Investment

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COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

ALAN H. VAN NOORD, CFA
Chief Investment Officer

Investment Overview

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 (currently 8.0%) 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, which is based on the Board-established asset allocation structure, is a custom benchmark designed to generate a return that meets the actuarial rate of return assumption).

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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 12% 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 at least once per 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 internal investment managers. The Board also retains various investment consultants to assist with the formulation and implementation of investment policies.

Operations

The Board provides oversight of investment activities through the Finance Committee that makes recommendations to the Board. 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, 2009, 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 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 Investment Policy Statement, Objectives and Guidelines regarding asset allocation, 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, 54 external public market investment management firms were managing $16.8 billion in assets of the System, $13.3 billion in assets were managed by the System's internal investment managers, and the remaining $13.2 billion in assets were managed by numerous emerging, alternative investment, and real estate 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 its peer group.

Asset Allocation

The Board reviews the long-term asset allocation targets of the System at least annually, usually in the first quarter of the 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, 2009 included an equity target allocation of **31.0%** consisting of publicly traded stocks. Specific targets have been established for U.S. equity exposure (13.2%) and international equity exposure (17.8%). 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 international equity exposure includes both developed and emerging markets portfolios as well as large and small capitalization investment managers.

The fixed income target allocation of **29.5%** consisted of U.S. core fixed income exposure (7.5%), leveraged Treasury Inflation-Protected Securities exposure (5.0%), high yield and opportunistic fixed income exposure (9.0%), global fixed income exposure (3.0%) and cash (5.0%). Historically, PSERS had an allocation of 0.0% to cash, however, given the known and potential cash flow requirements of the System, the Board, Staff, and Wilshire deemed it prudent to have an allocation to this asset class. Within these categories, all sectors of the bond market are represented.

The real estate target allocation of **11.0%** consisted primarily of opportunistic limited partnerships and publicly traded real estate securities.

Alternative investments had a target of **17.0%**. 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 and unlisted subordinated debt positions on behalf of PSERS and other limited partners.

The absolute return target allocation of **7.5%** 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 goal 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 the targeted actuarial rate of return of 8.0% and to diversify the System's total portfolio risk.

The commodities target allocation of **4.0%** 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, 2009, the fair value of the investment portfolio was $43.3 billion, a decrease of $20.6 billion from last year's value. This decrease came primarily from net investment losses ($16.2 billion) and benefit payments in excess of member and employer contributions ($3.3 billion) which was partially offset by net changes in other investment assets and liabilities ($1.1 billion). The investment portfolio, as invested, was composed of 32.4% common and preferred stocks (equity), 28.6% fixed income investments, 17.4% alternative investments, 9.9% real estate, 7.5% absolute return portfolios, and 4.2% commodities at June 30, 2009. The table immediately following the Investment Overview illustrates a more detailed description of the investment portfolio's asset classes in dollars and as a percentage of the total investment portfolio.

The past fiscal year saw the worst economic contraction in the United States since the Great Depression. The U.S. Gross Domestic Product (GDP) dropped by 2.7%, 5.4%, 6.4%, and 0.7% in the third quarter 2008, fourth quarter 2008, first quarter 2009, and second quarter 2009, respectively. The U.S. unemployment rate hit a cyclical low of 4.4% in March 2007, increased to 9.8% in September 2009, and is projected by some to eventually reach or exceed 10%. Coming into the fiscal year, the recent credit crises that started with the popping of the housing bubble and subprime meltdown reached a crescendo in September 2008 with numerous failures of large financial institutions. These included the federal government taking over Fannie Mae and Freddie Mac, the Lehman Brothers Holdings, Inc. bankruptcy, the AIG bailout by the federal government, and the Washington Mutual bankruptcy. These events and other financial stresses were driven by an extreme contraction in liquidity. In response, the U.S. Federal Reserve (the Fed) lowered the target Federal Funds rate to a 0.00% - 0.25% floor in the fourth quarter of 2008 and instituted numerous other quantitative easing programs to supply liquidity to the market. The Fed embarked on quantitative easing programs since they could not cut interest rates below 0.00%. The U.S. government started programs to help fill the void created by reduced economic activity in the private sector, such as the $787 billion fiscal stimulus package in February 2009. The size of the government purchases and guarantees was estimated by one of the System's managers to be over $29 trillion, or 200% of GDP.

A logical question arises as to how we have arrived here. While no one knows for certain, it appears that the credit/financial crisis can be traced back to lax underwriting standards for home loans during this decade which spawned a housing and credit bubble. This bubble allowed consumers to borrow against their homes, which significantly reduced homeowners' equity value (defined as fair market value of the house minus the outstanding mortgage balance). This borrowing helped to push the U.S. total debt as a percentage of GDP to 350%, much higher than the levels reached during the Great Depression (250%) and allowed the consumer to spend beyond his/her means as the savings rate in the United States went negative. Housing prices peaked in July 2006 and fell 31.3% by June 2009 according to the S&P/Case-Shiller Composite-20 Home Price Index which measures home prices in 20 metropolitan markets. This drop in home prices has led to a large number of consumers having zero or negative equity in their homes. As the ability of consumers to borrow against the equity in their homes ended, consumption slowed and the unemployment rate increased leading to a significant contraction in economic activity in the United States which spilled over to the world markets. The slowdown in spending was exacerbated by an estimated $14 trillion decline in consumer net worth. This contraction in consumer net worth led to an increased savings rate, which further decreased monies that can be used for consumption.

In this environment, equity, real estate, and commodity markets around the world had sharply negative returns during the fiscal year. The Morgan Stanley Capital International (MSCI) U.S. Broad Market Index, a U.S. equity index, returned -26.22% during the fiscal year. The past fiscal year saw the worst quarterly loss since the fourth quarter of 1987 (-22.76% in the quarter ended December 31, 2008) and the worst monthly loss since the crash of October 1987 (-17.65% in October 2008). Foreign markets in local currency terms fared equally as badly as the MSCI All-Country World (ACW) ex. U.S. Investable Market Index, an international equity index, which returned -24.12% when hedged back to the U.S. dollar. However, the unhedged MSCI ACWI ex. U.S. index returned -30.50%, much worse than the hedged index due to the strength of the U.S. dollar. 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 -13.36% during the fiscal year as these investments were written down to prices comparable to losses in the public equity markets. According to the FTSE EPRA/NAREIT Global Real Estate Index, a free-float index designed to track the performance of listed real estate companies and real estate investment trusts worldwide, global publicly traded real estate securities (PTRES) returned -35.22% during the past fiscal year. PTRES performance suffered due to the deterioration of credit markets, uncertain asset values, and the weakened outlook for the global economy. The Dow Jones – UBS Commodity Index, an index of 19 highly liquid and diversified commodities, returned -47.08% during the fiscal year as the severe economic contraction led to a decrease in economic growth projections and a resulting slowdown in demand for fuel and raw materials.

Fixed income markets performed better in this environment as interest rates fell and investors looked to reduce risk. The Barclays U.S. Universal Index, a U.S. fixed income index, was up 4.93% and the Barclays Multiverse Index, a global fixed income index, was up 2.54%. Returns in both of these indexes were driven by the Fed reducing the Fed Funds rate as well as falling inflation expectations due to the economic contraction. The Barclays U.S. TIPS Index, an index of U.S. treasury inflation protection securities, returned -1.11% driven by falling inflation expectations and slightly higher real yields.

As a result of the negative returns from domestic and international stock portfolios, alternative investments, real estate, and commodities, the System generated a total return of -26.54% for the one-year period ended June 30, 2009. This return fell short of the total fund Policy Index return of -20.67% by 587 basis points. Annualized total returns for the three-, five-, and ten-year periods ended June 30, 2009 were -4.26%, 2.68%, and 3.28%, respectively. The three-year returns ending June 30, 2009 fell short of the total fund Policy Index returns by 151 basis points while the five- and ten-year returns ending June 30, 2009 exceeded the total fund Policy Index returns by 17 and 82 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, 2009			
	1 Year	3 Years	5 Years	10 Years
PSERS Total Portfolio	**-26.54**	**-4.26**	**2.68**	**3.28**
Total Fund Policy Index	-20.67	-2.75	2.51	2.46
Median Public Defined Benefit Plan (DBP) Fund Universe (Wilshire Database)	-19.47	-3.61	2.39	2.71
PSERS Domestic Stock Portfolios	**-29.37**	**-9.90**	**-2.81**	**-0.49**
Domestic Equity Policy Index (1)	-26.30	-8.09	-1.58	-1.31
Median Public DBP Fund Universe - Domestic Equities (Wilshire Database)	-27.17	-8.95	-2.03	-0.94
PSERS International Stock Portfolios	**-25.66**	**-4.15**	**6.14**	**4.40**
International Equity Policy Index (2)	-27.01	-4.98	5.20	3.06
Median Public DBP Fund Universe - International Equities (Wilshire Database)	-31.11	-6.81	3.45	2.78
PSERS Domestic Fixed Income Portfolios	**-1.00**	**4.13**	**4.21**	**5.84**
Domestic Fixed Income Policy Index (3)	4.75	6.54	5.17	6.06
Median Public DBP Fund Universe - Domestic Bonds (Wilshire Database)	0.67	4.62	4.32	5.57
PSERS Global Fixed Income Portfolios	**0.98**	**5.17**	**4.98**	**5.80**
Global Fixed Income Policy Index (4)	2.54	6.46	5.40	6.03
Median Public DBP Fund Universe - Global Bonds (Wilshire Database)	1.38	5.17	4.98	5.88
PSERS Commodity Portfolios	**-45.09**	**N/A**	**N/A**	**N/A**
Dow Jones-UBS Commodity Index	-47.08	N/A	N/A	N/A
PSERS Real Estate (5)	**-42.68**	**-10.95**	**4.26**	**7.55**
Blended Real Estate Index (6)	-16.35	1.46	8.52	9.33
Median Public DBP Fund Universe - Real Estate (Wilshire Database)	-31.42	-5.41	5.44	7.92
PSERS Alternative Investments (5)	**-27.23**	**5.67**	**12.52**	**8.89**
Venture Economics Median Return, Vintage Year Weighted	-13.36	0.59	3.21	1.13
Median Public DBP Fund Universe - Private Equity (Wilshire Database)	-25.76	2.97	10.25	6.16

(1) MSCI U.S. Broad Market Index effective April 1, 2009; previously was the Dow Jones Wilshire 5000 Index.
(2) MSCI All Country World ex. U.S. 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 (34.9%), Barclays Capital U.S. TIPS Index (Series-L) (23.2%), and Barclays U.S. High Yield Index (41.9%) effective April 1, 2009. 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) Barclays Multiverse Index effective April 1, 2007; previously was the Barclays Global Aggregate Bond Index.
(5) Returns reported on a one-quarter lag, except for publicly traded real estate security investments.
(6) Returns presented are a blend of the FTSE EPRA/NAREIT Global Real Estate Index (13.6%) and the NCREIF Index (86.4%). The NCREIF Index is reported on a one-quarter lag. 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 $26.8 million in net losses during the year due to losses in the collateral reinvestment pool, primarily from investments in Sigma Finance, Inc., a structured investment vehicle that went bankrupt.

Accomplishments

The System decreased the actuarial investment rate of return assumption from 8.50% to 8.25% effective for the June 30, 2008 actuarial valuation. The Board also decreased the rate of return assumption further from 8.25% to 8.00% for the June 30, 2009 actuarial valuation. This was in expectation that the prospective returns from investment markets will be lower due to anticipated slower growth and a deleveraging of the U.S. economy. This 0.50% decrease has allowed the System to modify its asset allocation plan during FY 2009 to achieve this new return target with lower overall risk.

The System added and fully funded an allocation to cash during the fourth quarter of FY 2009 to provide for current and future liquidity needs. Given the current commitments the System has to alternative investments and real estate, as well as monthly benefit payments in excess of employer and member contributions, the System felt it prudent to allocate to cash. This allocation allows the System to fund these needs without selling assets at inopportune times.

The System continued its efforts to diversify its market exposures during the fourth quarter of FY 2009 as the target allocation to absolute return mandates, an asset class used as a risk diversifier added during the current fiscal year, was fully funded.

The System continued its multi-year project to implement an independent accounting book of record for the System's investment transactions and holdings. In FY 2009, the System continued the process of migrating its real estate and alternative investment portfolios to its internal accounting software provided by Financial Control Systems, Inc. and continued to develop various management reports using the internal accounting software.

Market Update

Subsequent to the close of FY 2009, the equity markets continued a broad rally that started in the middle of March 2009 as the domestic and international economies appeared to be bottoming and a number of "green shoots", or positive economic statistics, were starting to be priced by the market. For the quarter ended September 30, 2009, the MSCI U.S. Broad Market Index was up 16.47% while the MSCI ACW ex. U.S. Investable Market Index was up 20.05%. Fixed income markets also performed well as credit spreads continued to narrow and interest rates remained low. The Barclays U.S. Universal Index was up 4.48% during the quarter while the Barclays Multiverse Index was up 6.48%. Commodities also had a positive return for the quarter as the Dow Jones – UBS Commodity index was up 4.25%. The System's assets have increased by over $2 billion during the quarter ended September 30, 2009 as a result of positive investment performance offset partially by benefit payments in excess of member and employer contributions. The estimated return for the quarter was approximately 8.50%.

Summary

The System had a very challenging fiscal year ended June 30, 2009. The worst economic contraction since the Great Depression, deflating housing bubble, rising unemployment rate, and the credit crisis led to negative returns for most risk assets, including global equity markets, alternative investments, real estate, and commodities. For the fiscal year ended June 30, 2009, the System was unable to meet or exceed its long-term actuarial investment rate of return assumption of 8.0% on a three-, five-, or ten-year basis. While we believe that we are in the midst of a challenging period for asset returns, we continue to believe 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 for years to come.

Alan H. Van Noord, CFA
Chief Investment Officer

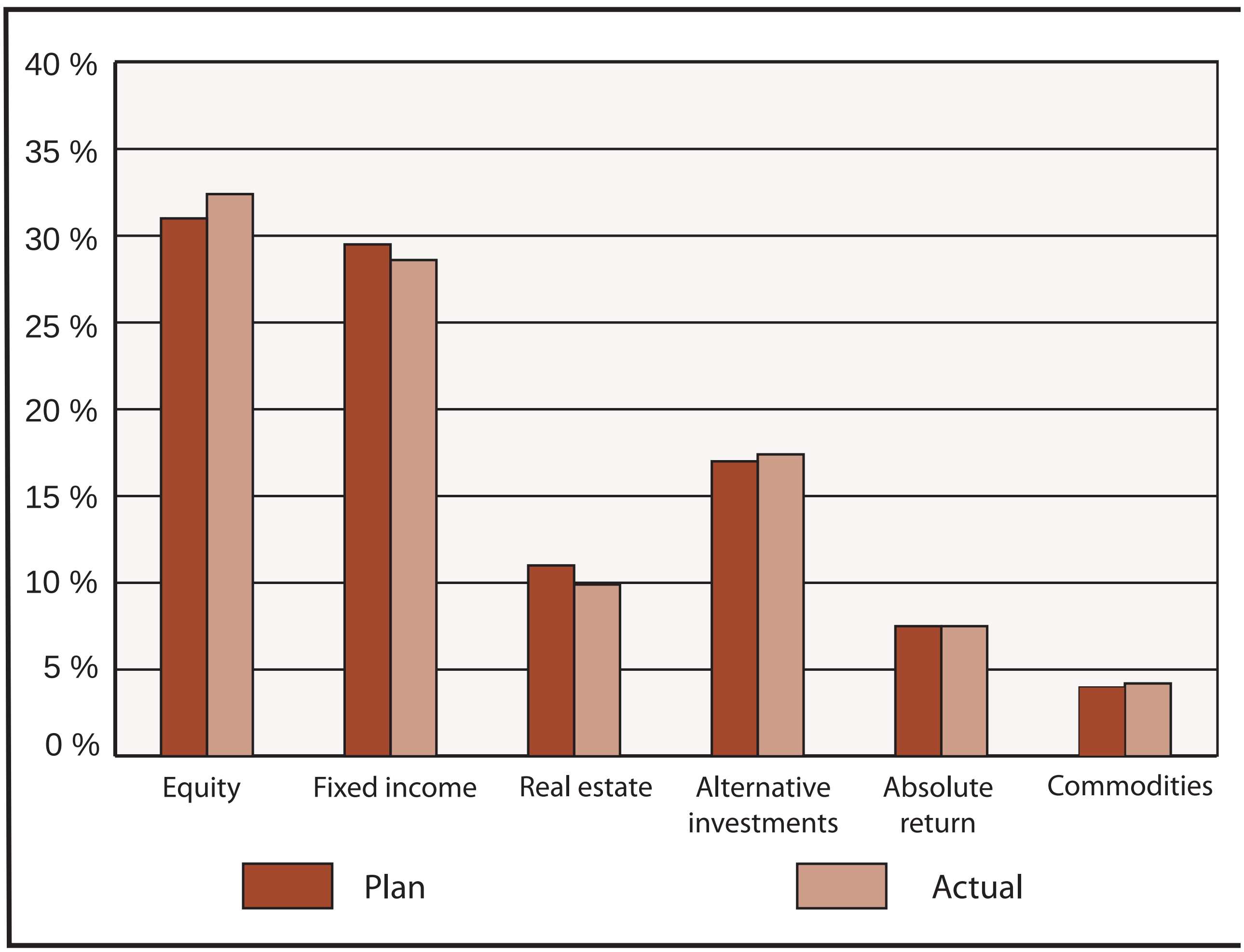
Portfolio Summary Statistics
Asset Allocation
As of June 30, 2009
(Dollar Amounts in Thousands)

Pension investments		Fair Value ($)	% Fair Value
Common and preferred stock (Equity):			
Domestic common and preferred stock	$	3,073,854	7.1%
Collective trust funds		3,929,724	9.1%
International common and preferred stock		6,879,794	16.0%
Subtotal per Statement of Plan Net Assets		13,883,372	32.2%
Net Asset Allocation Adjustment*		100,719	0.2%
Total Common and preferred stock - Asset Allocation Basis		**13,984,091**	**32.4%**
Fixed income:			
Domestic mortgage-backed securities		3,740,617	8.9%
U.S. government and agency obligations		1,416,505	3.3%
Domestic corporate and taxable municipal bonds		2,271,173	5.3%
Miscellaneous domestic fixed income		456,144	1.1%
Collective trust funds		2,529,667	5.9%
International fixed income		919,443	2.1%
Subtotal per Statement of Plan Net Assets		11,333,549	26.6%
Net Asset Allocation Adjustment*		870,053	2.0%
Total Fixed income - Asset Allocation Basis		**12,203,602**	**28.6%**
Real estate:			
Equity real estate		3,493,360	8.1%
Directly-owned real estate		205,993	0.5%
Subtotal per Statement of Plan Net Assets		3,699,353	8.6%
Net Asset Allocation Adjustment*		545,657	1.3%
Total Real estate - Asset Allocation Basis		**4,245,010**	**9.9%**
Alternative investments:			
Private equity		5,047,201	11.7%
Private debt		3,283,060	7.6%
Venture capital		698,671	1.6%
Subtotal per Statement of Plan Net Assets		9,028,932	20.9%
Net Asset Allocation Adjustment*		-1,520,666	-3.5%
Total Alternative investments - Asset Allocation Basis		**7,508,266**	**17.4%**
Absolute return:			
Net Asset Allocation Adjustment*		3,237,921	7.5%
Total Absolute return - Asset Allocation Basis		**3,237,921**	**7.5%**
Commodities:			
Net Asset Allocation Adjustment*		1,820,575	4.2%
Total Commodities - Asset Allocation Basis		**1,820,575**	**4.2%**
Pension investments - Asset Allocation Basis	$	**42,999,465**	**100.0%**
Net pension investment payable		150,159	
Pension investments per Statement of Plan Net Assets	$	**43,149,624**	
Postemployment Healthcare investments	$	**194,311**	**100.0%**

* Includes Short-term investments which are allocated to the asset class of the investment manager which holds them, 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.

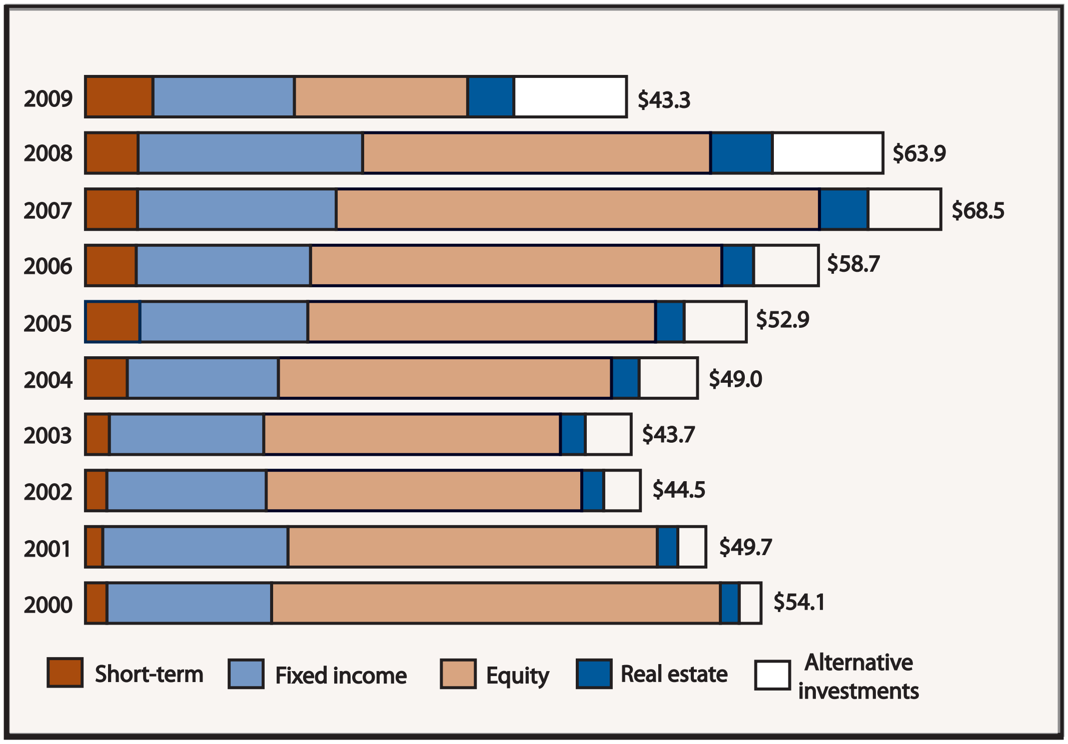
Comparison of Actual Portfolio Distribution to Asset Allocation Plan As of June 30, 2009

Asset Category	Plan	Actual
Common and preferred stock (Equity)	31.0%	32.4%
Fixed income	29.5%	28.6%
Real estate	11.0%	9.9%
Alternative investments	17.0%	17.4%
Absolute return	7.5%	7.5%
Commodities	4.0%	4.2%
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.

Domestic Common and Preferred Stock

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2009

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
Security Capital Preferred Growth	16,299	137,374
Exxon Mobil Corporation	1,342	93,786
Wyeth	1,678	76,159
Chevron Corporation	633	41,961
Microsoft Corporation	1,667	39,619
Johnson & Johnson	592	33,620
Procter & Gamble Company	624	31,866
AT&T Inc.	1,229	30,534
IBM	285	29,714
JP Morgan Chase & Company	834	28,454
Total of 10 Largest Holdings		**543,087**
Total System Holdings - Domestic Common and Preferred Stock		**3,073,854**

Collective Trust Funds - Common and Preferred Stock

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2009

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
Bridgewater Pure Alpha Fund II Ltd.	675	846,817
Barclays Global Ascent Ltd.	500	630,226
AQR Offshore Multi-Strategy Fund Ltd.	8	588,229
First Quadrant Global Macro Fund Ltd.	5,505	511,680
Wellington Trust Company Commodities II Portfolio	29,542	224,224
Barclays Global Investors Capital Structure Investments Fund Ltd.	198	203,025
Boston Company US Micro Cap Hedge Fund	149	181,712
Barclays Global Investors 32 Capital Fund Ltd.	158	141,939
Barclays Global Investors Emerging Markets Alpha Advantage Fund Ltd.	85	126,265
Barclays Global Investors Emerging Markets Strategic Insights Fund	4,014	125,359
Total of 10 Largest Holdings		**3,579,476**
Total System Holdings - Collective Trust Funds- Common and Preferred Stock		**3,929,724**

International Common and Preferred Stock

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2009

(Dollar Amounts and Shares in Thousands)

Description	No. of Shares	Fair Value ($)
Nestle SA	2,228	83,822
BP PLC	9,804	77,145
Royal Dutch Shell Class A	2,503	64,618
HSBC Holdings PLC	6,643	57,641
Toyota Motor Corporation	1,297	49,326
Roche Holding AG	357	48,536
Vodafone Group PLC	25,015	48,281
BHP Billiton Limited	1,628	45,695
Novartis AG	1,111	44,998
Petroleo Brasileiro SA	1,164	38,830
Total of 10 Largest Holdings		**558,892**
Total System Holdings - International Common and Preferred Stock		**6,879,794**

Fixed Income

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2009

(Dollar Amounts and Shares in Thousands)

Description	Maturity Date	Interest Rate (%)	Par Value($) or No. of Shares	Fair Value ($)
Brigade Leveraged Capital Fund	N/A	N/A	754	804,389
Barclays US Extended Core Global Alpha Fund	N/A	N/A	589	636,746
Bridgewater Int'l Inflation-Linked Bond Fund	N/A	N/A	332	354,044
Bridgewater U.S. Inflation-Linked Bond Fund	N/A	N/A	243	239,873
PIMCO Abs. Return Strategy V Offshore Fund	N/A	N/A	156	173,898
U.S. Treasury - Inflation Index	01/15/15	1.625	173,084	172,488
U.S. Treasury - Inflation Index	01/15/25	2.375	165,411	170,011
PIMCO Global Credit Opport.Offshore Fund	N/A	N/A	143	145,556
U.S. Treasury - Inflation Index	01/15/11	3.500	122,498	127,972
U.S. Treasury - Inflation Index	01/15/26	2.000	108,168	105,903
Total of 10 Largest Holdings				**2,930,880**
Total System Holdings - Fixed Income				**11,333,549**

Postemployment Healthcare Investments

10 Largest Holdings in Descending Order by Fair Value

As of June 30, 2009

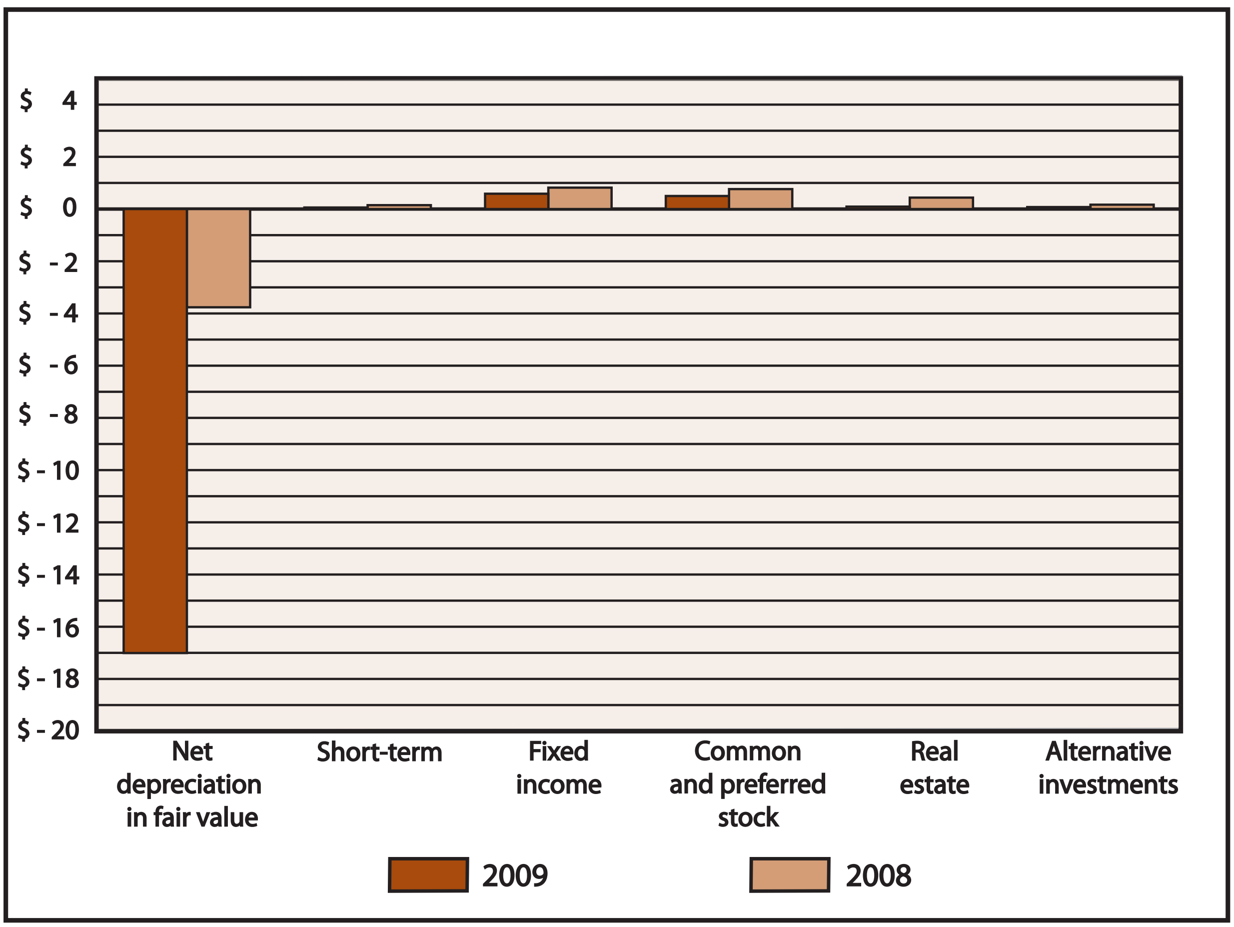
(Dollar Amounts in Thousands)

Description	Maturity Date	Interest Rate (%)	Par Value ($)	Fair Value ($)
PSERS Short-Term Investment Fund	Various	Various	111,746	111,746
M & T Bank Repurchase Agreement	07/01/09	0.009	21,433	21,433
M & T Bank Repurchase Agreement	07/01/09	0.009	13,055	13,055
FHLMC Multiclass 2090 Class PK	10/15/13	5.490	3,785	3,968
FHLMC Multiclass 2759 Class GB	04/15/25	5.000	3,000	3,074
FHLMC Multiclass 1609 Class FA	02/15/22	6.500	2,633	2,664
FHLMC Multiclass 2608 Class FJ	03/15/17	0.688	2,334	2,321
FHLMC Multiclass 2638 Class FA	11/15/16	0.688	2,287	2,266
FHLMC Multiclass 2960 Class BG	06/15/21	5.000	2,158	2,217
FHLMC Multiclass 2611 Class UB	06/15/16	4.000	1,977	2,023
Total of 10 Largest Holdings				**164,767**
Total System Holdings - Postemployment Healthcare Investments				**194,311**

Comparison of Investment Activity Income
For Fiscal Years Ended June 30, 2009 and 2008
(Dollar Amounts in Thousands)

Investing Activities	**2009**	2008
Net depreciation in fair value of investments	**$ (17,008,184)**	$ (3,763,381)
Short-term	**58,958**	149,194
Fixed income	**587,007**	820,338
Common and preferred stock	**500,001**	763,615
Real estate	**92,515**	437,880
Alternative investments	**75,776**	167,052
Total investment activity income (loss)	**$ (15,693,927)**	$ (1,425,302)

(Dollar Amounts in Billions)



Brokers' fees on equity investment transactions for the fiscal year ended June 30, 2009 were $23.6 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, 2009, the System earned $1 million 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, 2009

Broker Name	Fees Paid ($)	Broker Name	Fees Paid ($)
JP Morgan	1,644,416	Exane Securities	296,654
Merrill Lynch	1,506,658	Jefferies & Company Incorporated	278,979
UBS Securities	1,375,643	ITG Securities	268,182
Credit Suisse	1,230,582	Chevreux International	265,170
Instinet Corporation	1,033,706	CLSA Limited	260,275
Goldman Sachs & Company	1,024,964	Weeden & Company	231,887
Deutsche Bank	917,903	HSBC Securities	222,411
Citigroup/Salomon	827,124	ABN AMRO	213,019
Jones & Associates	788,512	Daiwa Securities	183,845
SG Securities	714,231	G-Trade Services	140,696
Credit Lyonnais Securities	594,003	Sanford Bernstein & Company	139,772
Macquaries Equities	592,636	Raymond James & Associates	133,294
Knight Securities	581,215	Samsung Securities	122,881
Morgan Stanley & Company	599,173	B-Trade Services, LLC	112,992
Nomura Securities International	511,803	Lehman Brothers	108,970
Liquidnet Incorporated	493,430	Mitsubishi Bank	102,472
Cazenove Incorporated	385,100	Stifel Nicolaus & Company	101,345
BNY Convergex	357,162	Goldman Redi	100,121
Cantor, Fitzgerald & Company	338,626		

Professional Consultants
External Investment Advisors
As of June 30, 2009

Absolute Return Managers

- Acorn Derivatives Management Corporation
- AQR Capital Management, LLC
- Barclays Global Investors, N.A.
- Boston Company Asset Management, LLC (The)
- Bridgewater Associates, Inc.
- First Quadrant
- FX Concepts, Inc.
- Pacific Investment Management Company

U.S. Style-Oriented Small Cap Equity Managers

- Emerald Advisers, Inc.
- First Pacific Advisors, Inc.

U.S. Micro Cap Equity Managers

- Donald Smith & Company, Inc.
- NorthPointe Capital, LLC
- Oberweis Asset Management, Inc.
- Thomson Horstmann & Bryant, Inc.
- Turner Investment Partners, Inc.

Publicly-Traded Real Estate Securities Managers

- Cohen & Steers Capital Management, Inc.
- European Investors, Inc.
- LaSalle Investment Management
- Morgan Stanley Investment Management, Inc.
- Security Capital Research & Management, Inc.

Non-U.S. Large Cap Equity Managers

- Baillie Gifford Overseas, Ltd.
- Barclays Global Investors, NA
- Marathon Asset Management Ltd.
- Martin Currie, Inc.
- Mercator Asset Management, LP

Non-U.S. Small Cap Equity Managers

- Acadian Asset Management
- AXA Rosenberg Investment Management, LLC
- Batterymarch Financial Management, Inc.

Professional Consultants (Continued)

Non-U.S. Small Cap Equity Managers (Continued)

- GlobeFlex Capital, LP
- Munder Capital Management
- Oberweis Asset Management, Inc.
- Pyramis Global Advisors
- Victory Capital Management
- Wasatch Advisors, Inc.

Non-U.S. Emerging Markets Equity Managers

- Batterymarch Financial Management, Inc.
- Boston Company Asset Management, LLC (The)
- Templeton Investment Counsel, Inc.
- Wasatch Advisors, Inc.
- Wellington Management Company, LLP
- William Blair & Company, LLC

Enhanced Commodity Index Managers

- Credit Suisse Asset Management, LLC
- Neuberger Berman Alternative Fund Management, LLC

Full Discretion Commodity Managers

- Deutsche Asset Management
- Schroders Investment Management North America
- Wellington Management Company, LLP

U.S. Core Plus Fixed Income Managers

- Aberdeen Asset Management, Inc.
- Barclays Global Investors, NA
- 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

Professional Consultants (Continued)

Emerging Markets Debt Manager

- Franklin Templeton Investments

Global Treasury Inflation - Protected Securities Manager

- Bridgewater Associates, Inc

Active Currency Hedging Overlay Program Manager

- Pareto Investment Management, Ltd.

LIBOR-Plus Short-Term Investment Manager

- BlackRock Financial Management, Inc.

Credit Opportunities Managers

- BlackRock Mortgage (Offshore) Investors, LP
- Brigade Leveraged Capital Structures Offshore, Ltd.
- Hyperion Brookfield Asset Management, Inc.
- LBC Credit Partners II, LP
- Oaktree Loan Fund 2x, LP
- Sankaty Credit Opportunities IV, LP
- Sankaty Managed Account (PSERS), LP
- TCW Asset Management Company
- TCW Credit Opportunities Fund, LP

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

Real Estate Partnerships

- Apollo European Real Estate Fund III, LP
- Apollo Real Estate Finance Corporation
- AREFIN Co-Invest Corporation
- AvalonBay Value Added Fund I & II, LP
- Avenue Real Estate Fund Parallel, LP
- Beacon Capital Strategic Partners V, LP
- Berwind Investment Partnership IV, V & VI, LP
- Blackstone Real Estate Partners V & VI.TE.1, LP
- BPG Co-Investment Partnership, LP
- Broadway Partners Real Estate Fund III, LP
- Cabot Industrial Value Fund III, LP

Professional Consultants (Continued)

Real Estate Partnerships (Continued)

- Carlyle Europe Real Estate Partners III-A, LP
- Carlyle Realty Partners III, IV & V, LP
- Centerline Diversified Risk CMBS Fund I & II, LLC
- Centerline High Yield CMBS Fund III, LLC
- Centerline Real Estate Special Situations Mortgage Fund, LLC
- 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
- Legg Mason Real Estate Capital I & II, Inc.
- Lehman Brothers Real Estate I, II & III, LP
- LEM Real Estate Mezzanine Fund II, LP
- LF Strategic Realty Investors I & II, LLC
- Lubert-Adler Real Estate Fund II, 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.
- Stockbridge Real Estate Fund I, II & III, LP
- Strategic Partners Value Enhancement Fund, LP
- UBS (US) Trumbull Property Fund, LP
- Westbrook Real Estate Fund I, 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, LP
- BG Media Investors, LP
- Blue Point Capital Partners (B) I & II, LP
- Bridgepoint Capital II Partnership, LP
- Bridgepoint Europe IA, IIA, IIIA and 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, 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
- Deutsche European Partners IV, 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
- Edison Venture Fund III, LP
- Evergreen Pacific Partners I & II, LP
- First Reserve Fund XI & XII, LP
- Franklin Capital Associates III, LP
- Furman Selz Investors II & 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
- Heritage Fund I, LP
- HSBC Private Equity Fund 6, LP
- Irving Place Capital Partners II & III, LP
- Jefferies Capital Partners IV, LP
- Jefferson Partners Fund IV (PA), LP

Professional Consultants (Continued)

Private Equity/Ventue Capital Partnerships (continued)

- KBL Healthcare Ventures, LP
- KKR 2006 Fund, LP
- KRG Capital Fund I, II, III & IV, LP
- Landmark Equity Partners II, III, IV, V, XIII & XIV, LP
- Landmark Mezzanine Partners, LP
- Lehman Brothers Communications Investors, LP
- Lehman Brothers Merchant Banking Partners II, LP
- Lexington Capital Partners I, 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

Professional Consultants (Continued)

Private Debt Partnerships (continued)

- Avenue Special Situations Fund II, III, IV& V, 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 III & 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
- Biondo Group, LLC (The)
- Conestoga Capital Advisors
- Denali Advisors, LLC
- Great Companies, Inc.
- Hanseatic Management Services, Inc.
- Harvest Fund Advisors, LLC
- John Hsu Capital Group, Inc.
- Opus Capital Management
- Piedmont Investment Advisors
- Pugh Capital Management, Inc.
- Shah Capital Management, Inc.
- Stillwater Capital Partners, Inc.
- Zacks Investment Management, Inc.

Alternative Investment Consultant

- Portfolio Advisors, LLC

Custodian 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.

Professional Consultants (Continued)

Proxy Voting Agent

- Glass, Lewis & Co., LLC

Real Estate Investment Consultant

- Courtland Partners, Ltd.