Investment

Northwest

Southwest

COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM
ALAN H. VAN NOORD, CFA
Chief Investment Officer

October 31, 2011

Dear Members of The PSERS Board of Trustees:

It is a privilege to present to you the Investment Section of the Comprehensive Annual Financial Report for the year ended June 30, 2011.

Authority and Fiduciary Standard

The Board has the responsibility to invest funds of the System in accordance with guidelines and limitations set forth in the Code and other applicable state law. As fiduciaries, the members of the Board and Staff must act solely in the interests of the members of the System and for the exclusive benefit of the System's members. In performance of their duties, the members of the Board and Staff delegated with investment authority shall be held to the Prudent Investor Standard.

The Prudent Investor Standard, as articulated in the Code, means "the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence who are familiar with such matters exercise in the management of their own affairs not in regard to speculation, but in regard to the permanent disposition of the fund, considering the probable income to be derived therefrom as well as the probable safety of their capital."

The Prudent Investor Standard requires a trustee to act prudently and with caution, discretion, loyalty, and care but does not restrict the assets in which the Board can invest. Under the Prudent Investor Standard, which recognizes modern portfolio theory, the Board's investment and management decisions with respect to individual assets shall be considered in the context of the portfolio as a whole and as part of an overall investment strategy, and not in isolation. No specific investment or course of action, taken alone, shall be considered inherently prudent or imprudent. This Standard recognizes the trade-off between risk and return.

Policies and Objectives

The Board is responsible for the formulation of investment policies for the System. The overall investment objectives of the System are as follows:

Return Objectives – the overall return objective is to realize a return sufficient to achieve funding adequacy on an inflation-adjusted basis. Funding adequacy is achieved when the actuarial market value of assets is at least equal to the System's projected benefit obligations. The System has a return objective of meeting or exceeding the targeted actuarial rate of return, which was reduced from 8.0% to 7.5% effective with the June 30, 2011 actuarial valuation, over the long-term. In addition, the Board has the following broad objectives:

1. The assets of the System shall be invested to maximize the returns for the level of risk taken; and,
2. The System shall strive to achieve a return that exceeds the Policy Index (the Policy Index is a custom benchmark, which is based on the Board-established asset allocation structure that seeks to generate a return that meets the actuarial rate of return assumption).

Risk Objectives

1. The assets of the System shall be diversified to minimize the risk of losses within any one asset class, investment type, industry or sector distribution, maturity date, or geographic location. Failure to do so could impair the System's ability to achieve its funding and long-term investment goals and objectives; and,
2. The System's assets shall be invested so that the probability of investment losses (as measured by the Policy Index) in excess of 15% in any one year is no greater than 2.5% (or two standard deviations below the expected return).

To achieve these objectives, the Board meets during the first quarter of the calendar year to review the overall asset allocation plan and investment policies for the System. Implementation of investment policies is accomplished through the use of external investment management firms who act as agents for the System and through the use of internal investment managers. The Board also retains various investment consultants to assist with the formulation and implementation of investment policies.

Operations

The Board, via the Finance Committee, provides oversight of investment activities. The Finance Committee generally conducts seven meetings per year and may meet more frequently as needed. Investment Office staff, as well as external investment advisors and Investment Accounting staff, assist the Board in achieving investment objectives and monitoring compliance with investment policies. For the fiscal year ended June 30, 2011, Wilshire Associates Incorporated (Wilshire) served as the general investment consultant to assist the Board in formalizing investment objectives, establishing an asset allocation plan, conducting investment advisor searches, reviewing performance, and commenting on compliance with investment policies. In addition, the Board utilized Aksia, LLC as an absolute return consultant, Courtland Partners, Ltd. as a real estate consultant, and Portfolio Advisors, LLC as an alternative investment consultant. Alternative investments generally consist of investments in private debt, private equity, and venture capital limited partnerships. Investment Office staff implement the investment decisions within the guidelines established in the Investment Policy Statement, Objectives and Guidelines regarding asset allocation, manager selection, security selection, and other objectives directed by the Board.

The Board employs both external investment management firms and internal investment managers to manage the investment portfolio of the System. At fiscal year end, 34 external public market investment management firms were managing $17.0 billion in assets of the System, $16.2 billion in assets were managed by the System's internal investment managers, and the remaining $18.6 billion in assets were managed by numerous emerging, alternative investment, and real estate investment managers. The performance of each external investment management firm and each internal manager is monitored quarterly against a pre-established benchmark as well as the performance of the manager's peer group.

Asset Allocation

The Board reviews the long-term asset allocation targets of the System during the first quarter of each calendar year. The Board will consult with its actuary, consultants, Investment Office staff, and other sources of information it deems appropriate in formulating the asset allocation plan. The Board believes that the level of risk assumed by the System is largely determined by the Board's strategic asset allocation plan. The Board, in determining its long-term asset allocation, shall take the following factors into consideration:

- The System's investment time horizon;
- The demographics of the plan participants and beneficiaries;

- The cash flow requirements of the System;
- The actuarial assumptions approved by the Board;
- The funded status of the System;
- The Board's willingness and ability to take risk; and,
- The employers' (Commonwealth and school districts) financial strength.

In establishing the asset allocation for the System, the Board considers capital market expectations for expected return, volatility, and asset class correlations as prepared by its general investment consultant. The current long-term, top-down asset allocation targets of the Board are discussed in the following paragraphs.

The long-term target allocation as of June 30, 2011 included an equity target allocation of 25.5% consisting of publicly traded stocks. Specific targets have been established for U.S. equity exposure (11.2%) and non-U.S. equity exposure (14.3%). Within the U.S. equity target, the portfolios are diversified between large, small, and micro capitalization investment managers, and growth and value investment managers. The non-U.S. equity exposure includes both developed and emerging markets portfolios as well as large and small capitalization investment managers.

The fixed income target allocation of 26.3% consisted of U.S. core fixed income exposure (5.3%), leveraged Treasury Inflation-Protected Securities exposure (5.0%), high yield exposure (6.0%), emerging markets fixed income exposure (2.0%), non-U.S. fixed income exposure (3.0%), and cash (5.0%). Within these categories, all sectors of the bond market are represented.

The real estate target allocation of 9.7% consisted primarily of limited partnerships. The types of partnerships the System invests in include core, value-added, and opportunistic real estate limited partnerships.

Alternative investments had a target allocation of 20.5%. The primary vehicle used to invest funds in this asset class is the limited partnership. The partnerships are established by individual management groups that have been selected by the System for the purpose of investing in and managing private equity, venture capital, and unlisted subordinated debt positions on behalf of PSERS and other limited partners.

The absolute return target allocation of 12.0% consisted primarily of investment managers retained by the System to generate positive returns over time independent of how the equity, fixed income, and commodity markets perform. Strategies implemented to achieve this target include, but are not limited to, global macro, currency, and relative value strategies such as equity long/short. The absolute return program is included in the allocation to generate returns equal to or greater than its benchmark of 8.00% and to diversify the System's total portfolio risk.

The commodities target allocation of 6.0% consisted primarily of commodity futures and commodity and commodity-related publicly traded stocks. Commodities are included in the allocation to diversify the System's total portfolio risk.

Investment Results

As of June 30, 2011, the fair value of the investment portfolio was $51.8 billion, an increase of $5.3 billion from last year's value. This increase was due to net investment income ($9.2 billion) less the deductions for benefits and administrative expenses exceeding member and employer contributions ($3.7 billion) less net changes in other investment assets and liabilities ($0.2 billion). The investment portfolio, as invested, was composed of 26.6% common and preferred stocks (equity), 27.0% fixed income investments, 20.8% alternative investments, 10.7% real estate, 10.3% absolute return portfolios, and 4.6% commodities at June 30, 2011. The table immediately following this letter illustrates a more detailed description of the investment portfolio's asset classes in dollars and as a percentage of the total investment portfolio.

The first half of the fiscal year saw a continued pickup in U.S. economic activity which began last fiscal year closing some of the slack in the economy. That growth, however, quickly tapered off in the second half of the fiscal year as fiscal and monetary supports started to wane. The U.S. Gross Domestic Product (GDP) increased by 2.6%, 3.1%, 0.4%, and 1.3% in the third quarter 2010, fourth quarter 2010, first quarter 2011, and second quarter 2011, respectively. The official unemployment rate (otherwise known as the U3 unemployment rate) fell modestly during the fiscal year from 9.5% as of June 2010 to 9.2% as of June 2011. The more encompassing U6 unemployment rate, however, which measures not only people without work seeking full-time employment (U3 unemployment rate) but also counts "marginally attached workers and those working part-time for economic reasons" remains elevated at 16.2% as of fiscal year end, down only slightly from 16.5% at the end of the last fiscal year. This past year saw a lot of cross currents for the U.S. economy, including the U.S. Federal Reserve (the Fed) implementing another round of quantitative easing (a.k.a. QE2), geopolitical strife in the Middle East and Africa, and a massive earthquake and resultant tsunami in Japan.

Internationally, the news was really driven by the European debt crisis which has the potential to be one of the largest debt crises in history. Countries in the periphery of Europe, including Greece, Portugal, Ireland, Spain, and Italy have tremendous amounts of debt and have required, in various degrees, rescue packages from the European Central Bank and International Monetary Fund. Conditions of support from these rescue packages include implementation of austerity measures which require each of these countries to either increase taxes or decrease government spending, both of which will have a negative impact on economic growth. The funding gaps in these countries have the potential to be economically destabilizing to world growth.

While corporations have strengthened their balance sheets and extended the maturity of their debts, the consumer, which represents about 70% of the U.S. economy, continues to have a significant amount of consumer and mortgage debt. The Fed has already lowered the Federal Funds rate to nearly 0.00% and has no further room to ease monetary policy through interest rate cuts. This position leaves the Fed with less conventional monetary stimulus tools such as quantitative easing which are blunter and less proven monetary tools than interest rate cuts. The U.S. unemployment rate remains elevated and consumer income is not growing quickly. Consumer confidence, as measured by the University of Michigan Survey of Consumer Confidence Sentiment, remains near levels normally seen in recessionary periods and has fallen from 76.0 at the end of last fiscal year to 71.5 at the end of this fiscal year and has continued to deteriorate so far in fiscal year 2011/2012. The U.S. federal deficit has grown significantly over the past few years in an effort to support the waning economy. The only ways to bring federal deficits under control are to cut spending or raise taxes, both of which will take money out of consumers' pockets. These issues represent significant headwinds to consumer spending and growth in the U.S. which could remain in place for a considerable period of time. With short-term interest rates anchored at nearly 0.00%, we anticipate that we will be in a low asset return environment for the foreseeable future, providing further headwinds to income growth.

With the continued backing of accommodative monetary and fiscal policies during the past fiscal year, there was a continued rally in risk assets worldwide which led to positive returns in most asset classes. The Morgan Stanley Capital International (MSCI) U.S. Broad Market Index, a U.S. equity index, returned 31.98% during the fiscal year. Returns for the first three quarters of the fiscal year were exceptionally strong, posting a 32.09% return before declining 0.08% in the fiscal fourth quarter as it had become apparent that the economy was slowing, fiscal austerity was being discussed more, and monetary policy was tightening with the end of QE2. Foreign markets in U.S. dollar terms also fared well as the MSCI All Country World (ACW) ex. U.S. Investable Market Index, an international equity index, returned 30.26% for the fiscal year.

The Venture Economics median return, a benchmark for alternative investments that represents the median performance of the venture capital/private equity industry listed in the Investment Benchmark Reports on Venture Capital and Buy-outs produced by Venture Economics, returned 11.37% during the fiscal year as these investments were written up to prices comparable to gains in the public equity markets.

Commodity markets performed very well in this environment as loose monetary policy drove up the prices of various commodities such as oil and gold. For the fiscal year, the Dow Jones UBS Commodity Index, an index composed of futures contracts on 19 physical commodities weighted to account for economic significance and market liquidity, was up 25.91%.

Fixed income markets were mixed in this environment as interest rates remained relatively steady during the year and investors looked to take advantage of wide credit spreads in search of yield. For the fiscal year, the Barclays U.S. Universal Index, a U.S. fixed income index, was up 4.78% as the yield curve remained fairly unchanged. The Barclays Multiverse Index, a global fixed income index, was up 10.77% driven primarily by a weakening U.S. dollar due to very low interest rates and QE2. The Barclays High Yield Index returned 15.63% during the past fiscal year due to a tightening of credit spreads as investors bid up credit in search of yield. The Barclays U.S. TIPS Index, an index of U.S. treasury inflation protection securities, driven by falling real yields and increasing inflation pressures due to the Fed's quantitative easing, returned 7.74% for the fiscal year.

According to the National Council of Real Estate Investment Fiduciaries (NCREIF) Index, a quarterly time series composite total rate of return measure of investment performance of a very large pool of individual commercial real estate properties acquired in the private market for investment purposes only, real estate returned 16.03% during the past fiscal year. Index returns are reported on a quarter lag due to the time taken to acquire this information from private market sources, so the returns are for the twelve months ended March 31, 2011. Investment performance in the private real estate markets have partially rebounded from significant declines since the beginning of the credit crisis in 2008.

The absolute return program had a strong fiscal year generating a total return of 13.18%, 518 basis points above its benchmark return of 8.00%. Returns were generated primarily from global macro managers who had their portfolios properly positioned for the current economic environment to take advantage of mispricings in the market. The absolute return program is structured to have low beta to the equity, fixed income, and commodity markets and to provide additional diversification from the remainder of the asset allocation.

As a result of strong returns from global equities, alternative investments, commodities, and the absolute return program, the System generated a total return of 20.37% for the one-year period ended June 30, 2011. This return exceeded the total fund Policy Index return of 17.56% by 281 basis points. Annualized total returns for the three-, five-, and ten-year periods ended June 30, 2011 were 0.44%, 3.89%, and 6.25%, respectively. The return for the three-year period ended June 30, 2011 fell short of the total fund Policy Index return by 66 basis points while the returns for the five- and ten-year periods ended June 30, 2011 exceeded the total fund Policy Index returns by 16 and 94 basis points, respectively.

Wilshire calculates the total investment return of the System as well as the performance of each external investment management firm and each internal investment manager employed by the Board to invest the System's assets. Performance is calculated using a time-weighted return methodology.

The following table provides the System's total investment return for each major asset class and the total portfolio, including, where applicable and available, respective benchmark indexes used by asset class and median performance by asset class:

	Annualized Total Returns (%) Net of Fees Ended June 30, 2011			
	1 Year	**3 Years**	**5 Years**	**10 Years**
PSERS Total Portfolio	**20.37**	**0.44**	**3.89**	**6.25**
Total Fund Policy Index	17.56	1.10	3.73	5.31
Median Public Defined Benefit Plan (DBP) Fund Universe (Wilshire Database)	21.87	3.53	4.56	6.04
PSERS U.S. Equity Portfolios	**32.69**	**3.57**	**2.81**	**3.73**
U.S. Equity Policy Index (1)	31.98	3.77	3.32	3.67
Median Public DBP Fund Universe - U.S. Equities (Wilshire Database)	32.62	4.23	3.21	3.75
PSERS Non-U.S. Equity Portfolios	**30.44**	**3.78**	**5.78**	**9.03**
MSCI All Country World ex. U.S. Investable Market Index (2)	30.26	1.96	4.50	8.11
Median Public DBP Fund Universe - Non-U.S. Equities (Wilshire Database)	30.84	-0.51	2.53	6.92
PSERS U.S. Fixed Income Portfolios	**11.55**	**10.26**	**8.85**	**7.60**
U.S. Fixed Income Policy Index (3)	10.38	10.59	9.32	7.17
Median Public DBP Fund Universe - U.S. Bonds (Wilshire Database)	7.06	7.73	6.63	6.15
PSERS Global Fixed Income Portfolios	**14.41**	**9.75**	**8.78**	**8.84**
Global Fixed Income Policy Index (4)	15.98	7.47	7.87	8.07
Median Public DBP Fund Universe - Global Bonds (Wilshire Database)	13.90	8.87	8.16	8.03
PSERS Commodity Portfolios	**31.84**	**-8.47**	**N/A**	**N/A**
Dow Jones - UBS Commodity Index	25.91	-11.87	N/A	N/A
PSERS Absolute Return Portfolios	**13.18**	**N/A**	**N/A**	**N/A**
Benchmark - 8.00% Annualized Return	8.00	N/A	N/A	N/A
PSERS Real Estate (5)	**20.18**	**-14.98**	**-5.42**	**6.01**
Blended Real Estate Index (6)	20.04	-1.09	3.85	8.50
Median Public DBP Fund Universe - Real Estate (Wilshire Database)	20.80	-4.13	0.48	6.76
PSERS Alternative Investments (5)	**18.60**	**1.84**	**11.36**	**10.87**
Venture Economics Median Return, Vintage Year Weighted	11.37	2.82	5.49	4.04
Median Public DBP Fund Universe - Private Equity (Wilshire Database)	22.03	4.20	10.78	9.41

1. MSCI USA Investable Market Index effective April 1, 2009; previously was the Dow Jones Wilshire 5000 Index.
2. MSCI All Country World (ACW) ex. USA Investable Market Index effective July 1, 2008; previously was the MSCI ACW ex. U.S. Index. The benchmark was 30% hedged to the U.S. dollar from July 1, 2006 to March 31, 2009; otherwise, the benchmark is unhedged.
3. Returns presented are a blend of the Barclays Capital U.S. Universal Index (27.8%), Barclays Capital U.S. TIPS Index (Series-L) (27.8%), and Barclays U.S. High Yield Index (44.4%) effective April 1, 2010. The weights to these indexes have varied in previous quarters. Prior to April 1, 2007, the Barclays Capital Aggregate Bond Index was used in place of the Barclays Capital U.S. Universal Index.
4. Returns presented are a blend of the Barclays Multiverse Index (40.8%) and the JP Morgan Global Bond Index Emerging Markets Global Diversified (USD Unhedged) Index (59.2%) Between April 1, 2007 and March 31, 2010, the Barclays Multiverse Index was used; previous to April 1, 2007, the Barclays Global Aggregate Bond Index was used.
5. Returns reported on a one-quarter lag, except for publicly traded real estate security investments.
6. NCREIF Index effective April 1, 2010. The NCREIF Index is reported on a one-quarter lag. Previously, returns presented were a blend of the FTSE EPRA/NAREIT Global Real Estate Index and the NCREIF Index. Prior to October 1, 2007, the Dow Jones Wilshire Real Estate Securities Index was used in place of the FTSE EPRA/NAREIT Global Real Estate Index.

The System also is involved in a securities lending program administered by The Bank of New York Mellon Corporation. This program is designed to provide incremental income to the System by lending securities in the System's portfolio to securities dealers in exchange for either cash collateral, which can be reinvested to generate income, or non-cash collateral plus a cash fee. This program generated $7.2 million in net gains during the year.

Accomplishments

The System continued its efforts to diversify its market exposures during the second quarter of FY 2011 as the target allocation to absolute return mandates, an asset class used as a risk diversifier added during the current fiscal year, was increased from 10.0% to 12.0%.

Recognizing the low return environment and the risks associated with reaching for too much return, the Board lowered the actuarial assumed rate of return, which was reduced from 8.0% to 7.5% effective with the June 30, 2011 actuarial valuation. This change allows the System to design an asset allocation with lower risk parameters given the continued uncertainty of the economic environment.

Summary

The System had a very good fiscal year ended June 30, 2011. Most risk assets across the spectrum performed well, allowing the System to generate returns substantially in excess of the actuarial investment rate of return assumption. The System was unable to meet or exceed this assumption for the three-, five-, and ten-year periods ended June 30, 2011. For the twenty-five-year period ended June 30, 2011, however, the System generated a return of 8.79%, well in excess of the actuarial investment rate of return assumption. We continue to believe that we are in the midst of a challenging period for asset returns for the reasons discussed above. We also believe, however, that the System's asset allocation is structured to generate a long-term return that meets or exceeds the targeted actuarial rate of return assumption of the System.

Alan H. Van Noord, CFA
Chief Investment Officer

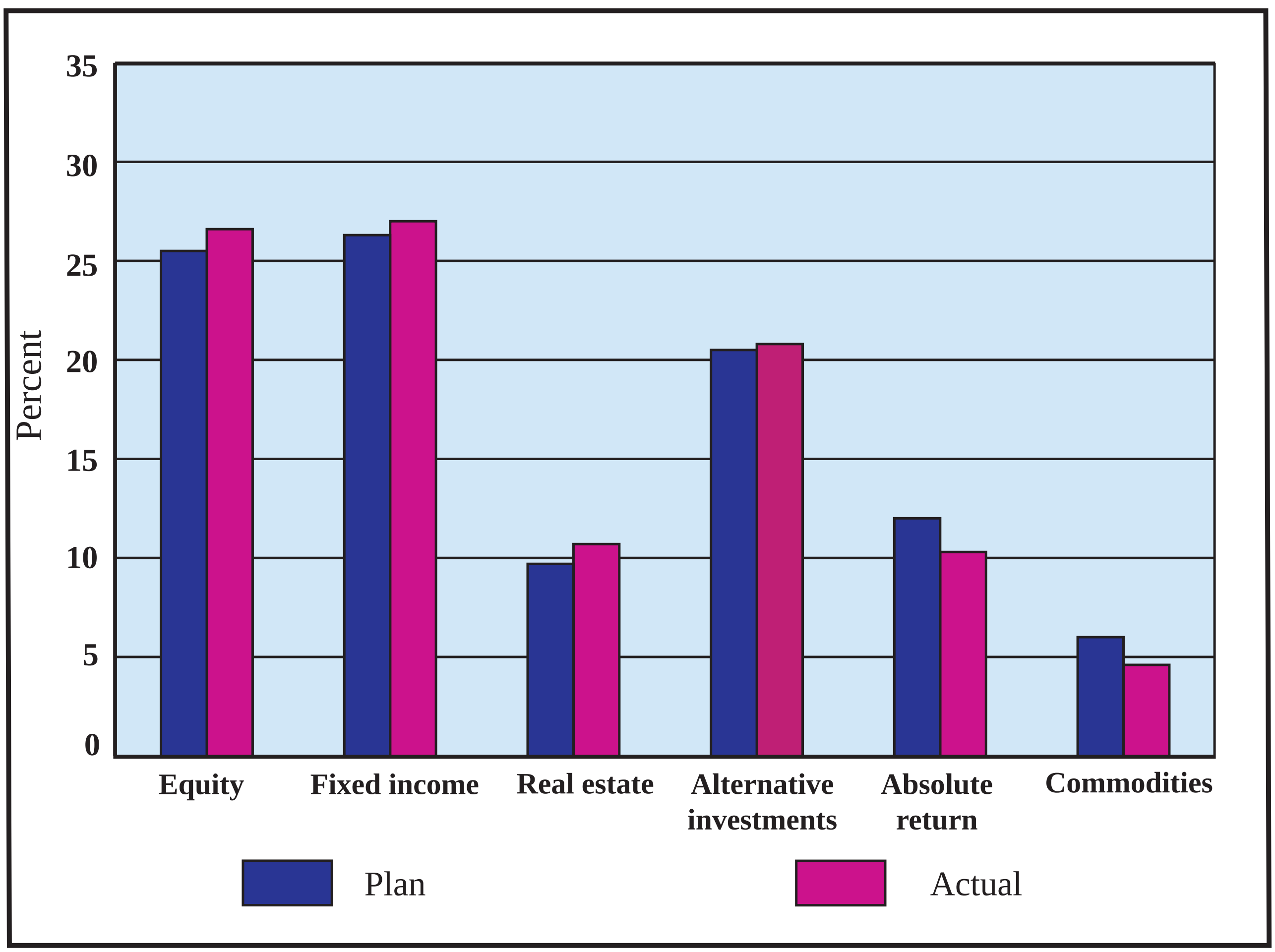
Portfolio Summary Statistics
Asset Allocation
As of June 30, 2011
(Dollar Amounts in Thousands)

Pension investments	Fair Value ($)	% Fair Value
Common and preferred stock (Equity):		
Large cap stocks	4,720,254	9.2
Mid and small cap stocks	1,043,757	2.0
Emerging markets stocks	1,968,476	3.8
Total Non-U.S. equity	**7,732,487**	**15.0**
Large cap stocks	4,153,489	8.1
Mid and small cap stocks	1,639,709	3.2
Microcap stocks	130,700	0.3
Total U.S. equity	**5,923,898**	**11.6**
Total Common and preferred stock - Asset Allocation Basis	**13,656,385**	**26.6**
Fixed income:		
Investment grade fixed income	5,223,403	10.2
High yield and opportunistic fixed income	2,787,758	5.4
Total U.S. Fixed income	**8,011,161**	**15.6**
Global core fixed income	882,037	1.7
Emerging markets fixed income	886,162	1.6
Total Global Fixed income	**1,768,199**	**3.3**
Cash and cash equivalents	**4,160,513**	**8.1**
Total Fixed income - Asset Allocation Basis	**13,939,873**	**27.0**
Real estate	**5,467,929**	**10.7**
Alternative investments:		
Private equity	7,821,209	15.2
Private debt	2,024,155	3.9
Venture capital	849,135	1.7
Total Alternative investments - Asset Allocation Basis	**10,694,499**	**20.8**
Absolute return	**5,297,524**	**10.3**
Commodities	**2,388,292**	**4.6**
Total Pension investments - Asset Allocation Basis	**51,444,502**	**100.0**
Net Asset Allocation Adjustment*	158,174	
Pension investments per Statement of Plan Net Assets	**51,602,676**	
Postemployment Healthcare investments	**226,488**	**100.0**

* Includes reclassifications of certain investments between asset classes and investment receivables\payables to adjust the Statement of Plan Net Assets classification to the basis used to measure Asset Allocation. See the table and graph which follow.

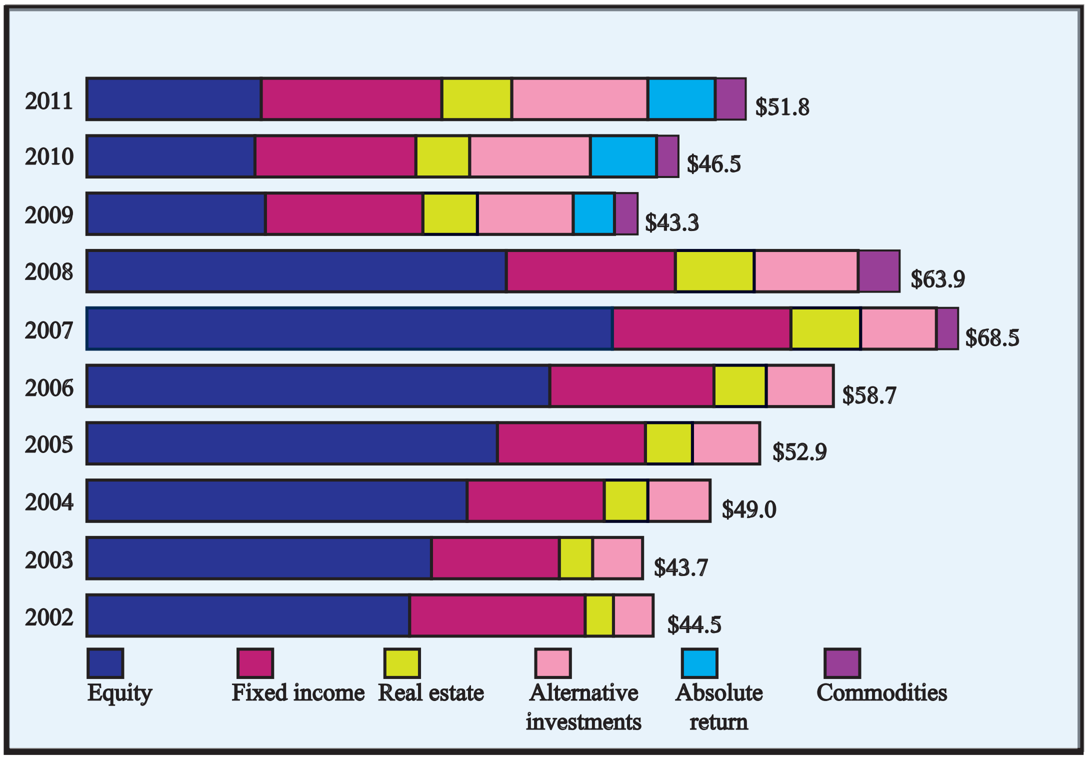
Comparison of Actual Portfolio Distribution to Asset Allocation Plan As of June 30, 2011

Asset Category	Plan	Actual
Common and preferred stock (Equity)	25.5%	26.6%
Fixed income	26.3%	27.0%
Real estate	9.7%	10.7%
Alternative investments	20.5%	20.8%
Absolute return	12.0%	10.3%
Commodities	6.0%	4.6%
Total	100.0%	100.0%



Portfolio Distribution 10 Year Trend

(Fair Value - Dollar Amounts in Billions)



The following lists of portfolio detail statistics present the ten largest holdings by descending order of fair value for the largest asset classes. Information on the complete holdings of the System is available by writing to the Public School Employees' Retirement System, Press Secretary, P. O. Box 125, Harrisburg, PA 17108.

Common and Preferred Stock - Non-U.S. Equity

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2011

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
BlackRock Emerging Markets Strategic Insights Fund	4,004	205,687
The 32 Capital Fund Ltd.	98	130,775
BHP Billiton Ltd.	1,930	118,806
Rio Tinto PLC	741	108,519
Royal Dutch Shell PLC	1,902	104,398
BlackRock Emerging Markets Alpha Advantage Fund Ltd.	34	103,130
Nestle SA	1,239	76,881
BP PLC	6,159	70,718
Schlumberger Ltd.	425	60,740
Shah Capital Offshore Opportunity Fund	415	55,862
Total of 10 Largest Holdings		**1,035,516**

Common and Preferred Stock - U.S. Equity

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2011

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
Security Capital Preferred Growth	13,039	177,582
Exxon Mobil Corporation	1,569	127,687
Apple Computer, Inc.	300	100,615
Chevron Corporation	652	67,099
IBM	380	65,146
General Electric Company	3,325	62,712
Microsoft Corporation	2,327	60,493
Johnson & Johnson	882	58,694
AT&T Inc.	1,857	58,320
Procter & Gamble Company	902	57,312
Total of 10 Largest Holdings		**835,660**

Fixed Income

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2011

(Dollar Amounts and Shares in Thousands)

Description	Maturity Date	Interest Rate (%)	Par Value($) or No. of Shares	Fair Value ($)
Bridgewater All Weather @ 12%, Ltd.	N/A	N/A	594	606,808
BlackRock US Extended Core Global Alpha Fund	N/A	N/A	359	507,405
Bridgewater Int'l Inflation-Linked Bond Fund	N/A	N/A	250	394,143
Bridgewater Pure Alpha Fund II Ltd.	N/A	N/A	140	348,344
U.S. Treasury - Inflation Index	01/15/25	2.375	190,411	218,854
Bridgewater U.S. Inflation-Linked Bond Fund	N/A	N/A	90	143,825
U.S. Treasury - Inflation Index	01/15/16	2.000	106,040	117,854
U.S. Treasury - Inflation Index	01/15/14	2.000	81,780	88,105
U.S. Treasury - Inflation Index	02/15/40	2.125	79,794	86,832
U.S. Treasury - Inflation Index	02/15/41	2.125	76,804	83,446
Total of 10 Largest Holdings				**2,595,616**

Absolute Return

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2011

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
Bridgewater Pure Alpha Fund II Ltd.	360	885,771
Brigade Leveraged Capital Structures Offshore Ltd.	633	847,346
AQR Offshore Multi-Strategy Fund Ltd.	8	797,727
BlackRock Global Ascent Ltd.	500	724,917
Brevan Howard Fund, Ltd.	3,194	364,700
Capula Tail Risk Fund Ltd.	2,500	251,322
BlackRock Capital Structure Investments Fund Ltd.	198	218,996
PIMCO Absolute Return Strategy V Offshore Fund	117	217,738
PIMCO Global Credit Opportunity Offshore Fund	159	215,932
The Boston Company Microcap Portfolio	149	207,509
Total of 10 Largest Holdings		**4,731,958**

Postemployment Healthcare Investments

10 Largest Holdings in Descending Order by Fair Value

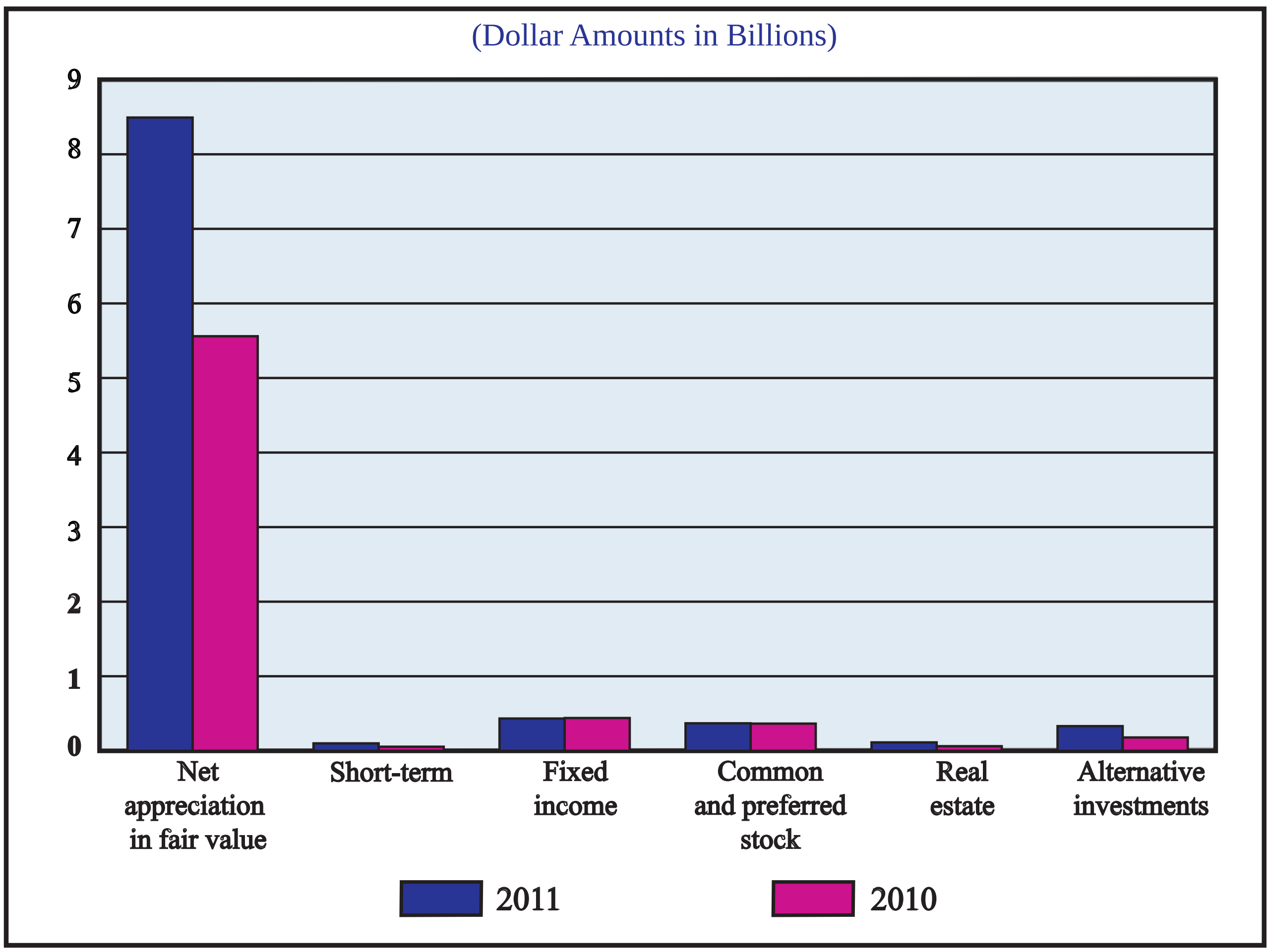
As of June 30, 2011

(Dollar Amounts in Thousands)

Description	Maturity Date	Interest Rate (%)	Par Value ($)	Fair Value ($)
PSERS Short-Term Investment Fund	Various	Various	112,277	112,277
M & T Bank Repurchase Agreement	7/1/11	0.010	28,292	28,292
M & T Bank Repurchase Agreement	7/1/11	0.010	21,407	21,407
M & T Bank Repurchase Agreement	7/1/11	0.010	8,116	8,116
GNMA Guaranteed REMIC 2004-29 Class B	8/16/29	5.000	2,914	2,908
GNMA Guaranteed REMIC 2006-60 Class PA	1/20/36	5.000	2,853	2,857
FHLMC Multiclass 2799 Class PF	1/15/31	0.537	2,792	2,791
FHLMC Multiclass 3545 Class LA	12/15/16	2.120	2,563	2,563
FHLMC Multiclass 2885 Class DT	5/15/18	4.500	2,306	2,303
FNMA Guaranteed REMIC 2005-118 Class ME	1/25/32	6.000	2,122	2,090
Total of 10 Largest Holdings				**185,604**

Comparison of Investment Activity Income
For Fiscal Years Ended June 30, 2011 and 2010
(Dollar Amounts in Thousands)

Investment Activity	**2011**	2010
Net appreciation in fair value of investments	$ **8,493,206**	$ 5,560,380
Short-term	**15,128**	21,410
Fixed income	**432,649**	440,358
Common and preferred stock	**368,901**	365,255
Real estate	**113,370**	62,273
Alternative investments	**331,286**	179,116
Total investment activity income	$ **9,754,540**	$ 6,628,792



Brokers' fees on equity investment transactions for the fiscal year ended June 30, 2011 were $11.8 million. The System has commission recapture contracts with several brokers. These contracts generally stipulate that the brokers rebate a percentage of commissions earned on investment transactions directly to the System. During the fiscal year ended June 30, 2011, the System earned $254,000 from the commissions recapture program. A list of the brokers receiving fees in excess of $100,000 during the fiscal year follows:

Summary Schedule of Brokers' Fees
(Cumulative Fiscal Year Amounts Exceeding $100,000)
Fiscal Year Ended June 30, 2011

Broker Name	Fees Paid ($)	Broker Name	Fees Paid ($)
Jones & Associates	1,651,302	Macquaries Equities Limited	236,756
Goldman Sachs & Company	1,550,678	Credit Lyonnais Securities	224,393
Instinet Corporation	922,781	Cantor, Fitzgerald & Company	211,274
UBS Securities	527,540	Liquidnet Incorporated	188,592
Citigroup	475,654	Barclays	171,047
Merrill Lynch	424,831	Nomura Securities International	166,185
JP Morgan Chase & Company	424,197	Fimat USA	157,521
Credit Suisse	386,578	BNY Convergex	139,434
Knight Securities	314,392	B-Trade Services, LLC	120,924
Morgan Stanley & Company	292,625	HSBC Securities Incorporated	103,751
Deutsche Bank	270,065		

Professional Consultants
External Investment Advisors
As of June 30, 2011

Absolute Return Managers

- AQR Capital Management, LLC
- BlackRock Financial Management, Inc.
- Boston Company Asset Management, LLC (The)
- Brevan Howard Asset Management, LLP
- Bridgewater Associates, Inc.
- Brigade Capital Management
- Capula Investment Management, LLP
- Caspian Capital Advisors
- FX Concepts, LLC
- Lazard Asset Management, LLC
- Pacific Investment Management Company
- Pareto Investment Management, Ltd.

U.S. Style-Oriented Small Cap Equity Manager

- First Pacific Advisors, Inc.

U.S. Micro Cap Equity Manager

- NorthPointe Capital, LLC

Publicly-Traded Real Estate Securities Manager

- Security Capital Research & Management, Inc.

Non-U.S. Large Cap Equity Managers

- Baillie Gifford Overseas, Ltd.
- BlackRock Financial Management, Inc.
- Marathon Asset Management, LLP

Active Currency Program Manager

- Pareto Investment Management, Ltd.

Non-U.S. Small Cap Equity Managers

- Acadian Asset Management, Inc.
- Batterymarch Financial Management, Inc.
- Oberweis Asset Management, Inc.
- Pyramis Global Advisors, Inc.
- Wasatch Advisors, Inc.

Non-U.S. Emerging Markets Equity Managers

- Batterymarch Financial Management, Inc.
- Wasatch Advisors, Inc.
- Wellington Management Company, LLP

Enhanced Commodity Index Managers

- Credit Suisse Asset Management, LLC
- NB Alternative Fund Management, LLC

Professional Consultants (Continued)

Full Discretion Commodity Managers

- DB Advisors
- Schroders Investment Mgmt. North America, Inc.
- Wellington Management Company, LLP

U.S. Core Plus Fixed Income Managers

- BlackRock Financial Management, Inc.
- Pacific Investment Management Company
- Western Asset Management Company

U.S. High Yield Fixed Income Manager

- MacKay-Shields Financial Corporation

Global Core Plus Fixed Income Managers

- Aberdeen Asset Management, Inc.
- Fischer Francis Trees & Watts, Inc.
- Rogge Global Partners

Emerging Markets Debt Managers

- Franklin Templeton Investments
- Stone Harbor Investment Partners, LP

Global Treasury Inflation - Protected Securities Manager

- Bridgewater Associates, Inc.

Credit Opportunities Managers

- BlackRock Financial Management, Inc.
- Brookfield Investment Management, Inc.
- LBC Credit Partners
- Mariner Investment Group, LLC
- Oaktree Capital Management, LP
- Sankaty Advisors, LLC

Real Estate Advisors

- Charter Oak Advisors, Inc.
- GF Management, Inc.
- Grandbridge Real Estate Capital, LLC
- Grosvenor Investment Management U.S., Inc.
- L&B Realty Advisors, LLP

Short-Term Investment Manager

- Bridgewater Associates, Inc.

Real Estate Partnerships

- Apollo European Real Estate Fund III, LP
- Apollo Real Estate Finance Corporation
- Apollo Value Enhancement Fund VII, LP
- AREFIN Co-Invest Corporation
- AvalonBay Value Added Fund I & II, LP
- Avenue Real Estate Fund Parallel, LP
- Beacon Capital Strategic Partners V, LP
- Blackstone Real Estate Partners V & VI.TE.1, LP
- Blackstone Real Estate Partners Europe III, LP
- BPG Investment Partnership V & VI, LP
- BPG Co-Investment Partnership, LP
- Broadway Partners Real Estate Fund II & III, LP
- Cabot Industrial Value Fund III, LP
- Carlyle Europe Real Estate Partners III-A, LP
- Carlyle Realty Partners III, IV & V, LP
- Cornerstone Patriot Fund, LP
- CS Strategic Partners IV RE, LP
- CSFB Strategic Partners II & III RE, LP
- DLJ Real Estate Capital Partners II, III & IV, LP
- DRA Growth and Income Fund VI, LLC
- Fillmore West Fund, LP
- Five Arrows Realty Securities V, LP
- Fortress Investment Fund I, IV & V, LP
- Hines U.S. Office Value Added Fund, LP
- JPMCB Strategic Property Fund
- Lazard Freres Real Estate Investors I & II, LLC
- LCCG Real Estate Special Situations Mortgage Fund, LLC
- Legg Mason Real Estate Capital I & II, Inc.
- LEM Real Estate Mezzanine Fund II, LP
- Lubert-Adler Real Estate Fund III, IV, V, & VI, LP
- Madison Marquette Retail Enhancement Fund, LP
- MGPA Asia Fund III, LP
- MGPA Europe Fund III, LP
- Morgan Stanley Real Estate Fund II, LP
- Morgan Stanley Real Estate Fund IV Special Domestic, LP
- Morgan Stanley Real Estate Fund IV, V & VI Special International, LP
- Morgan Stanley Real Estate Fund V Special U.S., LP
- Morgan Stanley Real Estate Fund VII Global, LP
- O'Connor North American Property Partners I & II, LP
- Paladin Realty Latin America Investors III, LP
- Peabody Global Real Estate Partners, LP
- Prime Property Fund, LLC
- PRISA
- ProLogis North American Industrial Fund, LP
- RCG Longview Debt Fund IV, LP
- RCG Longview Equity Fund, LP
- RREEF America REIT II, Inc.
- Silverpeak Legacy Partners I, II & III, LP
- Stockbridge Real Estate Fund I, II & III, LP
- Strategic Partners Value Enhancement Fund, LP
- UBS (US) Trumbull Property Fund, LP
- Westbrook Real Estate Fund, LP
- Whitehall Street Real Estate V, VI, VII & VIII, LP
- William E. Simon & Sons Realty Partners, LP

Farmland Advisor

- Prudential Agricultural Group

Professional Consultants (Continued)

Private Equity/Venture Capital Partnerships

- ABS Capital Partners II, LP
- Actis Emerging Markets 3, LP
- Adams Capital Management, LP
- Aisling Capital Partners II & III, LP
- Allegheny New Mountain Partners, LP
- Apax Europe VII, LP
- Baring Asia Private Equity Fund III, IV & V, LP
- Blue Point Capital Partners (B) I & II, LP
- Bridgepoint Capital II Partnership, LP
- Bridgepoint Europe IA, IIA, IIIA & IV, LP
- Bruckmann, Rosser, Sherrill & Company, LP
- Capital International Private Equity Fund V, LP
- Catterton Growth Partners, LP
- Catterton Partners V & VI, LP
- Cinven Fund (Fourth), LP (The)
- Clarity Partners I & II, LP
- Co-Investment 2000 Fund, LP (The)
- Co-Investment Fund II, LP (The)
- Credit Suisse First Boston Equity Partners, LP
- Credit Suisse First Boston International Equity Partners, LP
- Crestview Capital Partners I & II, LP
- Cross Atlantic Technology Fund I & II, LP
- CSFB Strategic Partners II, III-B & III-VC, LP
- CS Strategic Partners Fund IV & IV VC, LP
- CVC Capital Partners Asia Pacific III, LP
- CVC European Equity Partners V, LP
- DLJ Merchant Banking Partners III, LP
- DLJ Strategic Partners, LP
- Dubin Clark Fund II, LP
- Edgewater Growth Capital Partners, LP
- Edgewater Private Equity Fund III, LP
- Evergreen Pacific Partners I & II, LP
- First Reserve Fund XI & XII, LP
- Franklin Capital Associates III, LP
- Furman Selz Investors III, LP
- Graham Partners Investments (B), LP
- Green Equity Investors II, LP
- Greenpark International Investors III, LP
- Greenwich Street Capital Partners II, LP
- Halifax Capital Partners, LP
- Headland Private Equity Fund 6, LP
- Irving Place Capital Partners II & III, LP
- Jefferies Capital Partners IV, LP
- Jefferson Partners Fund IV (PA), LP
- KBL Healthcare Ventures, LP
- KKR 2006 Fund, LP
- KRG Capital Fund II, III & IV, LP
- Landmark Equity Partners II, III, IV, V, XIII & XIV, LP
- Landmark Mezzanine Partners, LP
- Lexington Capital Partners, LP
- Lindsay, Goldberg & Bessemer, LP
- LLR Equity Partners I, II & III, LP
- Milestone Partners II & III, LP
- Morgan Stanley Dean Witter Capital Partners IV, LP
- Navis Asia Fund V, LP
- NEPA Venture Fund II, LP
- New Mountain Partners I & III, LP
- New York Life Capital Partners, I, II, III & IV, LP
- Nordic Capital VII Beta, LP
- Novitas Capital I & II, LP
- P/A Fund (The)
- PAI Europe III, IV & V, LP
- Palladium Equity Partners II-A, LP
- Partners Group Secondary 2008, LP
- Permira IV, LP
- Perseus-Soros BioPharmaceutical Fund, LP
- Platinum Equity Capital Partners-A I & II, LP
- PNC Equity Partners I & II, LP
- Providence Equity Partners VI, LP
- Psilos Group Partners III, LP
- Quadrangle Capital Partners I & II, LP
- Quaker BioVentures I & II, LP
- SCP Private Equity Partners I & II, LP
- StarVest Partners I & II, LP
- Sterling Capital Partners, LP
- Sterling Venture Partners, LP
- TDH III, LP
- Tenaya Capital IV-P & V, LP
- TL Venture III, LP
- TPG Partners II, V & VI, LP
- Trilantic Capital Partners IV, LP
- U.S. Equity Partners II, LP
- Wicks Communications & Media Partners, LP
- Willis Stein & Partners, LP

Private Debt Partnerships

- Avenue Asia Special Situations Fund II, III & IV, LP
- Avenue Europe Special Situations Fund, LP
- Avenue Special Situations Fund IV, V & VI, LP
- Cerberus Institutional Partners, LP (Series Two, Three and Four)
- Gleacher Mezzanine Fund I & II, LP
- Gold Hill Venture Lending 03-A, LP
- GSC Partners CDO Investors IV, LP
- GSC Recovery II & III, LP
- NYLIM Mezzanine Partners Parallel Fund I & II, LP
- OCM Opportunities Fund VII & VII-B, LP
- Versa Capital Fund I & II, LP
- Windjammer Senior Equity Fund III, LP

Public Market Emerging Investment Program Managers

- AH Lisanti Capital Growth, LLC
- Ativo Capital Management, LLC
- Conestoga Capital Advisors
- Denali Advisors, LLC
- EDMP, Inc.
- Harvest Fund Advisors, LLC
- Hellman, Jordan Management Company, Inc.
- John Hsu Capital Group, Inc.
- Opus Capital Group, LLC
- Piedmont Investment Advisors, LLC
- Pugh Capital Management, Inc.
- Shah Capital Management, Inc.
- Westwood Global Investments, LLC

Professional Consultants (Continued)

Alternative Investment Consultant

- Portfolio Advisors, LLC

Custodian Bank and Securities Lending Agent

- The Bank of New York Mellon Corporation

Investment Accounting Application Service Provider

- Financial Control Systems, Inc.

Investment Evaluator and General Investment Consultant

- Wilshire Associates, Inc.

Proxy Voting Agent

- Glass, Lewis & Co., LLC

Real Estate Investment Consultant

- Courtland Partners, Ltd.

Hedge Fund Consultant

- Aksia, LLC