

## TRS REPORT

Two years ago following an investment study and a 19.6% return for our fund for Fiscal Year 2007, the TRS Board made the decision that while we did not know when the market would turn negative that it was inevitable that it would. TRS started to reduce our exposures to equities, especially U.S. stocks, and invested in new assets that do well in a down market and made other investments, such as commodities, that typically perform well during periods of inflation.

When the prevailing sentiment in the market turned last year, TRS had already made changes to its portfolio designed to minimize overall risk. At first, the System did see favorable returns from its managers that had positions in energy and other commodities. However, concerns about mortgage foreclosures, oil prices and a recession fueled a downturn in the equities markets. These factors produced a negative 5 percent return for the total TRS Trust Fund for FY08. It was the first negative return at TRS in six years and only the fourth in the last 30 years.

While that reduced the average of our three year return to 8.2%, it was still above the median return of all public funds of 8%; our five year number was 10.3% compared to the benchmark of 10%; and the ten year number, (which covers the downturn in the market during the dotcom bust) was 6.9%, well ahead of the benchmark of 6.3%. Unfortunately, this was just the beginning of unprecedented global market volatility.

The collapse of the housing market, the subprime loan mess, and then the financial institutions' meltdown has resulted in what is now being called the worst economic crisis since the Great Depression. For investors it meant that there was literally nowhere to hide. Not only U.S. stocks went down, but international equities as well. Bonds of most all types proved not to be a refuge and even commodities were pulled down by the worldwide decline in demand.

TRS lost 11% of its portfolio during October 2008 alone, one of the most volatile periods in the history of the financial markets. And the markets have only continued to decline. With the exception of some treasury notes and gold, diversity in investments has been of little value. From July 1, starting with \$38.4 billion the value of our fund fell to \$29.1 billion, a decline of 24%, by December 31, 2008.

TRS report pg 2

New projections from the Illinois State Comptroller show the Illinois state budget deficit is expected to balloon from \$4 billion to as much as \$10 billion for the fiscal year that begins July 1. The deficit has grown for multiple reasons, including a significant increase required in the state's contribution to all five pension funds. The state's contribution to TRS will increase by \$637,479,000 to a total of \$2,089,268,000 for FY 2010. A portion of the increase is attributed to investment losses during FY08. Additionally, FY2010 marks the last year of the so-called "ramp period" during which state contributions are sharply increased under a statutory funding plan designed to bring the state pension systems to a 90 percent funded level by 2045.

There is no way that Illinois can come up with the money needed to balance the budget by cutting unnecessary spending, selling an additional casino license, or hoping to gain money from privatizing a capital asset. Additional fees or increasing the motor fuel tax are not enough, they are going to have increase the income tax, or broaden the sales tax, or do a combination of both, but that will require a political courage that politicians are not noted for having.

While that is the sad reality of our fund and the state treasury, equally certain are that all of our pensions will continue to be paid. We have seen the fund reduced by billions, but billions remain, and the obligation of the state of Illinois to see that we receive our pensions remains and is guaranteed by both the state and federal Constitutions. A lack of funds may mean that Illinois will scale back their contribution for the pension systems, but the obligation will remain and the state will owe us that much more.

In time, the markets will turn and TRS will be well positioned to recover its losses. TRS has a longer term investment horizon and will continue to provide benefits not only us, but also our survivors and those teachers that are yet to retire. Though a recovery will take time, TRS continues to be vigilant to protect your retirement security.

Bob Lyons  
Elected Annuitant TRS board