Russell 2500 Index.

**Market Exposure as of December 31, 2011:** U.S. Stock had a \$3.3 billion market exposure, 13.5% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with five external investment advisors.

**Type of Investment Portfolios:** As of December 31, 2011, 10.8% of the total Fund was in large cap U.S. stocks, and 2.7% in mid/small cap U.S. stocks.

## SERS U.S. Stock Investments

U.S. Stock Investment Advisor	Investment Style	Market Exposure as of 12/31/11* (\$ millions)
<b>Large cap</b>		
1. Mellon Capital Management/Russell 1000 Index	Russell 1000 Index	\$2,608.9
2. Robeco Sage Capital	Fund-of-Hedge Funds	1.2
<b>Mid/small cap</b>		
3. Iridian Asset Management	Midcap private business value	200.7
4. Emerald Advisers	Pennsylvania companies	285.8
Mellon Capital Management Custom U.S. Equity	Pennsylvania companies	162.7
<b>Transition Manager</b>		
5. Northern Trust Transition Management	Transition manager	3.3
<b>Total U.S. Stock Investments</b>		<b>\$3,262.6</b>

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



# Non-U.S. Stock Investments Summary

as of December 31, 2011 - (Unaudited)

Non-U.S. Stock is a component of the stock asset class, one of six 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 component of the stock asset class is to achieve a total return, net of fees, that exceeds the total return of the MSCI ACWI ex U.S. IMI Net Index.

SERS' *2011 Annual Strategic Investment Plan* targets a long-term allocation of 21.5% of assets to non-U.S. stocks: 10.6% of the Fund to large/mid cap stocks in developed markets, 1.9% of the Fund to small cap stocks in developed markets, and 9.0% of the Fund to stocks in emerging markets.

The large/mid cap stocks in non-U.S. developed markets, benchmarked to the MSCI EAFE Index (net), uses indexed products and active strategies. The small cap stocks in non-U.S. developed markets, benchmarked to the MSCI EAFE Small Cap Index (net), uses active strategies. The emerging markets stocks allocation is benchmarked to the MSCI Emerging Markets Index (net) and uses an MSCI Emerging Markets Index fund as well as active strategies.

**Market Exposure as of December 31, 2011:** Non-U.S. Stock had a \$2.8 billion market exposure which was 11.8% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with eight external investment advisors.

**Type of Investment Portfolios:** As of December 31, 2011, 7.1% of the total Fund was allocated to large/mid cap stocks in non-U.S. developed markets; 1.4% to small cap stocks in non-U.S. developed markets; and 3.2% to emerging markets.

# Non-U.S. Stock Investments Summary *(continued)*

## SERS Non-U.S. Stock Investments

Non-U.S. Stock Investment Advisor	Investment Style	Market Exposure as of 12/31/11* (\$ millions)
<b>Large/mid cap</b>		
1. Mellon Capital Management MSCI World ex-U.S. Index	MSCI World ex-U.S. Index	\$650.2
2. Artisan Partners	Global ex-U.S. growth	282.4
3. Templeton Investment Counsel	Global ex-U.S. value	468.1
4. Morgan Stanley Investment Management	EAFE value	313.9
<b>Small cap</b>		
5. Harris Associates	Intrinsic value	347.0
6. Pictet Asset Management	Value with growth	2.0
<b>Emerging markets</b>		
7. BlackRock Emerging Markets Index Non-Lendable Fund	MSCI Emerging Markets Index	534.7
8. Vanguard Emerging Markets - Exchange Traded Fund (ETF)	MSCI Emerging Markets Index	146.2
Templeton Strategic Emerging Markets Fund II	Private placements with public companies	16.9
Templeton Strategic Emerging Markets Fund III	Private placements with public companies	85.2
<b>Total Non-U.S. Stock Investments</b>		<b>\$2,846.6</b>

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

# Absolute Return Strategies Investments Summary

as of December 31, 2011 - (Unaudited)

Absolute Return Strategies are used 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 (information ratio). SERS contracts with external fund-of-hedge funds (FOHF) investment advisors to manage these portfolios.

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

SERS' long-term investment objective for the Absolute Return Strategies is to achieve a total return, net-of-fees, that exceeds the 90 Day LIBOR + 300 bps benchmark.

SERS' *2011 Annual Strategic Investment Plan* targets a long-term allocation of 9.0% of Fund assets to Absolute Return Strategies.

**Market Exposure as of December 31, 2011:** Absolute Return Strategies had a \$2.0 billion market exposure, 8.2% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with six external investment advisors.

**Type of Investment Portfolios:** As of December 31, 2011, SERS' Absolute Return Strategies were diversified through many strategies and sub-strategies.

## SERS Absolute Return Strategies Investments

Absolute Return Strategies Investment Advisor	Investment Style	Market Exposure as of 12/31/11* (\$ millions)
1. Arden	Absolute Return	\$245.8
2. Blackstone Alternative Asset Management	Absolute Return	946.0
3. Mesirow	Absolute Return	350.6
4. Morgan Stanley Alternative Investment Partners	Absolute Return	136.4
5. Pacific Alternative Asset Management Company	Absolute Return	111.1
6. Rock Creek	Absolute Return	194.7
<b>Total Absolute Return Strategies</b>		<b>\$1,984.6</b>

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

# Fixed Income Investments Summary

as of December 31, 2011 - (Unaudited)

Fixed Income is one of six 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), provide the Fund with its primary source of liquidity, serve as a hedge against disinflation and/or deflation, and to help diversify the overall Fund.

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 Benchmark which is comprised of the Barclay's Capital Aggregate Index (34.8%), the Custom Intermediate TIPS (20.0%), the Citigroup High Yield Market (22.2%) and JP Morgan Emerging Market Bond indices (23.0%).

SERS' *2011 Annual Strategic Investment Plan* targets a long-term allocation of 26.0% of assets of the total Fund to the Fixed Income asset class. Of this amount, 70.0% is targeted to the core strategies (including global and TIPS) and 30.0% to specialty strategies (high-yield and emerging market debt).

**Market Exposure as of December 31, 2011:** Fixed Income had a \$4.5 billion market exposure, 18.5% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with 17 external investment advisors.

**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 nine actively managed core bond portfolios and one passively managed core fixed income portfolio; one Custom Intermediate Duration Treasury Inflation Protected (TIPS) portfolio, one global TIPS portfolio, two global core portfolios, two US Treasury portfolios, one asset backed security portfolio and one portfolio indexed to Barclay's Capital Aggregate Index and two corporate credit portfolios. The nine actively managed core portfolios totaled \$2.5 billion. The passively managed portfolio was valued at \$419.5 million. The combination of core portfolios represented 65.1% of the asset class.

**Specialty:** The specialty strategy portfolios (high-yield, emerging market debt, subordinated debt, mezzanine debt, and bank loan structured credit) focus on debt instruments offering higher return premiums and different risk characteristics than core fixed income securities. SERS had one corporate high yield portfolio with a market exposure of \$402.0 million, one high yield commercial mortgage-backed securities portfolio with a market exposure of \$250.7 million, one structured credit portfolio with a market exposure of \$125.3 million, four emerging market debt portfolios with a market exposure of \$755.7 million and \$24.5 million of other investments. The specialty portfolios represent 34.9% of the asset class.

# Fixed Income Investments Summary *(continued)*

## SERS Fixed Income Investments

Fixed Income Investment Advisor	Investment Style	Market Exposure as of 12/31/11* (\$ millions)
<b>Core</b>		
1. Brandywine Global	Global Core Fixed	\$162.9
2. Taplin, Canida & Habacht	US Credit	168.6
3. NISA Investment Advisors	Active Intermediate Duration TIPS	1,358.3
4. Ramius Advisors	US Short-term Corporate	105.7
5. Waterfall Asset Management	Asset-backed Securities	125.0
6. Franklin Templeton	Global Core Fixed	73.9
7. Wellington US Treasuries	Domestic Treasuries	149.7
8. PIMCO US Treasuries	Domestic Treasuries	151.7
PIMCO Global TIPS	Global TIPS	195.5
9. BNY Mellon Cash Investment Strategies	Passively Managed Barclay's Aggregate	419.5
<b>Specialty</b>		
10. Berwind - PA Capital Fund	PA Capital Fund (inactive)	2.3
11. Pyramis Global Advisors	Commercial Mortgage-backed Securities	250.7
12. Oaktree Capital Management	Mezzanine Fund (liquidating)	0.4
13. Stone Harbor	Global High Yield	402.0
Stone Harbor	Emerging Market Debt	233.9
14. Ashmore AEMDF	Emerging Market Debt - U.S. dollars	111.1
Ashmore LCD	Emerging Market Debt - local currency	122.6
15. W.R. Huff	High Yield (liquidating)	20.7
16. SEI Structured Credit Fund	High Yield Bank Loans	125.3
17. Greylock Capital Management	Emerging Market Debt (liquidating)	1.1
PIMCO Emerging Market Debt	Emerging Market Debt	288.1
<b>Total Fixed Income Investments</b>		<b>\$4,469.0</b>

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

# Cash Investments Summary

as of December 31, 2011 - (Unaudited)

Cash is one of six major asset classes that SERS uses to diversify the investments of the Fund. Historically, the Cash asset class has been employed by the System to provide for SERS' liquidity needs as well as accumulate funds for future investment.

The asset class emphasizes the use of higher credit quality debt instruments which are liquid and have short maturities and durations, or which have floating rates and have historically been invested in The Pennsylvania State Treasury Department's Short-Term Investment Fund (STIF).

**Investment Objective:** On an asset allocation basis, cash has the lowest expected return of all asset classes. Therefore, since SERS is a long-term investor, the objective is to minimize exposure to this asset and maintain a long-term allocation to the Cash asset class of zero.

Cash payments to meet the Fund's benefit payments and other obligations are sourced through employee and employer contributions, limited partnership distributions, and raising cash from public market managers from time to time. Distributions from limited partnerships are unpredictable and dependent on market conditions and terms of partnership agreements. Accordingly, raising cash from public market equity, fixed income, and fund-of-hedge funds managers is required to meet monthly cash flow requirements.

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 3 Month T-bills.

**Market Exposure as of December 31, 2011:** The effective cash exposure was \$759.9 million or 3.1% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** The cash strategy uses the State Treasury to manage the uninvested cash in the liquidity accounts.

**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 is invested in high-quality, highly liquid, short-term investments.

In the aggregate, the State Treasury managed approximately \$958 million on behalf of SERS and SERS' external investment advisors as of December 31, 2011.

# Real Estate Investments Summary

as of December 31, 2011 - (Unaudited)

Real Estate is one of six 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 investment 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 Townsend Stylized Benchmark for rolling five year periods. SERS' *2011 Annual Strategic Investment Plan* targets a long-term allocation of 8.0% 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
- Development phase

**Fair Value as of December 31, 2011:** Real Estate had \$2.6 billion fair value, 10.6% of the total Fund's \$24.2 billion.

**Number of Investment Advisors:** SERS had contracts with 26 external investment advisors to manage Real Estate portfolios as of December 31, 2011.

**Type of Investment Portfolios:** The most recent property diversification data is as follows:

- 40% pooled funds, 60% separate accounts
- 22% office, 4% industrial, 9% retail, 28% multifamily, 11% hotel, 8% timber, 18% other (including senior and student housing, land and various niche property investments)
- 9% Pennsylvania, 35% East excluding PA, 26% West, 13% South, 5% Midwest, 12% International
- 18% of the fair value of the separate accounts was invested in 14 investments located in Pennsylvania

# Real Estate Investments Summary *(continued)*

## SERS Real Estate Investments

Real Estate Investment Advisor	Vintage Year	Property Type	Investment Structure	Fair Value as of 9/30/11* (\$ millions)
1. AG Asia Realty Fund	2007	Diversified	Limited Partnership	\$17.0
2. Apollo Real Estate Fund III	1998	Diversified	Limited Partnership	5.6
3. Berwind Investment Partnership V	1999	Diversified	Limited Partnership	9.5
Berwind Investment Partnership VI	2002	Diversified	Limited Partnership	10.1
Berwind Investment Partnership VII	2005	Diversified	Limited Partnership	13.3
Berwind Investment Partnership VIII	2007	Diversified	Limited Partnership	10.5
4. Blackstone Real Estate Partners III	1999	Diversified	Limited Partnership	0.5
Blackstone Real Estate Partners IV	2003	Diversified	Limited Partnership	14.8
Blackstone Real Estate Partners V	2006	Diversified	Limited Partnership	52.8
Blackstone Real Estate Partners VI	2007	Diversified	Limited Partnership	82.5
5. CBRE Clarion Real Estate Securities	1996	REITs	Separate Account	259.1
6. Clerestory Small Cap Fund I	2007	Diversified	Limited Partnership	8.7**
7. Colony Investors VIII	2007	Diversified	Limited Partnership	6.2
8. Fidelity Real Estate Opportunistic Income Fund	2007	Debt	Limited Partnership	40.4
9. Fillmore East Fund	2005	Debt	Limited Partnership	7.7
Fillmore West Fund	2008	Debt	Limited Partnership	17.5
10. Forest I.M.A.	1992	Timber	Separate Account	193.1
11. Goldman Sachs Whitehall V & VI	1994	Diversified	Limited Partnership	0.2
Goldman Sachs Whitehall VII & VIII	1996	Diversified	Limited Partnership	0.5
12. Grosvenor I.M.A.	1994	Diversified	Separate Account	316.7
Grosvenor Residential Investment Partners I	2007	Residential	Limited Partnership	15.0
13. Hawkeye Scout Fund I	2006	Diversified	Limited Partnership	67.9
14. Heitman America Real Estate Trust	2007	Diversified	Limited Partnership	106.1
Heitman I.M.A.	1988	Diversified	Separate Account	78.3
15. LaSalle I.M.A.	1994	Diversified	Separate Account	264.3
16. Lowe I.M.A.	1994	Diversified	Separate Account	360.8
17. Lubert Adler Fund II	1998	Diversified	Limited Partnership	0.0
Lubert Adler Fund III	2000	Diversified	Limited Partnership	1.6
Lubert Adler Fund IV	2004	Diversified	Limited Partnership	4.9
Lubert Adler Fund V	2006	Diversified	Limited Partnership	9.4
Lubert Adler Fund VI	2008	Diversified	Limited Partnership	7.3
Lubert Adler Fund VI-A	2010	Diversified	Limited Partnership	1.1
18. OCM Real Estate Opp Fund A	1996	Diversified	Limited Partnership	0.8
OCM Real Estate Opp Fund II	1998	Diversified	Limited Partnership	0.9
OCM Real Estate Opp Fund III	2003	Diversified	Limited Partnership	12.4
19. The Oxford Fund	2006	Diversified	Limited Partnership	17.2



# Real Estate Investments Summary *(continued)*

	Real Estate Investment Advisor	Vintage Year	Property Type	Investment Structure	Fair Value as of 9/30/11* (\$ millions)
20.	Prudential Latin America Residential Fund III	2007	Residential	Limited Partnership	\$20.8
	Prudential Latin America Retail Fund I	2006	Retail	Limited Partnership	23.8
	Prudential Senior Housing Fund II	2001	Senior housing	Limited Partnership	0.4
	Prudential Senior Housing Fund III	2006	Senior housing	Limited Partnership	29.3
21.	Rockpoint Finance Fund I	2006	Diversified	Limited Partnership	1.9
	Rockpoint Real Estate Fund I	2004	Diversified	Limited Partnership	3.0
	Rockpoint Real Estate Fund II	2005	Diversified	Limited Partnership	10.2
	Rockpoint Real Estate Fund III	2007	Diversified	Limited Partnership	33.5
22.	Sentinel Real Estate Fund	1986	Residential	Open-Ended Fund	54.3
23.	Starwood Fund IV	1997	Diversified	Limited Partnership	0.3
	Starwood Fund V	1999	Diversified	Limited Partnership	0.3
	Starwood Fund VI	2001	Diversified	Limited Partnership	17.8
	Starwood Fund VII	2005	Diversified	Limited Partnership	24.8
	Starwood Fund VIII	2007	Diversified	Limited Partnership	45.3
24.	UBS Multi-Family Trust	1999	Residential	Limited Partnership	0.3
	UBS Trumbull Property Fund	1988	Diversified	Open-Ended Fund	75.0
	UBS Trumbull Property Income Fund	1988	Diversified	Open-Ended Fund	70.3
25.	Urdang Real Estate Securities	2002	REITs	Separate Account	58.0
26.	Westbrook Fund II	1997	Diversified	Limited Partnership	0.4
	Westbrook Fund III	1998	Diversified	Limited Partnership	2.9
	Westbrook Fund IV	2000	Diversified	Limited Partnership	0.2
	Westbrook Fund V	2004	Diversified	Limited Partnership	1.1
	Westbrook Fund VI	2005	Diversified	Limited Partnership	9.8
	Westbrook Fund VII	2006	Diversified	Limited Partnership	40.9
	Westbrook Fund VIII	2009	Diversified	Limited Partnership	23.1
<b>September 30, 2011 Real Estate Total</b>					<b>2,562.3</b>
Fourth Quarter Net Cash Flow Adjustment					(1.2)
<b>December 31, 2011 Real Estate Total</b>					<b>\$2,561.1</b>

\*Fair values are lagged by one quarter due to the timing of the receipt of private market valuations and information. Numbers may not add due to rounding.

\*\*Value shown is as of 6/30/11 adjusted for third quarter cash flows.

# Alternative Investments Summary

as of December 31, 2011 - (Unaudited)

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

## Private Equity and Venture Capital Defined

Private Equity primarily refers to investments in the equity and subordinated debt of established companies. Private equity approaches undertaken by SERS' limited partnerships include three types: (1) Leveraged buyouts and management buyouts, (2) Distressed debt investing, and (3) Secondary interests in established private equity funds. Leveraged buyouts and management buyouts involve companies 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. Distressed debt investing involves: deleveraging debt-laden but successful companies, by infusing capital to permit debt reduction in exchange for an equity stake in the company; or acquiring the 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. Secondary interests in established private equity funds 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.

Venture Capital is the financing of young, rapidly growing companies, typically at three stages of development: (1) seed and early stage, (2) late and later stage, and (3) growth or expansion stage. Seed financing supports companies in their conceptual phase, when 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. For instance, when a product has been developed and may have been shipped to customers for testing, and when management positions have been filled and an operating team is in place. Late and later stage financing supports companies that have proven revenues, and are in the process of rolling out operations and building sales to achieve profitability. Growth or expansion stage 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.

**Investment Objective:** SERS' long term investment objective for Alternative Investments is to achieve a total return, net of fees, in excess of the return generated by the Russell 3000 Index + 300 bps. SERS' *2011 Annual Strategic Investment Plan* targeted an Alternative Investment long-term allocation range with a midpoint of 15.0%.

**Fair Value as of December 31, 2011:** Alternative Investments had \$6.3 billion fair value after adjusting the September 30, 2011 valuation for subsequent cash flows in the fourth quarter. Alternative Investments constitutes 26.2% of the total Fund's \$24.2 billion. 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	\$365.4	\$1,749.2	7.2%
Private Equity	1,388.6	4,584.8	19.0
<b>Total Alternative Investments</b>	<b>\$1,754.0</b>	<b>\$6,334.0</b>	<b>26.2%</b>

**Number of Limited Partnerships:** As of December 31, 2011, SERS had commitments to 350 active Alternative Investments limited partnerships, 229 to Private Equity partnerships and 121 to Venture Capital partnerships.

# Alternative Investments Summary *(continued)*

**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 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, cross-border business opportunities within the region since the formation of the European 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 fund-of-funds. Additionally, SERS utilizes one manager to oversee stock distributions and another manager for co-investment opportunities.

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. Six 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.

**Alternative Investment Portfolio Exposure:** The Alternative Investment Program is well-diversified by stage of investment, industry focus, and geography. As of September 30, 2011, based on fair value, the Program's exposure was as follows:

<b>By Fund Sub Sector:</b>	<b>By Portfolio Company Geography:</b>	<b>By Portfolio Company Industry:</b>
U.S. Private Equity 40.5%	United States 66.3%	Information Technology 19.8%
U.S. Venture Capital 24.4	United Kingdom 6.0	Consumer Discretionary 18.8
Non-U.S. <sup>1/</sup> 21.7	France 2.7	Financials 18.6
Distressed/Opportunistic 9.6	Italy 2.5	Health Care 14.5
Pennsylvania Related 3.9	Germany 2.3	Industrials 11.3
	China 2.1	Energy 4.7
	Canada 1.6	Materials 3.4
	Rest of World 16.5	Consumer Staples 3.2
		Telecommunication Svcs 3.0
		Other 2.7

<sup>1/</sup> Some managers with a domestic investment focus may invest globally. Thus, Non-U.S. exposure measured on a portfolio company basis will be greater.

# Venture Capital Committed, Drawn and Distributed

as of September 30, 2011 - (Unaudited)

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 capital and profits returned to SERS.

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed*	Capital Drawn	Distributions
1. ABS Capital Partners VI	Later Stage	3/13/2009	\$40,000,000	\$32,132,843	\$2,975,636
2. Adams Capital Management II	Early Stage	10/1/1999	30,000,000	30,000,000	2,600,000
Adams Capital Management III	Early Stage	11/21/2000	30,000,000	30,000,000	4,761,905
3. Advanced Technology Ventures VI	Multi-Stage	3/9/2000	10,000,000	10,000,000	3,472,939
Advanced Technology Ventures VII	Multi-Stage	7/11/2001	27,000,000	25,784,700	12,304,127
4. Alloy Annex I	Seed/Early Stage	10/31/2003	5,000,000	5,000,000	0
Alloy Ventures 2000	Early Stage	5/19/2000	20,000,000	20,000,000	2,674,620
Alloy Ventures 2002	Early Stage	7/22/2002	25,000,000	25,000,000	5,604,706
Alloy Ventures 2005	Seed/Early Stage	8/11/2005	25,000,000	25,000,000	0
5. Apax Excelsior VI	Later Stage	7/3/2000	35,000,000	34,151,324	45,811,535
P/A Fund I	Later Stage	6/30/1993	30,000,000	30,000,000	66,195,539
P/A Fund III	Later Stage	3/31/1997	100,000,000	100,000,000	161,557,955
6. APEX Investment Fund IV	Early Stage	9/17/1999	25,000,000	25,748,664	2,303,927
APEX Investment Fund V	Early Stage	4/19/2002	20,000,000	20,534,571	4,775,986
7. Artiman Ventures II	Seed/Early Stage	10/27/2006	25,000,000	20,375,000	0
Artiman Ventures III	Seed/Early Stage	8/9/2010	20,000,000	2,750,000	0
8. Atlas Venture Fund IV	Early Stage	3/31/1999	26,000,000	23,809,496	8,042,039
Atlas Venture Fund V	Early Stage	2/7/2000	37,200,000	37,211,109	37,844,709
Atlas Venture Fund VI	Early Stage	8/1/2001	24,800,000	24,800,000	6,517,283
9. Austin Ventures VIII	Early Stage	7/26/2001	15,000,000	13,213,466	881,830
Austin Ventures IX	Early Stage	1/9/2006	20,932,140	21,652,612	7,675,945
10. Battery Ventures VIII	Diversified	8/13/2007	25,000,000	22,328,333	966,667
11. Birchmere Ventures III	Early Stage	5/5/2005	10,000,000	9,402,750	4,397,555
12. Care Capital Investments III	Middle/Later Stage	2/8/2006	25,000,000	14,831,108	109,214
13. Charles River Partnership XI	Early Stage	2/15/2001	11,032,259	10,858,417	14,360,660
14. Clearstone Venture Partners III-A	Early/Late Stage	12/22/2004	25,000,000	23,000,000	267,818
15. Cross Atlantic Technology Fund	Early Stage	2/14/2000	20,000,000	20,149,041	21,722,142
Cross Atlantic Technology Fund II	Early Stage	1/28/2002	32,900,000	32,900,000	18,871,600
Novo Vita	Early Stage	12/26/2000	11,616,498	11,616,498	5,377,593
16. Devon Park Bioventures	Early/Late Stage	12/15/2006	10,842,697	5,821,908	701,849
17. Draper Fisher Jurvetson Fund VI	Early Stage	8/13/1999	8,000,000	8,000,000	3,820,841
Draper Fisher Jurvetson Fund VII	Early Stage	9/22/2000	20,000,000	20,000,000	3,178,088
18. Draper Triangle Ventures	Early Stage	12/20/1999	20,000,000	20,431,137	10,505,577
Draper Triangle Ventures II	Early Stage	10/13/2004	12,000,000	11,651,287	696,538
19. Fairview Capital	Fund of Funds	9/30/1994	10,000,000	10,000,000	4,543,128
Fairview II	Fund of Funds	3/31/1998	10,000,000	9,870,000	3,865,556

# Venture Capital Committed, Drawn and Distributed *(continued)*

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed*	Capital Drawn	Distributions
20. Frazier Healthcare III	Early Stage	3/31/1999	\$30,000,000	\$30,000,000	\$10,337,350
Frazier Healthcare IV	Early Stage	9/27/2001	30,000,000	29,595,000	15,550,752
Frazier Healthcare V	Early/Late Stage	5/10/2005	30,000,000	28,530,000	17,546,962
21. Grotech PA III	Later Stage	6/29/1990	3,000,000	3,014,865	2,910,452
Grotech Partners V	Later Stage	9/30/1998	25,000,000	25,000,000	24,521,934
22. Guggenheim Technology Ventures I	Early/Late Stage	11/17/2008	2,000,000	1,560,000	297,134
23. Halpern Denny Fund III	Later Stage	4/26/2000	25,000,000	24,937,500	26,653,673
24. HarbourVest Partners VI	Fund of Funds	5/7/1999	200,000,000	194,586,055	142,782,053
HarbourVest Partners VII	Fund of Funds	3/24/2003	75,000,000	66,000,000	14,664,375
HarbourVest Partners VIII	Fund of Funds	10/5/2006	100,000,000	70,500,000	3,981,490
25. Healthcare Ventures III	Early Stage	9/30/1992	15,000,000	15,000,000	31,427,147
Healthcare Ventures V	Early Stage	12/31/1997	25,000,000	25,000,000	52,355,501
Healthcare Ventures VI	Early Stage	6/19/2000	35,000,000	35,000,000	3,481,797
Healthcare Ventures VII	Early Stage	10/29/2002	35,000,000	33,337,500	8,413,883
Healthcare Ventures VIII	Early Stage	8/22/2005	30,000,000	20,325,000	6,873,126
26. Highland Capital Partners VI	Early Stage	10/25/2001	25,000,000	25,000,000	23,621,783
Highland Capital Partners VII	Early Stage	10/13/2006	35,000,000	27,737,500	3,547,906
Highland Consumer Fund I	Diversified	5/4/2007	25,000,000	15,263,199	0
27. I.P. II	Early Stage	12/17/2001	8,600,000	8,584,074	1,126,082
I.P. III	Seed/Early Stage	11/19/2004	10,500,000	9,030,000	1,976,373
I.P. IV	Seed/Early Stage	9/21/2007	14,000,000	8,960,000	1,694,588
28. Insight Venture Partners VI	Buyouts	8/21/2007	30,000,000	29,591,209	4,539,423
Insight Venture Partners VII	Buyouts	4/27/2011	20,000,000	4,120,000	0
29. InterWest Partners VIII	Early Stage	8/25/2000	20,000,000	15,000,000	1,106,563
InterWest Partners IX	Early Stage	10/19/2005	25,000,000	25,000,000	7,990,495
InterWest Partners X	Early Stage	10/30/2008	30,000,000	12,000,000	0
30. J.H. Whitney Equity Fund III	Later Stage	3/31/1998	20,000,000	20,171,316	50,600,435
J.H. Whitney IV	Later Stage	2/1/2000	20,000,000	17,958,772	6,867,894
31. JMI Equity Fund V	Early/Late Stage	6/7/2005	24,000,000	23,117,205	29,478,324
JMI Equity Fund VI	Early/Late Stage	6/27/2007	40,000,000	37,080,000	0
JMI Equity Fund VII	Growth Equity	2/14/2011	10,000,000	2,370,000	0
32. JP Morgan Venture Capital Investors	Fund of Funds	7/8/1999	100,000,000	105,670,543	46,578,470
JP Morgan Venture Capital Investors II	Fund of Funds	9/8/2000	100,000,000	106,475,420	40,648,676
JP Morgan Venture Capital Investors III	Fund of Funds	6/20/2006	100,000,000	74,718,758	6,588,760
33. Keystone V	Later Stage	3/31/1998	25,000,000	25,000,000	2,157,117
34. Kline Hawkes Pacific	Early Stage	8/30/2000	15,000,000	15,100,498	5,089,301
35. Knightsbridge Venture Capital VI	Fund of Funds	12/7/2004	20,000,000	16,466,667	0
36. Lightspeed Venture Partners VII	Early Stage	2/27/2006	18,000,000	15,577,490	3,199,006
Lightspeed Venture Partners VIII	Early Stage	6/27/2008	15,000,000	9,900,000	0
37. Meritech Capital Partners II	Later Stage	1/2/2001	26,475,166	24,577,777	26,889,124
Meritech Capital Partners III	Later Stage	4/5/2006	35,000,000	33,950,000	16,936,663
Meritech Capital Partners IV	Later Stage	2/10/2011	20,000,000	3,900,000	0

# Venture Capital Committed, Drawn and Distributed *(continued)*

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed*	Capital Drawn	Distributions
38. Mid-Atlantic Venture Fund III	Early Stage	6/30/1997	\$20,008,308	\$20,000,000	\$5,654,702
Mid-Atlantic Venture Fund IV	Early Stage	5/4/2000	30,000,000	30,000,000	1,835,977
NEPA Venture-II	Early Stage	12/31/1992	7,500,000	7,500,000	34,879,769
39. Morgenthaler Partners VII	Early Stage	7/26/2001	20,000,000	7,000,000	434,724
Morgenthaler Partners VIII	Diversified	10/3/2005	35,000,000	35,000,000	20,307,380
Morgenthaler Partners IX	Early Stage	11/25/2008	35,000,000	28,700,000	7,396,904
40. New Enterprise Associates VI	Early Stage	3/31/1994	25,000,000	25,000,000	200,407,487
New Enterprise Associates VII	Early Stage	12/31/1996	30,000,000	30,000,000	102,186,705
New Enterprise Associates IX	Early Stage	11/15/1999	20,000,000	19,600,000	4,836,176
New Enterprise Associates X	Early/Late Stage	12/11/2000	35,000,000	34,503,000	26,419,301
New Enterprise Associates 11	Early/Late Stage	3/1/2004	25,000,000	23,500,000	13,734,534
New Enterprise Associates 12	Early/Late Stage	6/26/2006	35,000,000	30,104,833	4,156,464
41. NewSpring Growth Capital II, L.P.	Later Stage	12/5/2006	10,000,000	6,500,000	517,229
42. Novitas Capital III	Early Stage	4/17/2003	10,000,000	8,700,000	1,414,938
43. Oak Investment Partners XI	Later Stage	7/21/2004	35,000,000	35,000,000	12,516,412
Oak Investment Partners XII	Early/Late Stage	7/10/2006	40,000,000	36,710,052	5,448,813
44. Polaris Venture Partners II	Early Stage	9/30/1998	25,000,000	24,750,000	28,400,176
Polaris Venture Partners III	Early Stage	1/21/2000	50,000,000	49,500,000	20,831,679
Polaris Venture Partners IV	Early Stage	9/30/2002	50,000,000	49,750,000	12,723,022
Polaris Venture Partners V	Diversified	8/8/2006	50,000,000	39,750,000	2,821,500
45. Quaker BioVentures	Early Stage	2/20/2003	20,000,000	20,000,000	3,526,430
Quaker BioVentures II	Middle/Later Stage	4/3/2007	25,000,000	13,500,000	1,083,269
46. Sofinnova Venture Partners VII	Early Stage	1/18/2007	20,000,000	13,400,000	5,672,924
47. Sprout VII	Early Stage	3/31/1995	18,000,000	18,000,000	47,498,519
48. Summit Accelerator Fund	Early Stage	11/15/1999	8,000,000	7,609,500	12,168,635
Summit Partners VC Fund II	Diversified	9/22/2006	15,000,000	12,600,000	5,315,560
Summit IV	Later Stage	9/30/1995	25,000,000	24,250,000	182,806,450
Summit V	Later Stage	3/31/1998	37,500,000	36,187,500	49,099,944
49. T.Rowe Price Stock Distribution Acct.	Public Stock	1/3/2005	0	378,864,639	362,182,020
50. TA/ Advent VIII	Later Stage	6/30/1997	30,000,000	29,400,000	66,756,735
51. Three Arch Capital	Early Stage	12/20/2000	20,000,000	19,500,000	4,800,979
Three Arch Partners IV	Early/Late Stage	6/4/2004	20,000,000	17,550,000	4,484,378
52. TL Ventures III	Early Stage	3/31/1997	15,000,000	15,062,614	20,677,658
TL Ventures IV	Early Stage	5/13/1999	35,000,000	35,000,000	25,582,809
TL Ventures V	Early Stage	10/18/2000	40,000,000	40,048,219	11,510,535
53. US Venture Partners VII	Early Stage	2/18/2000	13,750,000	13,750,000	4,800,279
US Venture Partners VIII	Early Stage	6/1/2001	26,250,000	25,830,000	11,434,063
54. Weathergage Venture Capital	Fund of Funds	6/26/2007	25,000,000	15,250,000	559,887
Weathergage Venture Capital II	Fund of Funds	6/29/2010	25,000,000	3,750,000	0



# Venture Capital Committed, Drawn and Distributed *(continued)*

Active Venture Capital Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed*	Capital Drawn	Distributions
55. Weston Presidio III	Later Stage	12/31/1998	\$35,000,000	\$31,989,586	\$26,056,409
Weston Presidio IV	Later Stage	6/21/2000	35,000,000	34,451,015	26,420,992
Weston Presidio V	Later Stage	12/8/2005	50,000,000	39,378,129	21,129,987
56. Worldview Technology Partners IV	Early Stage	1/31/2001	18,130,023	16,951,175	6,562,490
<b>Total Active Venture Capital</b>			<b>\$3,478,037,091</b>	<b>\$3,506,620,874</b>	<b>\$2,518,874,963</b>

\*Commitments as of 12/31/11  
Cash flows as of 9/30/11

## Inactive Venture Capital Funds

Limited Partnership	Capital Committed	Capital Drawn	Distributions
<b>Total Inactive Venture Capital</b>	<b>\$279,700,000</b>	<b>\$268,938,557</b>	<b>\$508,661,021</b>

# Private Equity Committed, Drawn and Distributed

as of September 30, 2011 - (Unaudited)

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 capital and profits returned to SERS.

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
1. Abingworth Bioventures IV	Multi-Stage	9/1/2003	\$20,000,000	\$18,240,000	\$6,392,877
Abingworth Bioventures V	Multi-Stage	1/23/2007	33,775,000	17,690,794	1,866,550
2. ABRY Advanced Securities Fund	Senior Debt	8/1/2008	25,000,000	21,069,030	3,241,798
ABRY Mezzanine Partners	Mezzanine	3/15/2002	30,000,000	26,588,202	42,560,109
ABRY Senior Equity II	Private Equity	7/27/2006	30,000,000	27,198,413	21,325,113
ABRY Broadcast Partners III	Buyouts	2/7/1997	25,000,000	22,641,544	22,326,867
ABRY Partners IV	Buyouts	3/30/2001	35,000,000	25,119,146	37,459,148
ABRY Partners V	Buyouts	7/29/2005	45,000,000	40,563,642	63,056,017
ABRY Partners VI	Mid Market Buyouts	3/26/2008	50,000,000	41,063,330	8,462,040
ABRY Partners VII	Mid Market Buyouts	8/10/2011	30,000,000	4,129,860	24,886
3. ABS Capital Partners III	Buyouts	3/26/1999	35,000,000	29,428,915	18,465,307
ABS Capital Partners IV	Buyouts	10/13/2000	35,000,000	30,984,280	60,238,422
ABS Capital Partners V	Buyouts	11/14/2005	20,000,000	19,627,560	5,513,338
4. Accel Europe	Early Stage	7/2/2001	15,000,000	11,350,000	10,425,733
5. Advent International GPE VI-A	Mid Market Buyouts	7/7/2008	35,000,000	20,212,500	1,050,000
Advent Latin American PE Fund IV	Buyouts	8/2/2007	30,000,000	26,100,000	10,492,308
Advent Latin American PE Fund V	Buyouts	5/17/2010	15,000,000	3,000,000	0
6. AG Capital Recovery Partners IV	Distressed Debt	2/4/2003	50,000,000	35,415,216	55,777,537
AG Capital Recovery Partners V	Distressed Debt	4/17/2006	20,000,000	20,000,000	15,640,000
7. Alpha Private Equity Fund 4	Mid Market Buyouts	5/15/2002	26,508,000	35,605,050	74,703,236
Alpha Private Equity Fund 5	Mid Market Buyouts	4/1/2006	57,796,800	65,860,055	7,067,686
8. APAX Europe IV	Buyouts	3/31/1999	32,424,000	29,909,800	38,420,276
APAX Europe V	Buyouts	4/27/2001	53,262,000	70,385,477	138,669,512
APAX Europe VI	Buyouts	5/19/2005	76,349,190	75,559,000	51,579,928
APAX Europe VII	Buyouts	6/27/2007	132,170,235	111,526,875	17,651,434
9. Apollo Investment Fund IV	Buyouts	9/30/1998	75,000,000	74,838,620	120,169,059
Apollo Investment Fund V	Buyouts	8/23/2001	50,000,000	46,528,159	103,913,739
Apollo Investment Fund VI	Buyouts	7/19/2006	40,000,000	35,967,640	5,203,256
10. Asia Alternatives Capital Partners	Fund of Funds	6/26/2007	50,000,000	21,102,350	4,899,418
Asia Alternatives Capital Partners II	Fund of Funds	3/7/2008	50,000,000	9,165,897	1,048,262
Asia Alternatives Korea Buyout Investors	Buyouts	7/22/2011	7,000,000	1,007,445	0
11. Asia Pacific Growth Fund III	Global Situations	9/28/1999	15,000,000	15,314,778	12,712,967
12. Audax Private Equity Fund	Mid Market Buyouts	5/25/2000	35,000,000	36,839,098	52,347,295
Audax Private Equity Fund II	Mid Market Buyouts	6/17/2005	25,000,000	25,517,169	18,513,263
Audax Private Equity Fund III	Mid Market Buyouts	11/7/2007	37,000,000	34,426,518	6,036,240



# Private Equity Committed, Drawn and Distributed *(continued)*

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
13. Avenue Special Situations Fund IV	Distressed Debt	3/27/2006	\$50,000,000	\$50,000,000	\$62,882,608
Avenue Special Situations Fund V	Distressed Debt	6/4/2007	70,000,000	70,004,050	85,833,191
Avenue Special Situations Fund VI	Distressed Debt	11/2/2010	20,000,000	15,210,238	356,781
Avenue Asia Special Situations Fund IV	Distressed Debt	6/30/2006	50,000,000	31,897,973	10,374,296
Avenue Europe Special Situations Fund	Distressed Debt	7/30/2008	38,632,500	25,749,356	15,602,519
14. AXA Secondary Fund III	Secondaries	11/19/2004	26,000,000	21,361,892	30,216,994
AXA Secondary Fund III-2	Secondaries	11/24/2004	14,000,000	11,457,704	15,230,948
AXA Secondary Fund IV	Secondaries	2/26/2007	80,000,000	54,061,079	5,482,886
15. B III Capital Partners	Distressed Debt	9/30/1997	35,000,000	34,503,390	50,522,576
16. Bain Capital Asia Fund	Distressed Debt	10/18/2007	12,000,000	8,880,000	1,224,024
Bain Capital Fund VIII-E	Buyouts	12/15/2004	12,144,000	12,874,983	7,276,653
Bain Capital Europe III	Buyouts	7/10/2008	72,432,276	32,751,600	3,438,359
Bain Capital Fund VII	Buyouts	7/6/2000	25,000,000	25,000,000	43,679,933
Bain Capital Fund IX	Buyouts	4/10/2006	75,000,000	73,354,725	19,699,320
Bain Capital IX Coinvestment Fund	Buyouts	4/20/2006	90,000,000	58,950,000	5,700,167
Bain Capital Fund X	Buyouts	1/15/2008	15,000,000	14,550,000	3,182,465
Bain Capital X Coinvestment Fund	Buyouts	7/28/2008	5,000,000	700,000	16,957
Sankaty Credit Opportunities III	Distressed Debt	3/8/2007	50,000,000	50,000,000	563,636
Sankaty Credit Opportunities IV	Distressed Debt	7/15/2008	40,000,000	32,000,000	12,576,141
17. Baring India Private Equity Fund III Limited	Mid Market Buyouts	10/10/2008	5,000,000	1,210,764	261,932
Baring Vostok Private Equity Fund IV	Buyouts	3/10/2008	30,000,000	17,702,342	1,163,149
18. Battery Ventures VIII Side Car Fund	Diversified	8/29/2008	9,000,000	6,175,620	0
19. BC European Capital VII	Buyouts	7/28/2000	32,658,500	37,754,746	89,454,462
BC European Capital VII Top Up	Buyouts	7/2/2001	10,046,300	12,278,596	29,500,234
BC European Capital VIII	Buyouts	12/13/2005	98,107,500	93,818,169	22,122,390
BC European Capital IX	Buyouts	9/16/2011	26,472,535	2,390,370	0
20. Berkshire Fund VI	Mid Market Buyouts	7/11/2002	20,000,000	18,438,444	23,103,859
Berkshire Fund VII	Mid Market Buyouts	11/15/2006	32,000,000	25,112,525	4,686,884
Berkshire Fund VIII	Mid Market Buyouts	8/25/2011	30,000,000	1,136,046	0
21. Blackstone Capital II	Buyouts	9/30/1994	40,000,000	42,867,958	96,976,257
Blackstone Capital III	Buyouts	11/3/1997	75,000,000	77,288,491	154,478,924
Blackstone Capital IV	Buyouts	2/26/2003	75,000,000	66,247,334	115,891,754
Blackstone Capital Partners V	Buyouts	5/30/2006	150,000,000	141,458,731	13,504,958
Blackstone Communications Partners I	Buyouts	8/29/2000	25,000,000	24,857,336	21,936,068
22. Brait IV	Mid Market Buyouts	12/11/2006	25,000,000	17,705,383	2,540,477
23. Brynwood Partners V	Mid Market Buyouts	7/31/2005	10,000,000	10,308,189	9,936,670
Brynwood Partners VI	Mid Market Buyouts	10/13/2009	10,000,000	5,014,825	31,620
24. Centerbridge Capital Partners I	Distressed Debt	2/27/2007	50,000,000	51,866,490	30,030,458
25. Cerberus Institutional Partners	Distressed Debt	3/5/1999	35,000,000	35,000,000	77,271,105
Cerberus Institutional Partners Series Two	Distressed Debt	10/9/2001	35,000,000	30,100,793	73,856,044
Cerberus Institutional Partners Series Three	Distressed Debt	11/13/2003	35,000,000	22,321,354	21,613,112
Cerberus Institutional Partners Series Four	Distressed Debt	11/27/2006	75,000,000	64,366,694	0
26. Charterhouse Capital Partners VII	Buyouts	1/17/2003	61,145,000	54,236,275	94,038,529
Charterhouse Capital Partners VIII	Buyouts	4/19/2006	73,374,000	69,667,224	0
Charterhouse Capital Partners IX	Buyouts	4/28/2009	66,385,000	26,476,326	0

# Private Equity Committed, Drawn and Distributed *(continued)*

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
27. Charterhouse Equity Partners III	Buyouts	12/31/1997	\$50,000,000	\$55,395,586	\$75,000,205
28. Chequers Capital XV	Buyouts	7/5/2006	26,000,000	31,873,049	934,078
29. CID Greater China Venture Capital Fund II	Early Stage	8/10/2007	20,000,000	16,800,000	5,922,676
30. Clayton Dubilier & Rice V	Buyouts	6/30/1995	50,000,000	49,756,029	49,826,483
Clayton Dubilier & Rice VI	Buyouts	12/31/1998	50,000,000	36,211,768	55,410,949
31. Clessidra Capital Partners II	Buyouts	11/5/2008	20,000,000	5,650,222	2,242,896
32. Code Hennessy & Simmons	Mid Market Buyouts	9/28/1989	10,000,000	9,650,000	29,444,933
Code Hennessy & Simmons III	Mid Market Buyouts	9/30/1997	40,000,000	38,724,000	56,329,887
Code Hennessy & Simmons IV	Mid Market Buyouts	9/16/1999	100,000,000	100,000,000	154,943,496
Code Hennessy & Simmons V	Mid Market Buyouts	11/10/2005	50,000,000	46,792,612	7,514,723
33. Cognetas Fund II	Buyouts	11/2/2005	49,707,800	43,502,715	2,854,538
34. CVI Global Value Fund	Distressed Debt	2/23/2007	60,000,000	57,151,667	9,586,429
35. DLJ Merchant Banking Fund II	Buyouts	3/31/1997	75,000,000	83,261,423	103,859,860
DLJ Merchant Banking Fund III	Buyouts	8/14/2001	85,000,000	87,641,229	138,604,692
36. Elevation Partners	Private Equity	11/10/2005	35,000,000	30,369,560	15,277,493
37. Energy Spectrum Partners IV	Mid Market Buyouts	12/15/2004	50,000,000	52,615,557	59,690,235
Energy Spectrum Partners V	Mid Market Buyouts	7/9/2007	30,000,000	22,687,260	15,681,641
38. Eureka II	Small Buyouts	1/30/2006	20,000,000	16,396,138	2,908,011
39. Excelsior Capital Asia Partners III	Growth Equity	8/17/2006	25,000,000	22,974,936	4,316,788
40. First Reserve Fund X	Buyouts	10/28/2004	30,000,000	30,000,000	39,579,861
First Reserve Fund XI	Buyouts	12/14/2006	60,000,000	48,550,975	14,985,202
First Reserve Fund XII	Buyouts	11/19/2008	50,000,000	30,853,280	2,206,250
41. Francisco Partners	Mid Market Buyouts	7/27/2000	50,000,000	47,825,987	41,370,002
Francisco Partners II	Mid Market Buyouts	7/10/2006	30,000,000	27,750,000	16,565,692
Francisco Partners III	Mid Market Buyouts	*	20,000,000	0	0
42. Frontenac VII	Buyouts	9/30/1997	40,000,000	40,000,000	55,780,630
43. Great Hill Equity Partners	Mid Market Buyouts	4/12/1999	30,000,000	30,000,000	29,994,856
Great Hill Equity Partners II	Mid Market Buyouts	3/28/2001	35,000,000	35,063,336	68,085,735
Great Hill Equity Partners III	Mid Market Buyouts	3/7/2006	35,000,000	34,037,500	5,250,000
Great Hill Equity Partners IV	Mid Market Buyouts	9/8/2008	25,000,000	14,187,500	1,437,500
44. Gryphon Partners II	Mid Market Buyouts	11/3/1999	35,000,000	34,074,092	34,019,309
Gryphon Partners III	Mid Market Buyouts	9/8/2004	30,000,000	33,015,106	14,603,265
45. GTCR V	Buyouts	3/31/1997	11,400,000	11,400,000	20,502,976
GTCR VI	Buyouts	9/30/1998	50,000,000	50,000,000	43,229,799
GTCR VII	Buyouts	3/15/2000	55,000,000	50,074,671	121,729,912
GTCR VIII	Buyouts	7/7/2003	75,000,000	69,393,599	96,377,489
GTCR IX	Buyouts	12/1/2006	50,000,000	45,334,772	4,631,707
46. H.I.G. Bayside Debt & LBO Fund II	Distressed Debt	6/17/2008	30,000,000	11,550,000	2,726,034
H.I.G. Growth Buyouts & Equity Fund II	Distressed Debt	7/20/2011	15,000,000	300,000	0
47. HarbourVest IPEP II	Fund of Funds	6/30/1997	25,000,000	24,500,000	33,545,573
HarbourVest IPEP III	Fund of Funds	6/30/1998	40,000,000	39,000,000	53,487,083
HarbourVest IPEP IV	Fund of Funds	4/9/2001	40,000,000	37,800,000	39,660,429
HIPEP V-Asia Pacific & Rest of World	Buyouts	5/9/2006	30,000,000	22,695,316	1,137,931
Dover Street VII	Secondaries	7/2/2008	30,000,000	24,245,287	2,079,001

# Private Equity Committed, Drawn and Distributed *(continued)*

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
48. Hellman & Friedman Capital Partners IV	Buyouts	2/14/2000	\$75,000,000	\$67,317,209	\$188,912,266
Hellman & Friedman Capital Partners V	Buyouts	12/20/2004	80,000,000	71,022,545	107,505,626
Hellman & Friedman Capital Partners VI	Buyouts	6/5/2007	125,000,000	109,416,503	19,058,893
49. InterMedia Partners VII	Diversified	1/5/2007	15,000,000	15,275,924	1,893,229
50. Invemed Catalyst Fund	Mid Market Buyouts	10/19/1999	25,000,000	14,116,290	11,020,749
51. J.H. Whitney V	Later Stage	3/29/2001	20,000,000	23,307,275	42,361,692
J.H. Whitney VI	Buyouts	1/5/2006	50,000,000	49,008,720	13,420,201
J.H. Whitney VII	Buyouts	10/12/2010	25,000,000	6,069,093	467,888
52. J.W. Childs Equity Partners III	Mid Market Buyouts	8/20/2002	40,000,000	41,116,322	44,442,270
53. JP Morgan US Corp Finance Investors II	Fund of Funds	1/14/2003	50,000,000	50,760,796	30,170,146
54. Kelso VII	Buyouts	10/18/2004	40,000,000	39,651,495	27,007,163
Kelso VIII	Buyouts	11/29/2007	150,000,000	58,946,310	3,036,749
55. Landmark Equity IV	Secondaries	3/31/1995	14,923,291	12,495,850	18,640,869
Landmark Equity Partners V	Secondaries	12/31/1995	19,624,113	19,434,947	23,435,898
56. Leeds Equity Partners IV	Mid Market Buyouts	11/12/2004	20,000,000	20,104,739	7,652,650
57. Lexington Capital Partners II	Secondaries	6/30/1998	40,000,000	39,538,000	50,047,941
Lexington Capital Partners III	Secondaries	1/26/1999	35,000,000	34,516,449	40,061,209
Lexington Capital Partners V	Secondaries	1/17/2002	75,000,000	74,623,418	99,150,707
Lexington Capital Partners VI	Secondaries	10/21/2005	50,000,000	48,519,288	18,854,264
58. Lime Rock Partners III	Later Stage	3/7/2005	15,000,000	14,684,503	2,886,836
Lime Rock Partners IV	Later Stage	11/16/2006	25,000,000	22,365,430	1,516,862
Lime Rock Partners V	Later Stage	10/2/2008	42,500,000	29,036,290	19,089
Lime Rock Resources	Diversified	12/28/2005	20,000,000	19,171,636	9,137,274
59. LLR Equity Partners	Mid Market Buyouts	2/4/2000	25,000,000	24,357,320	51,608,574
LLR Equity Partners II	Mid Market Buyouts	1/29/2004	25,000,000	25,000,000	12,443,178
LLR Equity Partners III	Mid Market Buyouts	7/24/2008	30,000,000	17,783,721	2,204,234
60. Madison Dearborn Capital Partners III	Buyouts	4/6/1999	75,000,000	75,186,728	111,731,905
Madison Dearborn Capital Partners IV	Buyouts	4/2/2001	90,000,000	90,499,697	107,418,527
Madison Dearborn Capital Partners V	Buyouts	12/14/2006	75,000,000	67,708,781	9,869,151
Madison Dearborn Capital Partners VI	Buyouts	5/27/2008	50,000,000	14,626,666	3,284,516
61. Matlin Patterson Global Opps. Partners	Distressed Debt	5/31/2001	35,000,000	30,091,262	56,126,461
Matlin Patterson Global Opps. Partners II	Distressed Debt	6/30/2004	30,000,000	30,410,597	10,578,309
62. Media/Communication III	Buyouts	6/30/1997	25,000,000	23,750,000	37,704,073
Media/Communications IV	Buyouts	3/31/1999	25,000,000	23,125,000	17,102,401
Media/Communications Ventures Fund V	Buyouts	9/27/2000	35,000,000	34,812,205	49,627,103
63. Meridian Venture Partners II	Buyouts	2/11/2005	10,000,000	10,000,000	7,325,308
64. New York Life Capital Partners III	Co-investments	6/30/2006	50,000,000	50,462,637	8,169,250
New York Life Capital Partners IV	Co-investments	4/4/2008	50,000,000	35,522,793	3,692,423
65. Nordic Capital V	Buyouts	5/7/2004	34,996,500	45,749,337	39,121,987
Nordic Capital VI	Buyouts	7/25/2006	54,369,000	62,032,331	4,970,676
Nordic Capital VII	Buyouts	5/2/2008	92,519,165	62,393,753	0
66. Oakhill Capital Partners	Buyouts	5/17/1999	50,000,000	53,683,590	80,361,319

# Private Equity Committed, Drawn and Distributed *(continued)*

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
67. OCM/GFI Power Opportunities Fund II	Buyouts	5/9/2005	\$25,000,000	\$13,439,832	\$38,248,202
Oaktree Power Opportunities Fund III	Buyouts	10/18/2010	25,000,000	2,750,000	128,594
Oaktree Capital Management	Diversified	5/28/2004	40,000,000	40,581,778	49,069,121
OCM Opportunities Fund II	Distressed Debt	3/31/1998	40,000,000	40,000,000	60,311,304
OCM Opportunities Fund III	Distressed Debt	1/20/2000	60,000,000	60,007,890	88,975,999
OCM Opportunities Fund IV	Distressed Debt	9/26/2001	70,000,000	70,000,000	115,396,501
OCM Opportunities Fund V	Distressed Debt	8/12/2004	40,000,000	40,003,507	54,884,510
OCM Opportunities Fund VI	Distressed Debt	9/28/2005	40,000,000	40,000,000	33,517,357
OCM Opportunities Fund VII	Distressed Debt	5/16/2007	40,000,000	40,000,000	22,457,275
OCM Opportunities Fund VIIb	Distressed Debt	6/3/2008	40,000,000	36,000,000	19,800,000
OCM Opportunities Fund VIII	Distressed Debt	9/20/2010	12,500,000	11,333,425	0
OCM Opportunities Fund VIIIb	Distressed Debt	8/22/2011	12,500,000	1,250,000	0
OCM Principal Opportunities Fund IV	Distressed Debt	1/24/2007	20,000,000	20,000,000	3,638,059
OCM Principal Opportunities II	Distressed Debt	4/24/2001	25,000,000	25,000,000	36,426,714
68. Palamon European Equity	Buyouts	7/23/1999	29,779,989	38,316,950	47,972,180
Palamon European Equity II	Diversified	10/25/2005	36,114,000	35,948,993	16,929,447
69. Parthenon Investors II	Mid Market Buyouts	8/9/2001	20,000,000	22,038,045	21,636,107
70. Patriot Financial Partners	Mid Market Buyouts	6/12/2008	25,000,000	16,267,767	146,667
71. Permira European Fund	Buyouts	9/30/1997	33,494,536	32,159,947	84,005,717
Permira European Fund II	Buyouts	6/7/2000	48,000,000	45,672,612	83,557,419
Permira European Fund III	Buyouts	1/12/2004	115,960,000	125,077,125	164,455,245
Permira IV	Buyouts	12/14/2006	127,779,198	110,740,630	7,282,426
Permira UK Venture Fund III	Middle/Later Stage	3/31/1991	9,063,438	8,946,988	26,106,191
Permira UK Venture Fund IV	Middle/Later Stage	12/31/1995	15,248,000	15,993,572	22,721,533
72. Pitango Venture Capital Fund IV	Diversified	7/19/2004	20,000,000	19,601,534	4,826,274
Pitango Venture Capital Fund V	Seed/Early Stage	8/22/2007	30,000,000	17,250,000	0
73. PNC Equity Partners II	Mid Market Buyouts	8/30/2007	15,000,000	11,864,560	2,858,369
74. Providence Equity Partners IV	Mid Market Buyouts	11/27/2000	25,000,000	23,401,363	51,493,280
Providence Equity Partners V	Mid Market Buyouts	4/4/2005	45,000,000	41,826,805	14,875,939
Providence Equity Partners VI	Buyouts	3/16/2007	50,000,000	42,327,824	4,725,985
75. SCP Private Equity Partners II	Buyouts	6/15/2000	25,000,000	25,000,000	5,972,493
76. Segulah IV	Mid Market Buyouts	9/25/2008	16,705,647	9,041,671	63,821
77. SFC Energy Partners I	Buyouts	7/27/2007	25,000,000	16,372,545	6,667,567
SFC Energy Partners II	Buyouts	*	25,000,000	0	0
78. ShoreView Capital Partners	Buyouts	6/16/2003	38,000,000	31,325,970	46,628,590
ShoreView Capital Partners II	Buyouts	3/27/2008	40,000,000	17,434,249	1,246,023
79. Siguler Guff BRIC Opportunities Fund	Fund of Funds	5/8/2006	10,000,000	9,558,299	2,041,503
Siguler Guff BRIC Opportunities Fund II	Fund of Funds	4/9/2008	25,000,000	15,713,700	78,166
80. Sterling Capital Partners I	Buyouts	10/31/2002	15,000,000	15,272,797	23,366,651
Sterling Capital Partners II	Buyouts	8/18/2005	30,000,000	29,722,511	12,533,858
Sterling Capital Partners III	Buyouts	8/13/2007	32,000,000	22,369,164	2,408,422
81. Summit Ventures VI	Later Stage	3/23/2001	62,000,000	63,343,733	70,874,743
Summit Partners Private Equity Fund VII	Buyouts	2/9/2006	97,134,500	86,449,710	12,478,225

# Private Equity Committed, Drawn and Distributed *(continued)*

Active Private Equity Funds Limited Partnership	Financing Stage Focus	SERS Initial Funding	Capital Committed**	Capital Drawn	Distributions
82. TA IX	Later Stage	9/20/2000	\$45,000,000	\$43,650,000	\$90,634,128
TA X	Middle/Later Stage	4/25/2006	70,000,000	67,550,000	22,050,000
83. Thomas H. Lee Equity Fund V	Buyouts	7/3/2001	100,000,000	104,548,472	124,804,582
Thomas H. Lee Equity Fund VI	Mid Market Buyouts	11/14/2006	50,000,000	38,553,899	4,692,612
84. TPG Partners II	Buyouts	6/30/1997	75,000,000	72,111,267	127,798,284
TPG Partners III	Buyouts	1/13/2000	75,000,000	64,119,169	150,401,569
TPG Partners IV	Buyouts	12/29/2003	30,000,000	27,999,752	29,185,932
TPG Partners V	Buyouts	6/27/2006	100,000,000	88,927,438	13,132,756
TPG Partners VI	Buyouts	5/22/2008	45,000,000	26,813,919	3,900,063
Newbridge Asia III	Buyouts	2/15/2001	15,000,000	14,438,357	54,857,234
Newbridge Asia IV	Buyouts	9/27/2005	40,000,000	37,818,791	32,512,079
TPG Asia V	Buyouts	2/19/2008	22,500,000	17,119,927	2,329,636
85. UMS Partners Fund I	Distressed Debt	2/15/2005	5,000,000	5,000,000	3,004,752
86. Versa Capital Partners	Distressed Debt	10/16/2005	20,000,000	21,311,753	12,255,381
Versa Capital Partners II	Distressed Debt	7/31/2008	15,000,000	5,564,170	0
87. Vestar Capital Partners III	Buyouts	6/30/1997	25,000,000	24,362,534	23,541,126
Vestar Capital Partners IV	Mid Market Buyouts	1/25/2000	100,000,000	97,350,140	123,154,733
Vestar Capital Partners V	Mid Market Buyouts	1/25/2006	50,000,000	50,128,303	13,916,928
88. W Capital Partners II	Secondaries	8/8/2007	40,000,000	31,227,138	20,487,171
89. Yucaipa American Alliance Fund II	Mid Market Buyouts	1/13/2009	25,000,000	16,122,810	1,697,958
<b>Total Active Private Equity</b>			<b>\$9,460,502,013</b>	<b>\$8,210,008,335</b>	<b>\$7,316,052,477</b>

\*Not Funded as of 9/30/11

\*\*Commitments as of 12/31/11  
Cash flows as of 9/30/11

## Inactive Private Equity Funds

Limited Partnership	Capital Committed	Capital Drawn	Distributions
<b>Total Inactive Private Equity</b>	<b>\$626,086,484</b>	<b>\$609,589,801</b>	<b>\$1,119,545,804</b>



# Inflation Protection Investments Summary

as of December 31, 2011 - (Unaudited)

Inflation Protection is one of six 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. In accordance with SERS' investment plan, 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 Fund and to act as a hedge against inflation. The asset class is composed of actively managed commodities; 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. 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 periods of rising inflation, 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 SERS Custom Inflation Protection Benchmark.

SERS' *2011 Annual Strategic Investment Plan* targets a long-term allocation of 3.0% of assets to Inflation Protection. Within this 3.0% allocation, 50.0% is targeted to the active diversified inflation protection portfolio, and the remaining 50.0% is targeted to the active multi-manager commodity portfolio.

**Market Exposure as of December 31, 2011:** Inflation Protection strategies had a \$1.0 billion market exposure, 4.2% of the total Fund's \$24.2 billion.

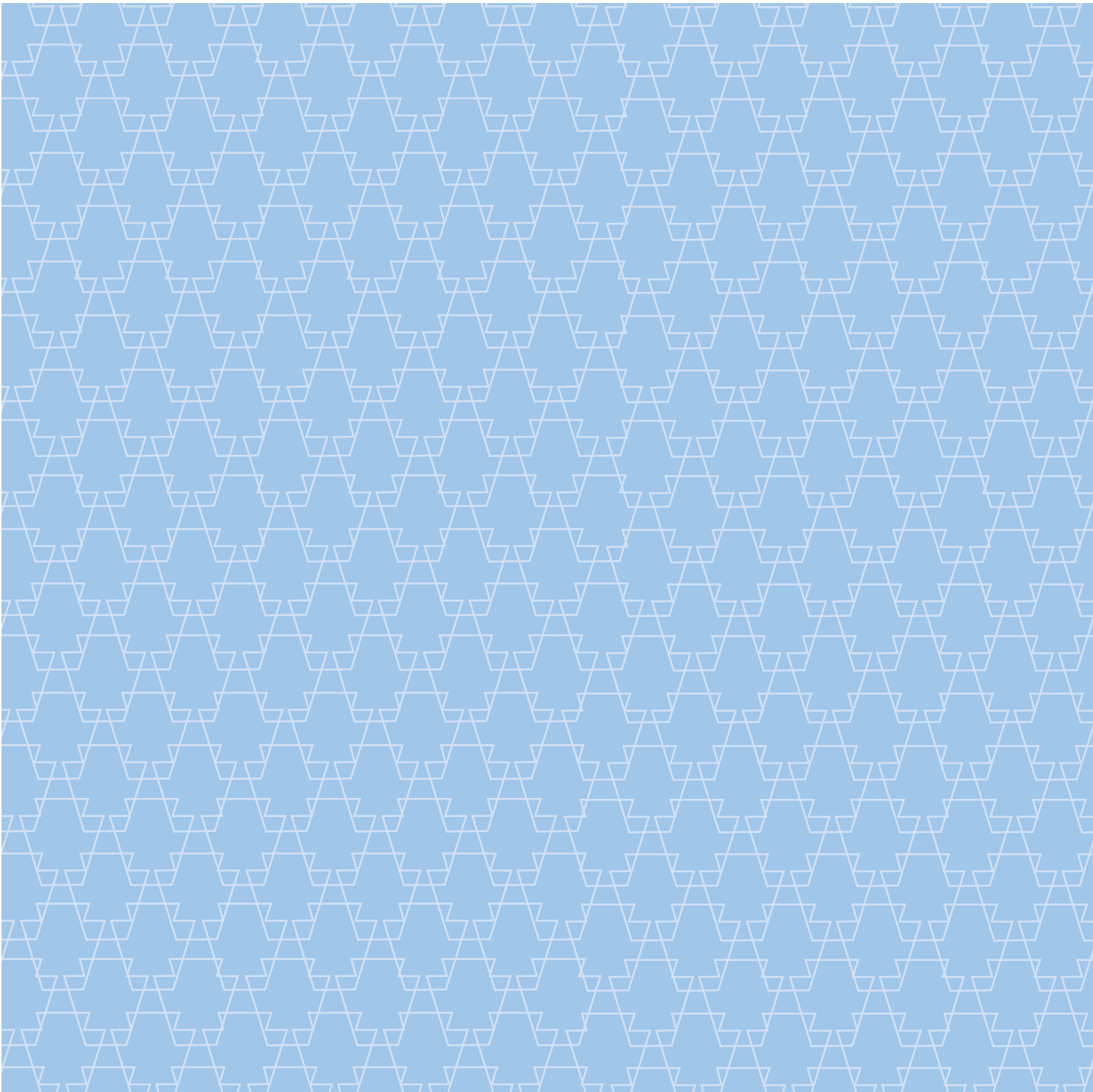
**Number of Investment Advisors:** SERS had contracts with two external investment advisors.

**Types of Investment Portfolios:** As of December 31, 2011, 45.4% of SERS' Inflation Protection allocation was invested in the actively managed diversified inflation protection portfolio which invests in commodities, inflation-sensitive global equity and TIPS. The remaining 54.6% was in the multi-manager commodity product, which employs five 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 12/31/11* (\$ millions)
1. Wellington Management Company	Diversified inflation protection portfolio	\$465.4
2. Blackstone Alternative Asset Management	Fund-of-commodity funds	560.1
<b>Total Inflation Protection Investments</b>		<b>\$1,025.5</b>

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



# Pennsylvania Investments Summary

as of December 31, 2011 - (Unaudited)

The Board, employees of SERS and agents of the Board stand in a fiduciary relationship to the members and beneficiaries of the System regarding the investments and disbursements of the Fund. Subject to “prudent investor” investment responsibilities contained in the Retirement Code and the Fiscal Code, the Board has exclusive control and management of the Fund and full power to invest the assets of the Fund. The Board adopted a formal *Statement of Investment Policy* in 1979, which was last revised effective April 2009 to reflect and incorporate subsequent legislative and policy changes governing investments. Where investment characteristics including yield, risk and liquidity are equivalent, the Board’s policy favors investments that have a positive impact on the economy of Pennsylvania.

The most significant impact the Fund can have on the State’s economy is to manage an overall program that achieves a fully funded status and lowers the employer contributions to the Fund below the normal cost. The reduction of such contributions may then be used by the legislature for purposes it deems most important to Pennsylvania citizens and taxpayers, such as tax reduction, economic development or other priorities. Nevertheless, the Fund also seeks to invest in State-based companies and other State entities when investment characteristics are equivalent.

**Fair Value of Pennsylvania Investments as December 31, 2011:** SERS’ assets had an unaudited fair value in Pennsylvania investments of approximately \$958.9 million, 4.0% of the SERS Fund.

## SERS Pennsylvania Investments By Asset Class (\$ millions)

Asset Class	Total PA Fair Value
Stocks	\$504.3
Fixed Income	19.4
Real Estate	226.8
Alternative Investments	208.4
<b>Total Pennsylvania Investments</b>	<b>\$958.9</b>

SERS investment portfolios have historically held investments in Pennsylvania firms, as some large national firms are headquartered in Pennsylvania, including Comcast Corporation (Philadelphia-Communications), PNC Financial Services (Pittsburgh-Financial), Air Products & Chemicals, Inc. (Allentown-Basic Materials), H. J. Heinz Company (Pittsburgh-Consumer), and PPG Industries Inc. (Pittsburgh-Basic Materials). In addition, SERS has invested in portfolios that are designed to give emphasis to investments in Pennsylvania while meeting the fiduciary standards mentioned previously.

### Stocks

SERS’ Pennsylvania stock universe is comprised of 346 publicly-traded corporations which: 1) name their headquarters as Pennsylvania and have Pennsylvania employees or operations; or 2) have Pennsylvania-based employment exceeding 25% of total corporate employment. The following are some of the top performing Pennsylvania stocks for the 2011 calendar year.



# Pennsylvania Investments Summary *(continued)*

## Top-Performing Pennsylvania Stocks

Company	Location	Return for 2011
<b>Parkvale Financial Corp</b> Parkvale Financial Corporation is a bank holding company for Parkvale Savings Bank. The Bank attracts deposits from the general public and uses those funds to originate loans through numerous full-service offices in Allegheny, Beaver, Butler, Washington and Westmoreland counties, Pennsylvania.	Monroeville	168%
<b>U.S. Rare Earths Inc</b> U.S. Rare Earths Inc. owns mining and mineral claims in Colorado. The company owns certain mining and/or mineral claims and/or leases located in and around the Lemhi Mining District of Idaho and the Montana Beaverhead District where it explores for rare earth elements.	Montoursville	163%
<b>Photomedex Inc</b> PhotoMedex Inc. manufactures excimer laser and fiber-optic systems used to treat dermatological conditions such as psoriasis, vitiligo, atopic dermatitis, and leukoderma. The company offers products and services on contract to dermatologists and hospitals. PhotoMedex develops skin health, haircare, and wound care products based on its copper peptide technology.	Montgomeryville	117%
<b>Fidelity Bancorp Inc</b> Fidelity Bancorp, Inc. is the holding company for Fidelity Bank. The Bank attracts deposits and invests in one to four family residential mortgage loans and securities. Fidelity Savings also originates commercial real estate, home equity, consumer, and small business loans. The Bank operates offices in Allegheny and Butler counties, Pennsylvania.	Pittsburgh	79%
<b>Atlas Energy Lp</b> Atlas Energy LP transports petroleum products. The company owns and operates natural gas processing plants and gas gathering pipeline systems in Kansas, Oklahoma and Texas; and a pipeline system in Tennessee. Atlas Energy also offers investment management services.	Moon Township	67%
<b>Harleysville Group Inc</b> Harleysville Group Inc. is an insurance holding company. The company operates with Harleysville Mutual Insurance Company to form a network of insurance companies primarily in the Eastern and Midwestern United States. Harleysville underwrites personal and commercial property and casualty coverages, including automobile, homeowners, commercial multi-peril, and workers compensation.	Harleysville	60%
<b>Atlas Pipeline Partners Lp</b> Atlas Pipeline Partners, LP. provides natural gas gathering services in the Anadarko and Permian Basins located in the southwestern and mid-continent United States and the Appalachian Basin in the eastern United States. The company also provides natural gas processing and treating services in Oklahoma and Texas.	Pittsburgh	59%
<b>Orasure Technologies Inc</b> OraSure Technologies Inc. develops, manufactures, and markets medical devices and diagnostic products. The company supplies oral fluid collection devices and assays to the life insurance industry and public health markets for the detection of antibodies to HIV. OraSure also supplies oral fluid testing solutions for drugs-of-abuse testing.	Bethlehem	58%
<b>Viropharma Inc</b> Viropharma Incorporated is a biopharmaceutical company committed to the commercialization, development, and discovery of new medicines. The company's products include a treatment for prophylaxis of hereditary angiodema as well as capsules for the treatment of antibiotic associated pseudomembranous colitis caused by clostridium difficile infection (CDI) and enterocolitis.	Exton	58%
<b>Education Management Corp</b> Education Management Corporation provides proprietary post-secondary education in the United States. The company offers, through its operating units, associate's and bachelor's degree programs in the areas of design, media arts, culinary arts, fashion, and professional development.	Pittsburgh	55%

# Pennsylvania Investments Summary *(continued)*

Emerald Advisors of Lancaster and Mellon Capital Management Corporation of Pittsburgh actively manage portfolios principally derived from the mid/small cap stocks in SERS' Pennsylvania stock universe. These two portfolios, plus the Pennsylvania stocks held in SERS other stock portfolios, provided a total of \$504.3 million invested in Pennsylvania stocks.

## Fixed Income

SERS had approximately \$19.4 million invested as of December 31, 2011, in corporate securities issued by Pennsylvania-based companies. These securities are held in SERS' various externally managed bond portfolios.

In 1998, the SERS Board approved the funding for the Pennsylvania Capital Fund with a \$50 million allocation committed to the program. The program commenced in March 1999 managed by Berwind Financial Group (Berwind) and PNC Equity Management (PNC). Each advisor was awarded commitments of \$25 million to be invested over four years. Both entities matched SERS' investment. The program provided debt financing to support the expansion and growth of Pennsylvania small business. The Fund's objective was to lend to established, profitable companies in good financial condition with annual revenues ranging from \$10-\$100 million. The majority of the Fund's investments had a maturity of between five and ten years. Loan amounts usually ranged from \$2 million to \$15 million. As of December 31, 2011 SERS portion of Berwind investments totaled \$2.3 million while the PNC investments had matured and all capital was returned to SERS. Nearly all of Berwind's investments have also matured and capital distributed back to SERS.

To date the fund also has PA exposure with various other asset managers. The break out is listed below:

Manager	Market Value (\$ millions)	% of Total PA Market Value
BNY Mellon	\$0.6	0.1%
Taplin Canida Habacht	5.7	0.6
Ramius Advisors	6.2	0.6
Stone Harbor	4.6	0.5

## Cash

SERS is one of the largest investors in the Pennsylvania State Treasury Department's Short-Term Investment Pool.

## Real Estate

In 1987 SERS began investing directly in the Pennsylvania commercial real estate market and subsequently established two separate account real estate portfolios managed by Heitman Capital Management and Grosvenor Investment Management, formerly Legg Mason Real Estate Services, with a Pennsylvania focus. The Heitman separate account originally had a requirement to invest on a best efforts basis 50% of its initial allocation within the Commonwealth while the Grosvenor account is focused primarily on investing within the state.

As of September 30, 2011, the SERS real estate portfolio contained 49 Pennsylvania investments totaling 6.2 million square feet of office, retail, and warehouse space, and 4,829 apartment, hotel and senior housing units. The gross fair value of the Pennsylvania real estate portfolio investments totaled \$1.0 billion, of which SERS' ownership share was \$226.8 million.

## Alternative Investments

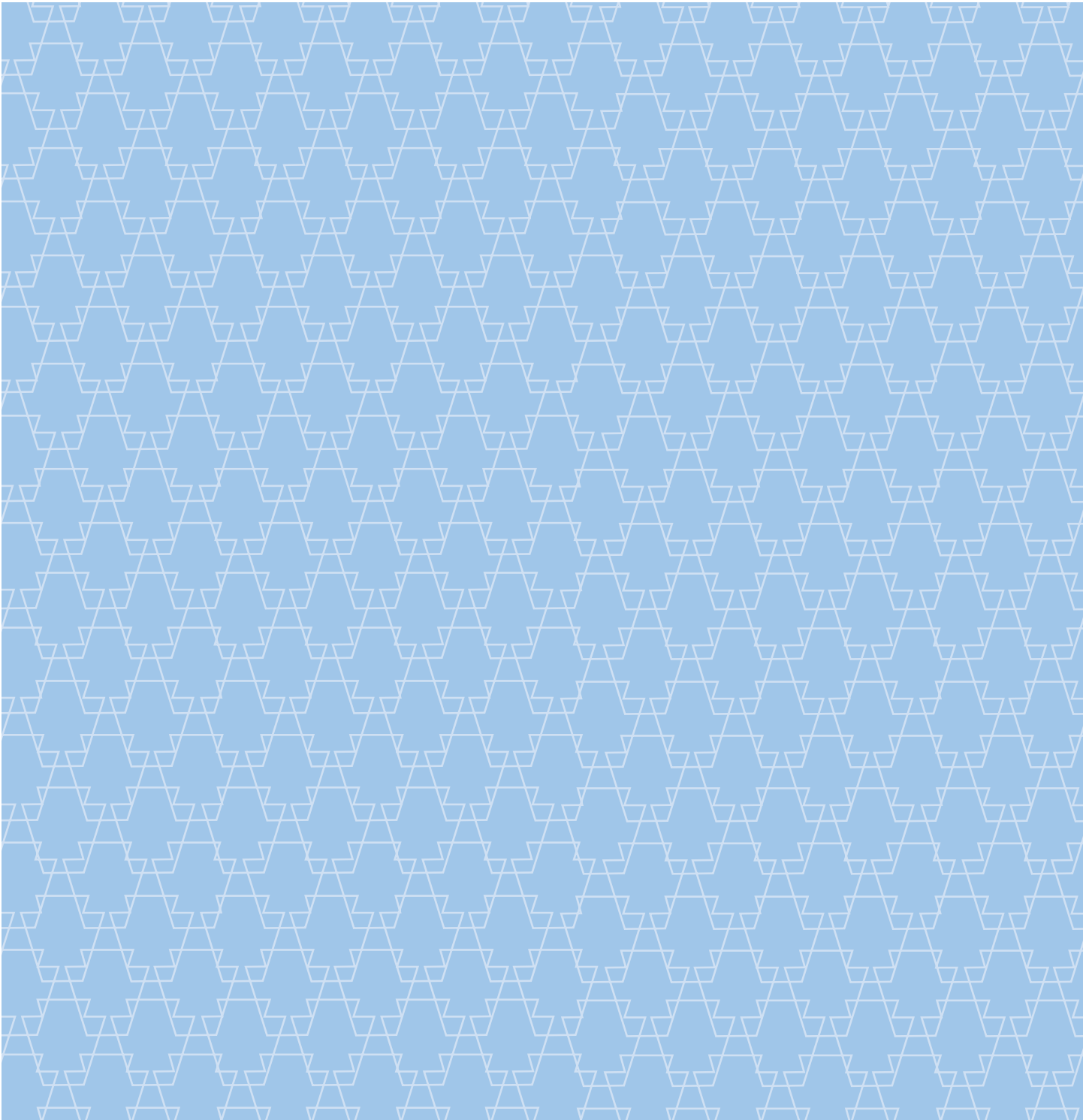
SERS' venture capital program dates back to 1985. Initially the program targeted a 1% allocation to venture capital with a focus to invest with managers located in Pennsylvania or with managers whom had a Pennsylvania investment mandate. Over its 26 year life the program has grown to include national and international based private equity and venture capital managers and the target allocation to alternative investments is currently 15%. Since inception, SERS' Alternative Investment program has made commitments of \$947 million to 52 limited partnerships based in Pennsylvania.

# Pennsylvania Investments Summary *(continued)*

In addition, the number of non-Pennsylvania based managers investing in companies that impact the state comprises a meaningful portion of the program.

As of September 30, 2011, SERS' active Alternative Investment managers held 120 Pennsylvania-based companies. SERS pro-rata investment value in these companies is approximately \$208.4 million. This equates to 3.3% of the Alternative Investment program fair value and does not include investments headquartered outside of Pennsylvania that may have impactful operations within the state.

Although the Board's fiduciary duty is to SERS' members and beneficiaries, investments in Pennsylvania provide an ancillary and subordinate benefit to the state's economy. The investment policy acknowledges that such benefit, derived from investments in Pennsylvania based companies, or firms employing Pennsylvanians, should be considered after other primary fiduciary investment characteristics are satisfied.



# Women/Minority Investment Advisor and Broker Report

as of December 31, 2011

## Investment Advisors

The following four women or minority-owned firms were under contract with SERS to provide investment advisory services as of December 31, 2011.

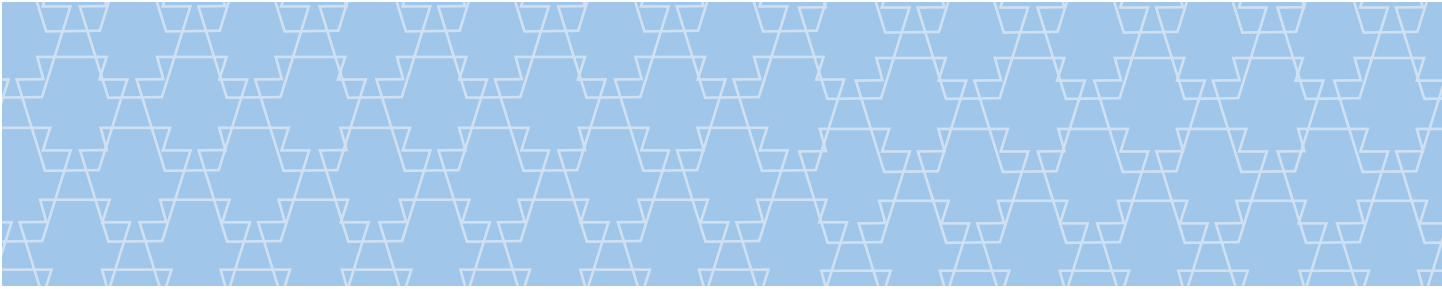
Firm	Status	SERS Assets Under Management
Fairview Capital I & II	Minority/Woman-Owned	\$20.0 million commitment; \$19.9 million funded
Hawkeye Partners	Woman-Owned	\$75.0 million commitment; \$75.0 million funded
Rock Creek (Penn Quarter, L.P.)	Minority/Woman-Owned	\$194.7 million fair value
Taplin, Canida & Habacht, Inc.	Minority/Woman-Owned	\$168.6 million fair value

## Brokers and Brokerage Commissions

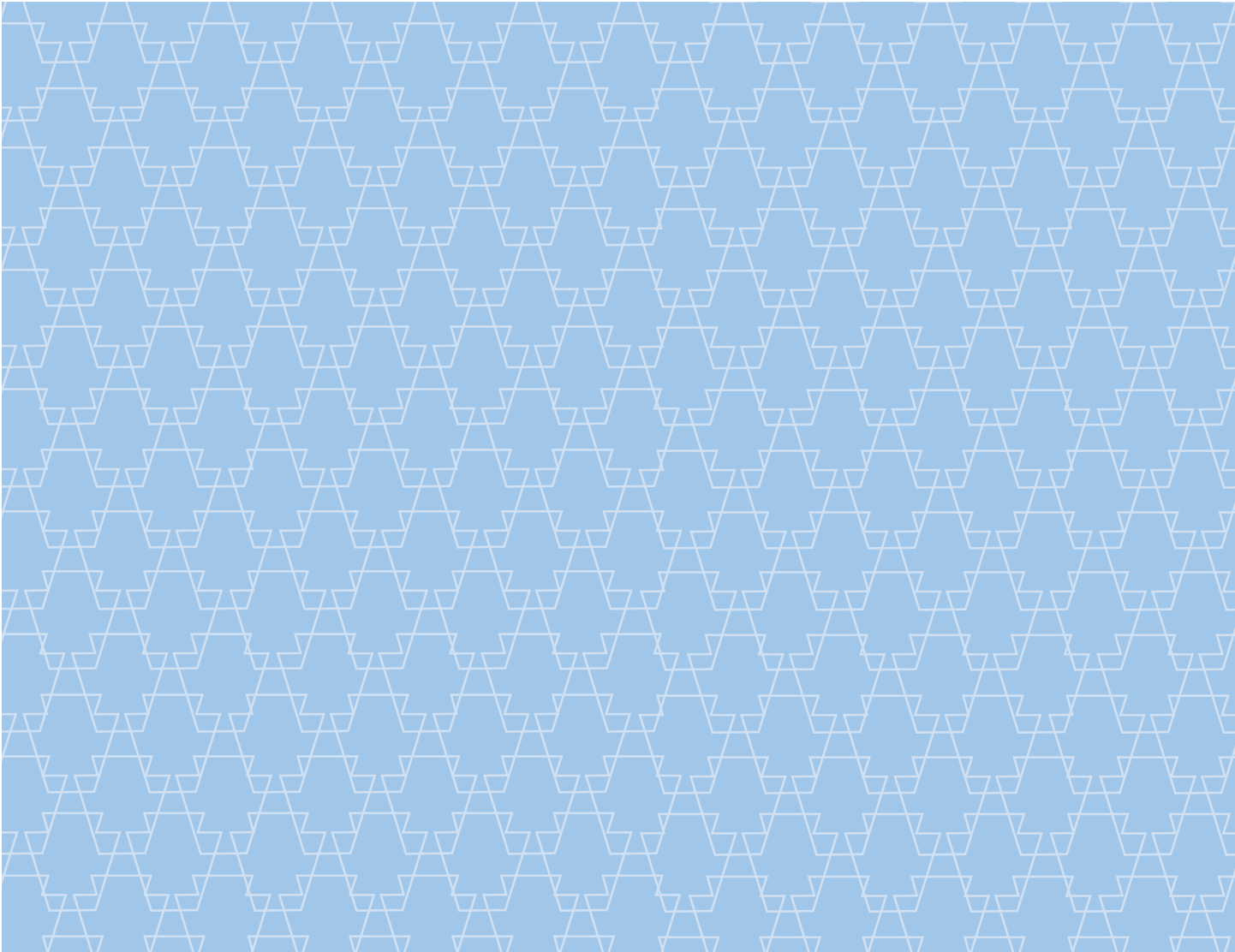
SERS's external investment advisors utilized the following minority-owned brokerage firms during calendar year 2011.

Minority commissions totaled \$186,131 for the year. Of this amount, international stock managers had \$52,865 of commissions credited to minority brokers. The SERS Board has a policy of targeting 5%-10% of U.S. stock commissions to be done with minority brokers. It is estimated that this year SERS U.S. stock managers directed 5% of their trades through minority brokers. In addition, although not included in the Board mandate, other SERS advisors are encouraged to trade through minority brokers. During 2011 fixed income managers traded \$27.2 million of securities through minority brokers.

Firm	Commissions
Cabrera Capital Markets	\$16,897
C L King	1,038
East West	9,768
Divine Capital Markets	2,339
Greentree Brokerage	7,358
Loop Capital Management	14,721
M Ramsey King	9,141
Seslia Securities	17,029
Sturdivant & Company	87,096
Williams Capital Group	20,744
<b>Total Minority Commissions</b>	<b>\$186,131</b>



# Deferred Compensation Program 12



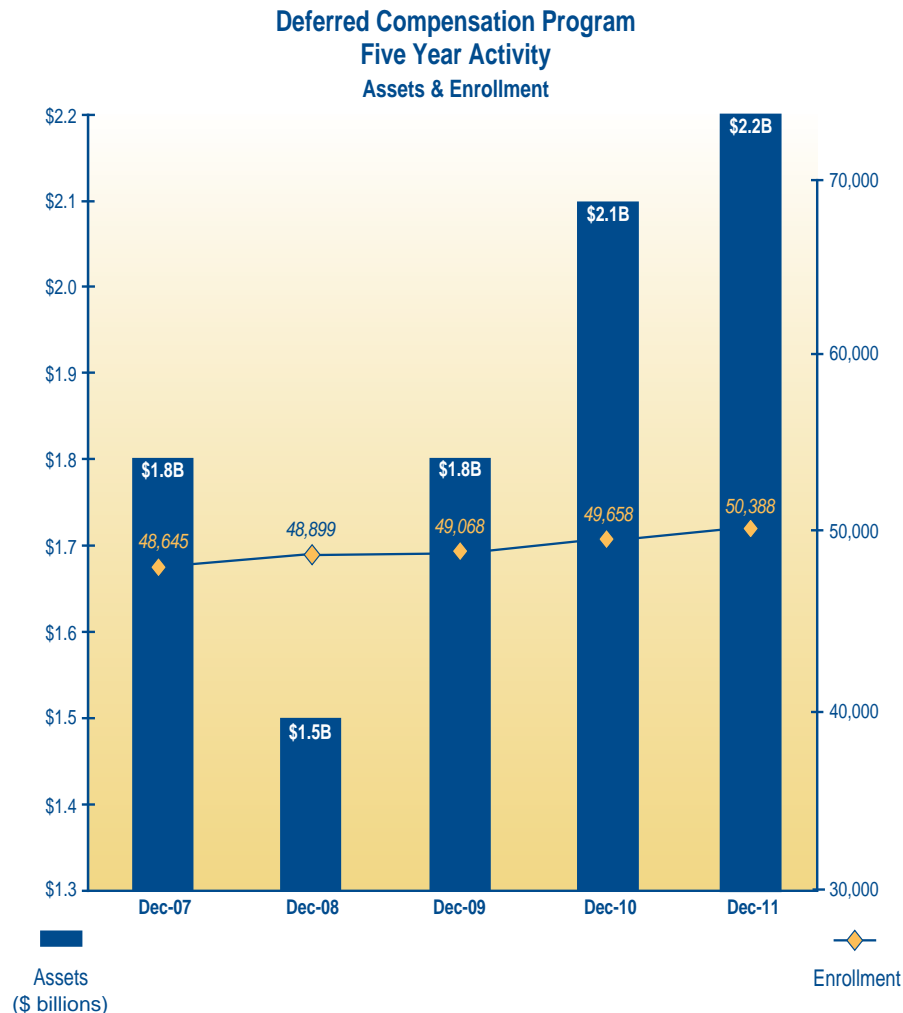
# Deferred Compensation Program

## Program History

Act 1987-81 assigned to the State Employees' Retirement Board (Board) the responsibility to establish and monitor a Deferred Compensation Program (Program) for Commonwealth officers and employees, through which participants may voluntarily build retirement savings by deferring a portion of salary to selected investment options. The Program is established as a trust, and is administered in accordance with Internal Revenue Code Section 457(b). Through the Request for Proposal process, the Board selected Great-West Retirement Services as Third Party Administrator (TPA) of the Program. The duties of the TPA are to maintain individual participant records, market the Program to participants, and counsel the members about the Program's benefits. The core investment options are selected by the Board, and are independent of the TPA's functions.

## Growth of the Program

Over the past five years, the Program's assets have increased in value from \$1.8 billion to approximately \$2.2 billion. The sharp drop in assets from \$1.8 billion in 2007 to \$1.5 billion in 2008 can be attributed to the downturn in the financial markets as participation in the program remained steady. As of December 31, 2011, there were 32,101 active and 18,237 inactive participants in the Program. The amount of annual participant deferrals over the past five years has ranged from \$122 million to \$160 million. In 2007, deferrals were \$160 million which was attributed to the large number of participant retirements that utilized the Program's special catch-up feature. Benefit payments to participants increased over that same time span, from \$48 million in 2007, to \$60 million in 2011. The chart below depicts the Program's asset and participation levels over the past five years.



# Deferred Compensation Program *(continued)*

## Program Highlights

The TPA provides participant assistance via individual and/or group counseling sessions with the eligible employee, at the employees' work site. The TPA has established a local walk-in office in the Harrisburg downtown area. A toll free telephone service with counselors is also available to offer personal assistance. A telephone Voice Response Unit can be accessed at anytime to allow the participant to check on their account balance, transfer funds among different investment options or inquire about other Program features. The participants may also access the Program's website at [www.sers457.com](http://www.sers457.com) to view their most recent investment position, to make future allocation changes, to transfer among investment options and to update beneficiary information. Educational videos on financial, investment and retirement planning are also available to help participants in their investment and retirement decisions. In January 2009, the Program began to offer managed accounts to its participants. Managed accounts are personalized investment portfolios put together from among the plan's investment options for participants who want a professional to do the investing for them.

