

Integrity

Comprehensive Annual Financial Report

Fiscal Year Ended June 30, 2001



STATE TEACHERS RETIREMENT SYSTEM
OF OHIO

Among the several pieces of artwork at the STRS Ohio offices in downtown Columbus is a bronze and stainless steel sculpture titled “Integrity.” The naming of the piece was intentional and deliberate. Located outside the entrance to the State Teachers Retirement Board meeting room, this sculpture symbolizes the touchstone that guides all that is done at STRS Ohio, from board actions to counseling members and investing funds.

The decision to use the theme “integrity” for this year’s annual report was made last summer. Because it is a quality that our members and benefit recipients often name in describing STRS Ohio, we believed it was an appropriate theme. Then the events of Sept. 11 occurred and the concept of integrity took on even greater significance.

Like the rest of the world, each of us has been affected in some way by the turbulent times in which we now find ourselves. But, as we go about our work at STRS Ohio, we remain focused on our mission of being the leader in providing financial security for Ohio’s educators.



in•teg•ri•ty \in-¹te-grə-tē\ *n* **1**: firm adherence to a code of esp. moral or artistic values : INCORRUPTIBILITY **2**: an unimpaired condition : SOUNDNESS **3**: the quality or state of being complete or undivided : COMPLETENESS *syn* see HONESTY

Certificate of Achievement for Excellence in Financial Reporting

Presented to

The State Teachers Retirement System of Ohio

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2000

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



Timothy A. Crave
President

Jeffrey L. Essler
Executive Director

Table of Contents

State Teachers Retirement System of Ohio 2001 Comprehensive Annual Financial Report

A review of the 2000–2001 fiscal year

Introduction	
Certificate of Achievement	2
State Teachers Retirement Board	4
STRS Ohio Senior Staff Members	6
Letter of Transmittal	7
Year in Review	10
Financial	
Independent Auditors' Report	15
Financial Statements	
Combining Statements of Plan Net Assets	16
Combining Statements of Changes in Plan Net Assets	17
Notes to Financial Statements	19
Required Supplemental Information	
Required Schedule of Employer Contributions, 1996–2001	27
Required Schedule of Funding Progress, 1996–2001	27
Notes to the Trend Data	27
Additional Information	
Schedule of Administrative Expenses	28
Schedule of Investment Expenses	29
Investments	
Investment Review	31
Investment Objective and Policy	35
Investment Performance	48
STRS Ohio Long-Term Policy Objective (5 Years)	48
Summary of Investment Assets as of June 30, 2001 and 2000	49
Investment Distribution by Fair Value as of June 30, 2001	50
Ohio Investment Profile as of June 30, 2001	50
Schedule of Largest Investment Holdings as of June 30, 2001	50
Actuarial	
Actuary's Certification Letter	53
Statement of Actuarial Assumptions and Methods	55
Benefit Recipients Added to and Removed From the Rolls, 1996–2001	56
Schedule of Valuation Data — Active Members, 1992–2001	56
Schedule of Valuation Data — Retirees/Beneficiaries, 1992–2001	56
Solvency Test, 1992–2001	57
Analysis of Financial Experience	57
Summary of Benefit and Contribution Provisions	58
Statistical	
Expenses by Type, 1992–2001	61
Revenues by Source, 1992–2001	61
Number of Benefit Recipients by Type, 1992–2001	62
Average Monthly Allowances by Type, 1992–2001	62
Benefit Expenses by Type, 1992–2001	62
Selected Funding Information, 1992–2001	63
Number of Reporting Employers by Type, 1992–2001	63

2000–2001 State Teachers Retirement Board

While more than 700 full- and part-time STRS Ohio associates handle the day-to-day operations of the retirement system, it is the Retirement Board that provides the direction, fiduciary oversight and policies that have enabled STRS Ohio to fulfill its mission of assuring financial security for Ohio's educators. Membership on the board includes six elected members — five active teachers and one retired teacher — who devote thousands of volunteer hours every year in service to STRS Ohio. These six educators are joined at the board table by three ex officio voting members: the auditor of state, the attorney general and the superintendent of public instruction.



Michael N. Billirakis

Teacher member since 2000.
Perry Local Schools,
Lake County

Deborah Scott

Teacher member since 1994.
Finneytown Local Schools,
Hamilton County

Richard Moore

Representing Betty D. Montgomery,
Attorney General.
Ex officio member of the board
since elected to office in 1995.

Jack H. Chapman

Chair
Teacher member since 1990.
Reynoldsburg City Schools,
Franklin County

Robert P. Shreve

Retired teacher member
since 1997.
Delaware County



During the 2000–2001 fiscal year, Michael N. Billirakis was chosen to complete the unexpired term of William A. Dorsey, who resigned from the board in August 2000 upon retirement. Deborah Scott was reelected to a four-year term as an active teacher member and Joseph I. Endry was elected as the retired teacher member on the board, replacing Robert P. Shreve, who chose not to seek reelection. Both began their terms on Sept. 1, 2001.

Hazel A. Sidaway
Vice Chair
Teacher member since 1986.
Canton City Schools,
Stark County

Gloria L. Gaylord
Representing James M. Petro,
Auditor of State.
Ex officio member of the board
since elected to office in 1995.

Herbert L. Dyer
Executive Director,
State Teachers
Retirement System
of Ohio

Alice Gibson
Representing Susan Tave Zelman,
Superintendent of Public Instruction.
Ex officio member of the board since
appointed to office in 1999.

Eugene E. Norris
Teacher member since 1996.
South-Western City Schools,
Franklin County

STRS Ohio Senior Staff Members



Shown here are the members of senior staff for 2000–2001. Pictured from left to right are: Damon F. Asbury, deputy executive director — Administration; Sandra L. Knoesel, deputy executive director — Member Benefits; Herbert L. Dyer, executive director; Cynthia E. Hvizdos, general counsel; Terri Meese Harrison, director of Governmental Relations; Laura R. Ecklar, director of Communication Services; Robert A. Slater, deputy executive director — Finance and chief financial officer; Adrian R. Mullins, director of Information Technology Services; Joan M. Williams, director of Human Resource Services; Stephen A. Mitchell, deputy executive director — Investments; and Eileen F. Boles, executive assistant.



Nov. 28, 2001

Members of the State Teachers Retirement Board:

We are pleased to present the *Comprehensive Annual Financial Report* of the State Teachers Retirement System of Ohio for the fiscal year ended June 30, 2001. This report is intended to provide readers with financial, investment, actuarial and statistical information in a single publication. STRS Ohio management is responsible for the accuracy of the data and for the completeness and fairness of the presentation.

STRS Ohio was created by legislative act on May 8, 1919, as an alternative to separate, often unstable local school district retirement plans. STRS Ohio is a cost-sharing, multiple-employer plan providing service retirement, disability, survivor and health care benefits to teachers and faculty members of public boards of education, state-supported colleges and universities, and the state of Ohio and its political subdivisions.

The *Comprehensive Annual Financial Report* is divided into five sections: (1) the Introductory Section includes this letter of transmittal and information about the administrative organization of STRS Ohio; (2) the Financial Section contains the general purpose financial statements and footnotes along with the report of the independent auditors; (3) the Investment Section includes a summary of investment assets and the Retirement Board's Objective and Policy Statement; (4) the Actuarial Section includes results of the annual actuarial valuation and the certification letter of Buck Consultants; and (5) the Statistical Section includes historical data showing the progress of the system.

Major Initiatives

Legislation that went into effect in July 2000 resulted in major changes for STRS Ohio members and benefit recipients. Substitute Senate Bill 190 did the following:

- Increased the benefit formula for active teachers to 2.2% of final average salary for the first 30 years of earned Ohio service. It also increased the benefit formula for members with 35 or more years of service.
- Recalculated the base benefit for many age and service retirees.
- Provided a one-time increase for all benefit recipients who needed a raise in their monthly benefit to restore a level equal to at least 85% of their benefits' original purchasing power.
- Enabled STRS Ohio to establish a defined contribution option for new members and current members with less than five years of service credit.

STRS Ohio worked throughout the year to develop two new retirement options: the Defined Contribution Plan (DC Plan) and the Combined Plan. These new plans became available to eligible members as of July 1, 2001. They provide attractive options for members who want more choice and increased portability for their funds.

Choice is also one of the goals of the STRS Ohio Health Care Program. Today, STRS Ohio benefit recipients have access to indemnity, PPO (preferred provider organization) and HMO (health maintenance organization) plans — depending on their age and location of their permanent residence.

However, faced with annual double-digit percentage increases in health care costs and an ever-changing health care marketplace, the Retirement Board established "trigger points" in fall 2000 to consider terminating health plans. Using these criteria, the board eliminated seven HMO plans, affecting 5,300 enrollees, beginning Jan. 1, 2002.

RETIREMENT BOARD

HAZEL A. SIDAWAY, *Chair*
Canton City Schools
Stark County

DEBORAH SCOTT, *Vice Chair*
Finneytown Local Schools
Hamilton County

MICHAEL N. BILLIRAKIS
Perry Local Schools
Lake County

JACK H. CHAPMAN
Reynoldsburg City Schools
Franklin County

JOSEPH I. ENDRY
Retired Teacher Member

BETTY D. MONTGOMERY
Attorney General of Ohio

EUGENE E. NORRIS
South-Western City Schools
Franklin County

JAMES M. PETRO
Auditor of State

SUSAN TAVE ZELMAN
Superintendent of
Public Instruction



HERBERT L. DYER
Executive Director

CYNTHIA E. HVIZDOS
General Counsel

TERRI MEESE HARRISON
Governmental Relations

EILEEN F. BOLES
Executive Assistant



DEPUTY EXECUTIVE DIRECTORS

DAMON F. ASBURY
Administration

SANDRA L. KNOESEL
Member Benefits

STEPHEN A. MITCHELL
Investments

ROBERT A. SLATER
Chief Financial Officer

The board also approved a change in the prescription drug program administrator for more than 100,000 benefit recipients and their dependents — again driven by the priority of providing exceptional service in an efficient and cost-effective manner. During the next three years, STRS Ohio anticipates saving more than \$27 million using AdvancePCS over the previous provider.

The full complement of services available to STRS Ohio members while they are teaching and in retirement continued to attract an increasing number of callers, workshop and counseling session attendees, and Web site users. This past year, records were set in several areas.

For additional information on these and other 2000–2001 highlights, refer to the Year in Review on Pages 10 through 13.

Investments

Total investments decreased to \$52.8 billion (excluding invested securities lending collateral) as of June 30, 2001, representing an 8.2% decrease from 2000. The Investment Review starting on Page 31 discusses the declines experienced in the investment markets. The allocation of investment assets is designed to provide high long-term yields while minimizing risk. A summary of the asset allocation can be found on Page 50.

For calendar year 2000, investments provided a –2.43% return. STRS Ohio’s annualized rate of return over the last three years was 9.44% and 10.97% for the last five years. Similar benchmark returns over the same one-, three- and five-year periods were –2.60%, 9.77%, and 11.78%, respectively.

Additions to Plan Net Assets

Member and employer contributions, as well as income from investments, provide the reserves needed to finance retirement benefits. Total contributions and the net investment loss totaled \$1.66 billion for the year. The net investment loss includes the fair value declines of our investment portfolio from last year to this year. Member and employer contributions increased from last year by 4.0 and 5.2%, respectively. Covered payroll grew by 5.2%, which includes salaries paid to participants in alternative retirement plans (ARPs). ARP participants are not members of STRS Ohio; however, their employers were required to contribute 5.76% of salaries to STRS Ohio to help pay for unfunded liabilities.

Deductions From Plan Net Assets

The principal purpose for STRS Ohio is to provide retirement, survivor and disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments as designated by the plan, refunds of contributions to terminated members, and the administrative costs of operating STRS Ohio. Benefit, withdrawal and administrative costs totaled \$3.0 billion in fiscal year 2001, an 8.0% increase over fiscal year 2000.

Funding

Contribution rates are actuarially determined to provide a level basis of funding using the entry age normal cost method, and an actuarial valuation is performed annually by Buck Consultants, Chicago, Ill. The July 1, 2001, valuation shows that

Additions to Plan Net Assets (in thousands)	
	2001
Net Investment Income	\$(3,694,121)
Contributions:	
Member	\$ 785,009
Employer	\$ 1,142,440
Other	\$ 103,582
Total Contributions	\$ 2,031,031
Total Additions to Plan Net Assets	\$(1,663,090)

Deductions From Plan Net Assets (in thousands)	
	2001
Benefits	\$ 2,855,859
Withdrawals	\$ 93,868
Administrative Expenses	\$ 72,277
Total Deductions from Net Assets	\$ 3,022,004

the amortization period for the unfunded accrued liability increased to 27.5 years from 23.1 years, and the ratio of assets to total accrued liabilities decreased slightly to 91.2% from 92%. A detailed discussion of funding is provided in the Actuarial Section of this report beginning on Page 53.

Certificate of Achievement and Other Awards

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to STRS Ohio for its *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2000. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

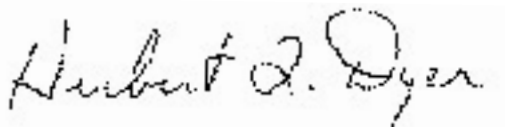
To be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report that conforms to program standards. This report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for one year. STRS Ohio has received a Certificate of Achievement for the last 11 years. We believe our current report continues to conform to the Certificate of Achievement program requirements and are submitting it to the GFOA.

In addition, STRS Ohio again successfully met the rigorous requirements for the Public Pension Coordinating Council Achievement Award by documenting compliance with all 18 specific principles in the areas of benefits, actuarial valuations, financial reporting, investing and disclosure to members. Only 27 public retirement systems in the United States qualified for the 2000 award.

Acknowledgments

The preparation of this report is possible only through the combined efforts of the STRS Ohio staff. It is intended to provide complete and reliable information as a basis for making management decisions, complying with legal provisions and determining responsible stewardship of the assets contributed by members and their employers.

Respectfully submitted,



Herbert L. Dyer
Executive Director



Robert A. Slater, CPA
Deputy Executive Director
Chief Financial Officer

Year in Review

July 1, 2000, through June 30, 2001

STRS Ohio Expands Its Retirement Plan Options

Developing and launching additional retirement plan options for eligible STRS Ohio members was a significant undertaking for the Retirement Board and system associates during the 2000–2001 fiscal year.

The passage of Substitute Senate Bill 190 in April 2000 by the Ohio Legislature resulted in one of the most far-reaching benefit improvement packages for Ohio's public educators in STRS Ohio's history. An important component of the bill enabled STRS Ohio to establish a defined contribution plan option for new members and current members with less than five years of service credit as of June 30, 2001.

On July 1, 2001, two new plans were launched to eligible members: the STRS Ohio Defined Contribution Plan and the STRS Ohio Combined Plan.

Several factors led to development of the new plan options. Many beginning teachers were looking for more choice among retirement options and increased ability to move their contributions if they left teaching or moved out of the state. Some educators also wanted to have a more active role in managing their retirement funds.

With the addition of these defined contribution options, STRS Ohio now stands as one of only a few teacher pension plans in the country to offer significantly different retirement plan options to its members.

Reemployment Rules Relaxed Under New Ohio Laws

During the 2000–2001 fiscal year, almost 1,700 STRS Ohio members returned to public employment after retirement. Many of them took advantage of new state legislation — Amended Substitute Senate Bill

144 and Substitute House Bill 535 — that relaxed a number of previous restrictions on reemployment for public retirees, including STRS Ohio members. Reemployment rules now state the following:

- Retirees may return to any Ohio public employment after two months of retirement.
- Members who are contributing to PERS, SERS or STRS Ohio through more than one job may retire with the highest-paying employer and continue to work with one or all of the lower-paying employers.
- Retirees are no longer restricted from working under private contract or through an independent contractor for the same employer with whom they were employed at the time of retirement. However, they must still wait two months after their effective retirement date before returning to public employment.



As assistant portfolio manager at STRS Ohio, Don analyzes mid-cap value stocks — an investment class with potential for excellent long-term returns.

COLAs Help Protect Benefits From Inflation

A cost-of-living increase, up to 3%, is automatically granted each year to benefit recipients. Ohio law allows STRS Ohio to pay a COLA (cost-of-living adjustment) up to 3% based on the increase in the Consumer Price Index (CPI) over the previous calendar year. The COLA is calculated on the retiree's original benefit and is paid on the anniversary date of retirement. Based on a 2.2% increase in the CPI for 1999, STRS Ohio paid \$29.6 million in added benefits for the 2000–2001 fiscal year.

In 2000, the CPI increased by 3.5% — marking the first year of inflation greater than 3% since 1991. Consequently, in March 2001, the Retirement Board approved a 3% COLA increase for all Defined Benefit Plan benefit recipients for 2001–2002.

Looking to the future, new legislation that goes into effect on Feb. 1, 2002, establishes an annual 3% COLA for benefit recipients of all five Ohio public retirement systems, including STRS Ohio — regardless of changes in the CPI. Benefit recipients will no longer need to rely on their COLA reserve bank to receive a 3% increase.

Retirement Board Actions Result in Cost Savings

Providing quality health care benefits at an affordable cost to STRS Ohio benefit recipients and their dependents remains a challenging and increasingly important priority for the Retirement Board. In March 2000, the board approved several changes to the prescription drug program administered by Merck-Medco Managed Care. These

plan design and cost-sharing adjustments resulted in \$10.5 million in savings for the STRS Ohio Health Care Program in 2001.

During the 2000–2001 fiscal year, the board implemented additional significant initiatives to help ensure health care benefits remain available well into the future.

Choice has always been one of the goals of the STRS Ohio Health Care Program. Since the program's founding in 1974, the number of plans available has steadily increased, reflecting changes in the health care industry itself, such as the advent of managed care, as well as members' requests for more options.

However, faced with annual double-digit increases in health care costs and an ever-changing health care marketplace, the Retirement Board established "trigger points" in fall 2000 to consider in terminating health plans. These trigger points first focus on market share and administrative costs. If administrative costs are high and market share is low, the health plan is considered for termination. Additional factors that are evaluated are the plan's financial status; enrollee satisfaction ratings; the plan's ability to control cost trends; merger and acquisition activity; commitment to account management; and the plan's relationship to the provider community.

Using these criteria the board evaluated its current plan offerings. Facing a proposed 44% overall increase in HMO (health maintenance organization) premiums for next year, plus current low enrollment figures, the board chose to eliminate seven HMO plans, affecting 5,300 enrollees, beginning on Jan. 1, 2002.

During this past fiscal year, the Retirement Board also approved a change in the pre-

scription drug program administrator for more than 100,000 benefit recipients and their dependents, again driven by the priority of providing exceptional service in an efficient and cost-effective manner. During the next three years, STRS Ohio anticipates saving more than \$27 million using AdvancePCS as its pharmacy benefits manager for enrollees in the indemnity and PPO (preferred provider organization) plans administered by Aetna U.S. Healthcare and Medical Mutual of Ohio, and Paramount Health Care HMOs. As part of this change to a new program, which went into effect on Jan. 1, 2002, the three-fill limit at retail pharmacies was eliminated for these enrollees.

Finally, three changes to the Aetna U.S. Healthcare and Medical Mutual of Ohio PPO and indemnity plans were approved by the Retirement Board, effective Jan. 1, 2002:

1. ***To promote greater use of network providers***, the coinsurance level for non-network providers under the PPOs was reduced to 60% and the out-of-pocket maximum for non-network services was increased to \$3,000/single and \$6,000/family.
2. ***To support plan enrollees' efforts to be proactive in managing their health***, the current \$150 annual wellness benefit was increased to \$250.
3. ***To encourage enrollees to seek hospice services in an outpatient setting***, the coverage level was increased to 100% as opposed to the former 80% coverage for outpatient services.

Year in Review

Time Frame Lengthens for Purchasing Service Credit

The ability to purchase service credit for certain types of past employment and leaves of absence is a valued feature of STRS Ohio's defined benefit structure. This past year, the time frame for paying for purchased credit was expanded. Members can now complete purchases of credit up to three months *after* retirement. Previously, all purchases of service credit had to be completed by the member's retirement date. For members, this change means they may withdraw funds from an individual investment account after retiring, such as a 403(b) plan, to purchase credit with STRS Ohio and enhance their monthly service retirement benefit.

2000 Marks the 21st Year for a 13th Check

Nearly 94,000 benefit recipients received a supplemental benefit payment in December 2000. A total of \$50.4 million of investment earnings was used to fund this benefit for individuals who had received a benefit payment for the 12 consecutive months preceding Jan. 1, 2001. The "unit value" of the payment was \$14 for each year of service and each year monthly benefits had been received.

The Ohio Legislature has given the Retirement Board the authority to grant a "13th check" if investment earnings in the previous fiscal year exceed funding requirements.

Retirement Board Actions Improve Service

Last spring, the Retirement Board approved two actions resulting in more efficient, improved services for members and benefit recipients.

The first change involved adjusting the hours of the Member Services Center. A detailed analysis of the center's operation showed that peak calling times are from 9:30–11 a.m. A large number of calls also are made to the center during the first few days of each month and on Mondays. In contrast, less than 2% of the calls were taken on Saturday and only 1% are taken during the Monday through Thursday 6–7 p.m. time period.

Taking this information into consideration, the board approved adjusting the center's hours to provide better service during the peak periods. Saturday hours were eliminated and the Monday through Thursday hours were shortened by one hour to 7:30 a.m.–6 p.m. Friday hours remain 7:30 a.m.–5 p.m.

A second change approved by the Retirement Board involved the use of "direct deposit" by STRS Ohio benefit recipients. Nearly 85% of benefit recipients have their monthly benefit check sent directly to their bank by electronic funds transfer (EFT), also known as direct deposit. This service has been highly valued by recipients because it is free, secure, reliable and convenient.

However, each year several thousand benefit recipients need assistance from STRS Ohio to replace paper checks that were lost, returned to the post office due to bad addresses or damaged envelopes, or not cashed by the "void after" date.

To reduce the number of benefit recipients who could experience similar problems, all new benefit recipients now receive their monthly benefits through direct deposit. The only exceptions are recipients with foreign addresses and college students.

Both of these changes went into effect on July 1, 2001.

Callers Top 300,000 Mark

In a world that is becoming increasingly dominated by voice mail and lengthy pre-recorded messages, STRS Ohio's Member Services Center stands in stark contrast. Callers to the center receive personal assistance from 39 highly trained and knowledgeable member service representatives — *usually within 50 seconds of dialing their phone*. This year, more than 316,000 calls were answered, exceeding last year's record by almost 21,000 calls.

Program Attendance at an All-Time High

For the majority of Ohio's public educators, STRS Ohio is the main source of income during their retirement. That's why it is extremely important that STRS Ohio members take an active role in planning for a financially secure future at all stages of their life — including *in retirement*!

The newest addition to STRS Ohio's educational offerings is the STRS Ohio Retiree Seminar. This three-hour program provides valuable estate planning information, as well as information about providing advance directives for health care and selecting a long-term care facility. Using this informa-

tion, STRS Ohio benefit recipients can alleviate many unnecessary concerns for their loved ones and heirs.

Through expanded program offerings and in-service presentations, almost 5,500 members were served last year — a 54% increase over the previous year.

STRS Ohio Death Benefit Made Tax-Free

All STRS Ohio Defined Benefit Plan service retirement and disability benefit recipients are covered by an automatic \$1,000 death benefit funded by the retirement system. Previously, the beneficiary of this benefit was liable for federal income taxes. However, with the passage of House Bill 628 by the Ohio General Assembly in 2000, payment of this death benefit now qualifies for the same nontaxable status as life insurance. Therefore, no federal taxes are withheld when payment is made.

Discovery Park Benefits Endowment Fund

More than \$542,000 has been contributed to Discovery Park — the first park developed specifically to honor Ohio's educators. The park sits adjacent to the STRS Ohio Building in downtown Columbus and was created as part of the system's 80th anniversary celebration in 2000.

When the retirement system celebrated its 75th anniversary in 1995, gifts from members and retirees helped to establish a \$100,000 endowed scholarship fund to support students pursuing teacher licensure at Ohio's 13 state universities. Due to the

tremendous response to the Discovery Park project, Retirement Board members decided in December 2000 that an additional \$100,000 from STRS Ohio 80th, Inc. could be allocated to that endowment fund.

Research Ensures High Service Levels Continue

At STRS Ohio, research is done on a year-round basis. For the Member Services Center, surveys and call monitoring are conducted. In addition, telephone and written surveys are administered throughout the year, evaluating such items as proposed benefits, communications and service delivery.

Health care plans are also reviewed quarterly, providing valuable data to STRS Ohio associates and the Retirement Board. Benefit recipients also receive an annual "report card" that compares enrollees' satisfaction with their plan.

In short, by asking — and asking often — STRS Ohio ensures that all members and benefit recipients are well served by their retirement system.

System Receives Financial Reporting, Public Relations Awards

In 2000, STRS Ohio again successfully met the rigorous requirements for the Public Pension Coordinating Council Achievement Award by documenting compliance with all 18 specific principles in the areas of benefits, actuarial valuations, financial reporting, investing and disclosure to members. Only 27 public retirement systems in the United States qualified for the 2000 award.

STRS Ohio also received the Certificate of Achievement for Excellence in Financial Reporting from the Government Finance Officers Association for its *Comprehensive Annual Financial Report* for the fiscal year ending June 30, 2000. This marks the 11th consecutive year STRS Ohio has received this award.

Finally, STRS Ohio received six awards — three PRISM Awards (best of category) and three runner-up Awards of Excellence — from the Central Ohio Chapter of the Public Relations Society of America.

Associates Give Generously to the Community

STRS Ohio associates once again demonstrated their care and commitment to the central Ohio community by contributing \$113,673 to the annual United Way campaign. Not only did they exceed the \$100,000 goal they had set for this project, but they also raised funds to provide two "canine companions" for visually limited individuals and made donations to Operation Feed.



An assistant portfolio manager, Terrill helps STRS Ohio toward its goal of meeting or exceeding its benchmark for fixed-income investments.

Independent Auditors' Report



191 West Nationwide Boulevard
Suite 500
Columbus, OH 43215-2568

Telephone 614 249 2300
Fax 614 249 2348

To the Retirement Board
The State Teachers Retirement System of Ohio:

We have audited the accompanying combining statements of plan net assets of the State Teachers Retirement System of Ohio (the System) as of June 30, 2001 and 2000, and the related combining statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements present fairly, in all material respects, the financial position of the System as of June 30, 2001 and 2000, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 26, 2001, on our consideration of the System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

The schedules of funding progress and employer contributions on page 27 are not a required part of the financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures prescribed by professional standards, which consisted principally of inquiries of management regarding the methods of measurement and presentation of schedules. However, we did not audit and do not express an opinion on such information.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The additional information included on pages 28 and 29 is presented for the purpose of additional analysis and is not a required part of the basic financial statements. This additional information is the responsibility of the System's management. Such additional information has been subjected to the auditing procedures applied in our audits of the basic financial statements for the years ended June 30, 2001 and 2000, and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

October 26, 2001

KPMG LLP



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is a member of KPMG International, a Swiss association.

Financial

Combining Statements of Plan Net Assets (in thousands)

	June 30, 2001			June 30, 2000		
	Pensions	Postemployment Health Care	Totals	Pensions	Postemployment Health Care	Totals
Assets:						
Cash and short-term investments	\$ 591,481	\$ 39,208	\$ 630,689	\$ 714,385	\$ 45,415	\$ 759,800
Receivables:						
Accrued interest and dividends	163,769	10,856	174,625	176,530	11,222	187,752
Employer contributions	189,137	12,537	201,674	179,557	11,415	190,972
Retirement incentive	14,507		14,507	29,876		29,876
Member contributions	161,166		161,166	148,830		148,830
Securities sold	77,866	5,162	83,028	243,360	15,471	258,831
Miscellaneous receivables	1,191		1,191	3,481		3,481
Total receivables	<u>607,636</u>	<u>28,555</u>	<u>636,191</u>	<u>781,634</u>	<u>38,108</u>	<u>819,742</u>
Investments, at fair value:						
Fixed income	10,861,681	720,002	11,581,683	11,984,781	761,904	12,746,685
Common and preferred stock	22,671,485	1,502,852	24,174,337	25,111,718	1,596,417	26,708,135
International	8,598,248	569,963	9,168,211	10,069,930	640,171	10,710,101
Real estate	5,941,282	393,837	6,335,119	5,503,754	349,888	5,853,642
Alternative investments	865,857	57,396	923,253	702,843	44,682	747,525
Total investments	<u>48,938,553</u>	<u>3,244,050</u>	<u>52,182,603</u>	<u>53,373,026</u>	<u>3,393,062</u>	<u>56,766,088</u>
Invested securities lending collateral	3,391,009	224,784	3,615,793	3,289,356	209,113	3,498,469
Fixed assets, at cost, net of accumulated depreciation of \$46,713 and \$38,610, respectively	149,524		149,524	118,287		118,287
Total assets	<u>53,678,203</u>	<u>3,536,597</u>	<u>57,214,800</u>	<u>58,276,688</u>	<u>3,685,698</u>	<u>61,962,386</u>
Liabilities:						
Securities purchased	190,923	12,656	203,579	264,538	16,817	281,355
Accrued expenses and other liabilities	14,461	958	15,419	20,535	1,305	21,840
Pension benefits payable				101,896		101,896
Medical benefits payable		42,035	42,035		39,357	39,357
Obligations under securities lending program	3,394,384	225,008	3,619,392	3,289,356	209,113	3,498,469
Total liabilities	<u>3,599,768</u>	<u>280,657</u>	<u>3,880,425</u>	<u>3,676,325</u>	<u>266,592</u>	<u>3,942,917</u>
Net assets held in trust for pension and postemployment health care benefits:						
(A schedule of funding progress is presented on Page 27.)	<u>\$ 50,078,435</u>	<u>\$ 3,255,940</u>	<u>\$ 53,334,375</u>	<u>\$ 54,600,363</u>	<u>\$ 3,419,106</u>	<u>\$ 58,019,469</u>

See accompanying Notes to Financial Statements.

Combining Statements of Changes in Plan Net Assets (in thousands)

	Year Ending June 30, 2001			Year Ending June 30, 2000		
	Pensions	Postemployment Health Care	Totals	Pensions	Postemployment Health Care	Totals
Additions						
Contributions:						
Member	\$ 785,009		\$ 785,009	\$ 755,146		\$ 755,146
Employer	779,274	\$ 363,166	1,142,440	470,473	\$ 615,652	1,086,125
Retirement incentive	25,390		25,390	42,189		42,189
State of Ohio appropriations				1,514		1,514
Benefit recipient health care premiums		68,582	68,582		60,375	60,375
Other retirement systems	9,416		9,416	6,476		6,476
Additional death benefits (net)	194		194	11		11
Total contributions	<u>1,599,283</u>	<u>431,748</u>	<u>2,031,031</u>	<u>1,275,809</u>	<u>676,027</u>	<u>1,951,836</u>
Investment (loss) income from investing activities:						
Net (depreciation) appreciation in fair value of investments	(4,993,942)	(318,843)	(5,312,785)	3,770,584	222,348	3,992,932
Interest	754,350	48,162	802,512	716,174	42,232	758,406
Dividends	395,654	25,261	420,915	384,106	22,650	406,756
Real estate income	379,727	24,244	403,971	333,561	19,670	353,231
	<u>(3,464,211)</u>	<u>(221,176)</u>	<u>(3,685,387)</u>	<u>5,204,425</u>	<u>306,900</u>	<u>5,511,325</u>
Less investment expenses	(21,662)	(1,383)	(23,045)	(18,934)	(1,117)	(20,051)
Net (loss) income from investing activities	<u>(3,485,873)</u>	<u>(222,559)</u>	<u>(3,708,432)</u>	<u>5,185,491</u>	<u>305,783</u>	<u>5,491,274</u>
From securities lending activities						
Securities lending income	208,346	13,302	221,648	185,052	10,912	195,964
Securities lending expenses	(194,894)	(12,443)	(207,337)	(172,905)	(10,196)	(183,101)
Net income from securities lending activities	<u>13,452</u>	<u>859</u>	<u>14,311</u>	<u>12,147</u>	<u>716</u>	<u>12,863</u>
Net investment (loss) income	<u>(3,472,421)</u>	<u>(221,700)</u>	<u>(3,694,121)</u>	<u>5,197,638</u>	<u>306,499</u>	<u>5,504,137</u>
Total (deductions) additions	<u>(1,873,138)</u>	<u>210,048</u>	<u>(1,663,090)</u>	<u>6,473,447</u>	<u>982,526</u>	<u>7,455,973</u>
Deductions						
Benefits:						
Service retirement	2,203,280		2,203,280	2,019,521		2,019,521
Disability retirement	160,775		160,775	152,365		152,365
Survivor benefits	65,591		65,591	62,346		62,346
Supplemental benefit	50,386		50,386	48,493		48,493
Health care		369,354	369,354		343,512	343,512
Other retirement systems	6,473		6,473	8,247		8,247
Total benefit payments	<u>2,486,505</u>	<u>369,354</u>	<u>2,855,859</u>	<u>2,290,972</u>	<u>343,512</u>	<u>2,634,484</u>
Refunds to members who have withdrawn	93,868		93,868	105,759		105,759
Administrative expenses	68,417	3,860	72,277	54,543	3,274	57,817
Total deductions	<u>2,648,790</u>	<u>373,214</u>	<u>3,022,004</u>	<u>2,451,274</u>	<u>346,786</u>	<u>2,798,060</u>
Net (decrease) increase	<u>(4,521,928)</u>	<u>(163,166)</u>	<u>(4,685,094)</u>	<u>4,022,173</u>	<u>635,740</u>	<u>4,657,913</u>
Net assets held in trust for pension and postemployment health care benefits						
Beginning of year	<u>54,600,363</u>	<u>3,419,106</u>	<u>58,019,469</u>	<u>50,578,190</u>	<u>2,783,366</u>	<u>53,361,556</u>
End of year	<u>\$ 50,078,435</u>	<u>\$ 3,255,940</u>	<u>\$ 53,334,375</u>	<u>\$ 54,600,363</u>	<u>\$ 3,419,106</u>	<u>\$ 58,019,469</u>

See accompanying Notes to Financial Statements.

Financial

Babu's detailed analysis of global and domestic markets provides STRS Ohio with solid investments in large-cap equities. Her diligence helps to make the system — and our members' retirement income — financially secure.





Notes to Financial Statements

Years ended June 30, 2001 and 2000

1. Summary of Significant Accounting Policies

The financial statements of the State Teachers Retirement System of Ohio (STRS Ohio) presented herein have been prepared on the accrual basis of accounting following the accounting policies set forth below.

- a. **Organization** — STRS Ohio is a cost-sharing, multiple-employer plan that was created by Chapter 3307 of the Ohio Revised Code (Revised Code) and is administered by a board comprised of five active teacher members, one retired teacher and three voting ex officio members.

The accompanying financial statements comply with the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 14, *Financial Reporting Entity*. This statement requires that financial statements of the reporting entity include all of the organizations, activities, functions and component units for which the reporting entity is financially accountable. Financial accountability is defined as the appointment of a voting majority of the component unit's board and either (1) the reporting entity's ability to impose its will over the component unit, or (2) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the reporting entity. STRS Ohio does not have financial accountability over any entities.

- b. **Investment Accounting** — Purchases and sales of investments are recorded as of their trade date. Dividend income is recognized on the ex-dividend date. Interest and rental income is recognized as the income is earned.

STRS Ohio has no individual investment that exceeds 5% of net assets available for benefits.

- c. **Contributions and Benefits** — Employer and member contributions are recorded in the period the related member salaries are earned. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

- d. **Fixed Assets** — Fixed assets are recorded at historical cost. Depreciation is provided on a straight-line basis over estimated useful lives of five to 10 years for equipment and 40 years for building and building improvements.

- e. **Method Used to Value Investments** — Investments are reported at fair value. Short-term investments are reported at amortized cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at the then current exchange rates. Fixed-income investments are valued based on their coupon rate relative to the coupon rate for similar securities. The fair value of real estate investments is based

on independent appraisals and internal valuations. The fair value of alternative investments is determined by the partnership based on the valuation methodology outlined in the partnership agreement.

- f. **Federal Income Tax Status** — STRS Ohio qualifies under Section 401(a) of the Internal Revenue Code and is exempt from federal income taxes.
- g. **Reclassifications** — Certain 2000 balances have been reclassified to conform to the current-year presentation.

2. Description of the STRS Ohio Plan

Plan Membership — STRS Ohio is a state-wide retirement plan for certified teachers and other faculty members employed in the public schools of Ohio (the state) or any school, college, university, institution or other agency controlled, managed and supported, in whole or part, by the state or any political subdivision thereof.

See charts on Page 20 for participating employers and member and retiree data.

Plan Benefits — Plan benefits are established under Chapter 3307 of the Revised Code. Any member may retire who has (i) five years of service credit and attained age 60, (ii) 25 years of service credit and attained age 55, or (iii) 30 years of service credit regardless of age.

Financial

The maximum annual retirement allowance, payable for life, is the greater of the “formula benefit” or the “money-purchase benefit” calculation. Under the “formula benefit,” the retirement allowance is based on years of credited service and final average salary, which is the average of the member’s three highest salary years. The annual allowance is determined by multiplying final average salary by 2.2% for the first 30 years of credited service. Each year over 30 years is incrementally increased by .1%, starting at 2.5% for the 31st year of Ohio service up to a maximum allowance of 100% of final

average salary. Upon reaching 35 years of contributing service, the first 31 years of contributing service is multiplied by 2.5%, and each year over 31 years is incrementally increased by .1%, starting at 2.6% for the 32nd year. Members retiring before age 65 with less than 30 years of service credit receive a percentage reduction in benefit amounts.

Effective July 1999, legislation enacted in July 2000 provided an adjustment for retirees whose benefits have not kept pace with the rate of inflation. A pension benefit payable has been reported in the statement of

plan net assets to properly accrue for the retroactive application of the legislation.

Under the “money-purchase benefit” calculation, a member’s lifetime contributions plus interest at specified rates are matched by an equal amount from contributed employer funds. This total is then divided by an actuarially determined annuity factor to compute the maximum annual retirement allowance.

Since the plan is tax-qualified, benefits are subject to limits established by Section 415 of the Internal Revenue Code.

After retirement, benefits are increased annually by the greater of the amount of the change in the Consumer Price Index (CPI) or the cumulative CPI increase since retirement, less previous cost-of-living increases, up to a maximum of 3% of the original base amount.

A retiree of STRS Ohio or another Ohio public retirement system is eligible for reemployment as a teacher following the elapse of two months from the date of retirement. Contributions are made by the reemployed member and employer during the reemployment. Upon termination of reemployment or age 65, whichever comes later, the retiree is eligible for a money-purchase benefit or a lump-sum payment in addition to the original retirement allowance.

Death, Survivor and Disability Benefits

— A member with five or more years of credited service who becomes disabled (illness or injury preventing individual’s ability to teach for at least 12 months) may qualify for a disability benefit. Additionally, eligible survivors of members who die prior to service retirement may qualify for monthly benefits. A death benefit of \$1,000 is payable to the beneficiary of each deceased

Participating Employers at June 30, 2001 and 2000		
	2001	2000
City school districts	194	194
Local school districts	369	369
County educational service centers	61	61
Exempted village school districts	49	49
Joint vocational schools	49	49
Colleges and universities	37	37
County boards of mental retardation and developmental disabilities	80	82
Community schools	72	51
State of Ohio	1	1
Other	7	7
Total	919	900

Member and Retiree Data at June 30, 2001 and 2000		
	2001	2000
Current active members	177,013	174,072
Inactive members eligible for refunds only	105,617	102,935
Terminated members entitled to receive a benefit in the future	17,827	17,428
Retirees and beneficiaries currently receiving a benefit	102,132	99,011
Reemployed retirees	14,380	13,081
Total Plan Membership	416,969	406,527

retired member. Additional death benefit coverage up to \$2,000 can be purchased. Various other benefits are available to members' beneficiaries.

Health Care Benefits After Retirement

— The plan authorizes the Retirement Board to provide access to health care benefits to retirees and their dependents.

Coverage under the current program includes hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare Part B premiums. Pursuant to the Revised Code, the State Teachers Retirement Board (the Retirement Board) has discretionary authority over how much, if any, of the associated health care costs will be absorbed by the plan. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium.

Under Ohio law, medical costs paid from the funds of the plan are included in the employer contribution rate, currently 14% of compensation. For the fiscal years ended June 30, 2001 and 2000, 4.5% and 8.0%, respectively, of covered payroll were allocated by the Retirement Board to the Health Care Reserve Fund.

Pension and postemployment health care assets are commingled for investment purposes. Consequently, amounts reported for individual asset classes are allocated between pension and postemployment health care based upon ending net assets.

Supplemental Benefits — In December of each year, if the Retirement Board determines that sufficient funds are available, a lump-sum supplemental benefit payment is made to eligible retirees. The payment is based on the retiree's years of service and date of retirement. The amount of the payment may vary and is not guaranteed from year to year.

Refunds — Upon termination of employment, a member may withdraw accumulated contributions made to STRS Ohio. Withdrawal cancels the individual's rights and benefits in STRS Ohio. Refunds of member contributions may include interest and 50% matching payments.

Alternative Retirement Plan — Eligible faculty of Ohio's public colleges and universities may choose to enroll in either STRS Ohio or an alternative retirement plan (ARP) offered by their employer.

Employees hired after the ARP is established have 120 days from their hire date to select a retirement plan.

For employees who elect an ARP, employers are required to remit 5.76% employer contributions to STRS Ohio on compensation paid for the years ended June 30, 2001, and June 30, 2000. The employer contribution rate is based on independent actuarial studies. For the year ended June 30, 2001, the ARP participant payroll totaled \$186,332,000 and there were 4,380 participants. For the year ended June 30, 2000, the ARP participant payroll totaled \$149,376,000 and there were 3,337 participants.

3. Contribution Requirements and Reserves

Employer and member contribution rates are established by the Retirement Board and limited by Chapter 3307 of the Revised Code. The employer rate is limited to 14% and the member rate is limited to 10% of covered payroll. The employer and member contribution rates for the years ended June 30, 2001 and 2000, were 14% and 9.3%, respectively. Of the 14% employer

rate, 4.5% and 8% were allocated for postemployment health care for the fiscal year ended June 30, 2001, and June 30, 2000, respectively.

Various funds are established under the Revised Code to account for contributions, reserves, income and administrative expenses.

- The Teachers' Savings Fund (TSF) is used to accumulate member contributions in trust.
- The Employers' Trust Fund (ETF) is used to accumulate employer contributions in trust. The ETF includes assets allocated to the Health Care Reserve Fund from which payments for comprehensive health care benefits are made.
- The Annuity and Pension Reserve Fund (APRF) is the fund from which all annuities and pension payments to retired members are made. Reserves are transferred to this fund from the TSF and ETF at the time of retirement.
- The Survivors' Benefit Fund (SBF) is the fund from which all survivor benefit payments are made for which reserves have been transferred from the Teachers' Savings Fund and the Employers' Trust Fund.
- The Guarantee Fund is used to accumulate income derived from gifts, bequests and investments for the year.
- The Expense Fund is the fund from which all expenses for the administration and management of STRS Ohio are paid each year.

After interest is allocated to the various funds, the Guarantee Fund and the Expense Fund are closed into the Employers' Trust Fund at year-end. At June 30, 2001 and

Fund Balances (in thousands)		
	2001	2000
Teachers' Savings Fund	\$ 7,445,894	\$ 7,174,675
Employers' Trust Fund	15,896,463	23,532,839
Annuity and Pension Reserve Fund	29,293,437	26,648,931
Survivors' Benefit Fund	698,581	663,024
Total	\$ 53,334,375	\$ 58,019,469

2000, plan net assets were included in the various funds as shown in the table above.

4. Commitments and Contingencies

STRS Ohio has made commitments to fund various real estate investments totaling approximately \$592,555,000 as of June 30, 2001. The commitments for the year ended June 30, 2001, have expected funding dates from October 2001 to December 2004.

STRS Ohio has made commitments to fund various alternative investments totaling approximately \$1,291,729,000 as of June 30, 2001. The average expected funding dates for the commitments as of June 30, 2001, range from July 2001 to June 2008.

STRS Ohio is a party in various lawsuits. While the final outcome cannot be determined at this time, management is of the opinion that the liability, if any, for these legal actions will not have a material adverse effect on the net assets available for benefits.

5. Cash and Investments

GASB Statement No. 3 — Statement No. 3 of the Governmental Accounting Standards Board requires governmental entities to

categorize investments as an indication of the level of risk at fiscal year-end. Category 1 includes investments that are insured or registered or for which the securities are held by STRS Ohio or its agent in the name of STRS Ohio. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of STRS Ohio. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty in STRS Ohio's name or held by the counterparty's trust department or agent but not in STRS Ohio's name.

All investments subject to categorization at June 30, 2001 and 2000, meet the criteria of Category 1. Investments are held in the name of STRS Ohio or its nominee by the treasurer of the state of Ohio as custodian. Real estate investments and securities on loan are investments that, by their nature, are not required to be categorized.

At June 30, 2001 and 2000, the carrying amount of STRS Ohio cash deposits were \$2,441,000 and \$(1,816,000) and the bank cash balances were \$10,048,000 and \$10,757,000, respectively. Of the bank balances, \$100,000 was insured by the Federal Deposit Insurance Corporation. The remaining bank balance was covered by collateral

held in the name of STRS Ohio's pledging financial institution, as required by state statute (Category 3).

Investment Authority — The investment authority of the Retirement Board is governed by Section 3307.15 of the Revised Code that also requires the Retirement Board to publish its investment policies annually and make copies available to interested parties. This section requires that investments be made with care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. It further provides that the Retirement Board may invest in bonds, notes, certificates of indebtedness, mortgage notes, real estate, stocks and debentures with certain restrictions as to the nature and quality of the investment and composition of the investment portfolio.

Investments held at fair market value by STRS Ohio at June 30, 2001 and 2000, are summarized in the chart on Page 23.

Fair Valuation — Stocks traded on a national securities exchange are valued at the closing price on the last business day of the fiscal year; stocks traded over the counter are valued at the closing price, as reflected by NASDAQ, on the last business day of the fiscal year; international investments are valued by the subcustodian using relevant closing market prices and exchange rates; U.S. government and governmental agency securities, bonds, certain guaranteed mortgages, and short-term corporate and government notes are valued based on information from an independent service organization for institutional investors; guaranteed mortgages are valued based on their

coupon rate relative to the coupon rate for similar mortgages on the last business day of the fiscal year; short-term cash equivalent investments are stated at amortized cost which approximates fair value; real estate is valued based on appraisals performed by independent appraisers or, for properties not appraised, at the present value of the projected future net income stream. All real estate investments have independent appraisals at the minimum of every three years. The fair value of alternative investments is determined by the alternative investment partnership based on the valuation methodology outlined in the partnership agreement.

Securities Lending — STRS Ohio participates in a domestic and international securities lending program whereby securities are loaned to investment brokers/dealers (borrower). Securities loaned are collateralized by the borrower at 102% of the domestic loaned securities' fair value and 105% of the international loaned securities' fair value.

STRS Ohio lends domestic equities, international equities, U.S. Treasuries, agencies and corporate bonds. The collateral received is cash, U.S. Treasuries or related agency securities. STRS Ohio cannot sell or pledge collateral received. If a borrower defaults, then the collateral can be liquidated.

A custodial agent bank administers the program and STRS Ohio receives a fee from the borrower for the use of loaned securities. Cash collateral from securities lending is invested in repurchase agreements, commercial paper and U.S. corporate obligations. The credit quality of the invested cash collateral is the same as the credit quality on STRS Ohio direct holdings. There are slight mismatches between the duration of the cash

Investments Held at Fair Value by STRS Ohio at June 30, 2001 and 2000 (summarized and in thousands)

Category	June 30, 2001	June 30, 2000
Short-term:		
Commercial paper	\$ 613,248	\$ 735,186
Government notes	10,000	10,000
Short-term investment funds	5,000	14,614
Total short-term	<u>628,248</u>	<u>759,800</u>
Fixed income:		
Guaranteed mortgages	3,371,419	4,078,061
U.S. government/agencies:		
Not on securities loan	594,246	1,798,761
On securities loan	1,932,186	2,260,891
Corporate bonds:		
Not on securities loan	4,378,725	4,331,807
On securities loan	126,527	59,646
Canadian bonds	110,632	116,559
Supernationals	127,386	100,667
Municipal bonds	—	293
High yield and emerging market:		
Not on securities loan	827,737	—
On securities loan	112,825	—
Total fixed income	<u>11,581,683</u>	<u>12,746,685</u>
Common and preferred stock:		
Not on securities loan	23,325,508	26,054,617
On securities loan	848,829	653,518
Total common and preferred stock	<u>24,174,337</u>	<u>26,708,135</u>
International: (See Note 6)		
Not on securities loan	8,674,099	10,256,266
On securities loan	494,112	453,835
Total international	<u>9,168,211</u>	<u>10,710,101</u>
Real estate: (See Note 7)		
East region	1,260,205	1,118,422
Midwest region	939,894	1,006,963
South region	927,093	931,457
West region	1,602,373	1,407,536
REITs	636,360	492,718
Other	969,194	896,546
Total real estate	<u>6,335,119</u>	<u>5,853,642</u>
Alternative investments	923,253	747,525
Invested securities lending collateral	3,615,793	3,498,469
Total investments and invested securities lending collateral	<u>\$ 56,426,644</u>	<u>\$ 61,024,357</u>

invested and the length of time the securities are on loan. As of June 30, 2001, the average maturity of the invested cash collateral is 459 days. Because much of the cash collateral is invested in floating rate securities, interest rates are reset every 29 days on average as of June 30, 2001. STRS Ohio has minimized its exposure to credit risk due to borrower default by having the custodial agent bank determine daily that the required collateral meets the specified collateral requirements. There are no restrictions on the amount of securities that can be loaned. The fair value of the loaned securities was \$3,514,479,000 and \$3,427,890,000 as of June 30, 2001 and 2000, respectively. The fair value of the associated collateral received as of June 30, 2001 and 2000 was \$3,619,392,000 and \$3,498,469,000, respectively.

The difference between the obligations under securities lending and the invested securities lending collateral is caused by the default of a Pacific Gas & Electric commercial paper investment. Pacific Gas & Electric is in bankruptcy and the fair value as of June 30, 2001, of the commercial paper investment has been recorded in the financial statements.

6. International Investments

Externally Managed — STRS Ohio has investments in international equity securities through the use of external money managers. It is the intent of STRS Ohio and the money managers to be fully invested; however, cash and short-term fixed-income investments are held temporarily. The portfolios are managed in accordance with various mandates based on Morgan Stanley

Capital International's (MSCI) indexes. Investments are held in both developed and emerging international markets.

Internally Managed:

Country Funds — STRS Ohio actively invests in developed and emerging markets through traded country funds. Each country fund consists of individual equity securities pooled together in an attempt to match or exceed the local country's index.

Europe, Australasia and Far East (EAFE) Index Fund — To increase diversification in international developed markets, STRS Ohio invests in an EAFE Index Fund. The EAFE Index Fund purchases foreign equities, futures and other traded investments to replicate the makeup of the EAFE benchmark.

Emerging Markets Free (EMF) Index Fund — STRS Ohio invests in an EMF Index Fund to increase diversification in emerging market countries. The fund invests in foreign equities, swaps and other traded investments to imitate the EMF Index.

EAFE Equity Swaps — Four international equity swap agreements were contracted during fiscal 2001 with maturity dates in fiscal 2002. In exchange for a negotiated LIBOR (London Interbank Offered Rate), STRS Ohio will receive dividends on a quarterly basis. At maturity, STRS Ohio will receive or pay the difference in the change in the various market indices included in the swap agreement. Fixed-income securities with an initial notional amount of \$1.5 billion have been set aside at the Bank of New York as security.

The fair values of international investments held at June 30, 2001 and 2000, are shown in the chart on Page 25.

7. Real Estate Investments

General — STRS Ohio properties are geographically distributed throughout the United States. Real estate investments include retail single-tenant stores and malls, single and multitenant office properties and warehouses, apartments, REITs and other.

REITs — Real estate investment trusts (REITs) are real estate company stocks with a high dividend-income component. REITs divide the ownership of the real estate company and its properties among all the shareholders. REITs are required to distribute 95% of the company's taxable income to their shareholders. Distributions are taxable to shareholders rather than the real estate company. STRS Ohio is exempt from federal and state income taxes.

Other — Other real estate investments include farmland, timberland and opportunity funds, that are externally managed, and private REITs. Farmland investments generate income primarily as a result of harvest proceeds. Income is generated from the sale of timber on timberland investments. Opportunity funds generate income as a result of operations and property sales, which are distributed to the investors. Finally, private REITs are privately traded real estate company stocks with a dividend-income component, similar to the public REIT investments discussed above.

8. Derivatives

Equity Swap Agreements — As discussed in Note 6, STRS Ohio has entered into international equity swap agreements. No funds are required as collateral by either party; however, STRS Ohio has purchased fixed-income securities equivalent to the initial

exposure, which are located in a subcustodial account at the Bank of New York. The initial notional amount of the fixed-income securities is \$1.5 billion. The market risk of the swap is the same as if STRS Ohio owned the underlying stocks that comprise the indexes. The net interest revenues and expenses resulting from these agreements have been recorded in the financial statements. See the chart below for the related equity swap fair values as of June 30, 2001 and 2000. Equity swaps were also used in the EMF Index Fund during 2000. Of the total EMF holdings, \$12.6 million were invested in swap agreements at June 30, 2000.

Forward Contracts — Forward contracts in various currencies were used to transact and hedge direct foreign equity investments that STRS Ohio maintains through the use of outside managers. Additionally, forward contracts were used to hedge currency exposure as a result of the EAFE Equity Swap agreements. STRS Ohio is obligated to deliver the foreign currency at a certain dollar price sometime in the future. To fulfill this obligation at maturity, STRS Ohio must obtain the currency in the open market. Before the contract matures, STRS Ohio can enter into an offsetting forward contract that nets out the original contract. These events expose STRS Ohio to currency market risk, which can fluctuate. STRS Ohio is also subject to the risk that the counterparty will fail to fulfill the contract. The external money managers hedged \$1.37 and \$1.95 billion of currency exposure in various currencies with varying maturities as of June 30, 2001 and 2000, respectively. At June 30, 2001, STRS Ohio hedged \$1,441 and \$32 million of currency exposure on the EAFE Index Fund and the Country Funds, respectively. At June 30, 2000, STRS Ohio hedged \$1,388 and \$57

million of currency exposure on the EAFE Index Fund and the Country Funds, respectively.

Futures — STRS Ohio had investments in S&P 500 index futures during the year. Index futures are designed to offer lower-cost and more efficient alternatives to buying a basket of individual stocks that comprise the index. The market and credit risk of the futures were the same as if STRS Ohio had owned the underlying stocks that comprise the index. From July 1999 to June 2000, S&P future notional amounts ranged from \$3.6 million to \$459 million. From July 2000 to June 2001, S&P future notional amounts ranged from \$7.1 to \$896.6 million. Additionally, futures were used in the EAFE Index Fund. Of the total EAFE Index Fund holdings, \$15.1 and \$34.7 million were invested in futures at June 30, 2001 and 2000, respectively. External money managers also used futures. Approximately, \$52.7 and \$49.9 million of external money managers' holdings

were invested in futures at June 30, 2001 and 2000, respectively.

Options — STRS Ohio writes option contracts on existing stock positions to enhance the return on the stock portfolio. In exchange for a premium, STRS Ohio gives the option buyer the right to buy or sell the underlying stock. Options are also purchased to "cover" existing written open option positions. There were no open option contracts as of June 30, 2001 or 2000.

9. State Appropriations

From time to time, the Legislature of the state has increased benefit payments to retirees. In certain instances, concurrent with the passage of such legislation, a provision for reimbursement of these benefits through future state appropriations has been made. In January 2001, the state Legislature acted to discontinue reimbursement for these benefit increases in the future.

Fair Values of International Investments Held at June 30, 2001 and 2000 (in thousands)		
	June 30, 2001	June 30, 2000
Externally managed		
International stocks	\$ 5,179,648	\$ 6,880,342
International fixed income	95,390	137,587
International currency and liquidity reserves	222,157	242,263
Forward contracts	7,102	(24,890)
Total externally managed	<u>5,504,297</u>	<u>7,235,302</u>
Internally managed		
Country Funds	533,363	515,172
EAFE Index Fund	2,983,118	2,583,604
EMF Index Fund	253,394	342,276
EAFE Equity Swaps	(105,961)	33,747
Total internally managed	<u>3,663,914</u>	<u>3,474,799</u>
Total international	<u>\$ 9,168,211</u>	<u>\$ 10,710,101</u>

Financial

STRS Ohio received approximately \$1,514,000 from the state for increased benefits paid for the year ended June 30, 2000.

10. Pension Plan

Substantially all STRS Ohio employees are required to participate in a contributory retirement plan administered by the Public Employees Retirement System of Ohio (PERS). PERS is a cost-sharing multiple-employer public employee retirement system.

Eligible employees are entitled to a retirement benefit, payable monthly for life, equal to 2.2% of their final average salary for each year of credited service up to 30 years and 2.5% for each year of service over 30 years. Final average salary is the employee's average salary over the highest three years of earnings. Benefits fully vest on reaching five years of service. Vested employees may retire at any age with 30 years of credited service, at age 55 with a minimum of 25 years of credited service, and at age 60 with a minimum of five years of service. Employees retiring with less than 30 years of service and under age 65 receive reduced retirement benefits. Benefits are established by state statute.

Employees covered by PERS are required by Ohio statute to contribute 8.5% of their salary to the plan. STRS Ohio is required by the same statute to contribute 13.55% of covered payroll; 9.25% is the portion used to fund pension obligations, with the remainder used to fund the health care program for retirees. PERS made a one-time employer contribution rate rollback for calendar year 2000. The employer rate was 10.84% for calendar year 2000. The required employer contributions for the current year and the two preceding years are shown in the chart on this page.

Historical trend information showing the progress of PERS in accumulating sufficient assets to pay benefits when due is presented in the PERS *Comprehensive Annual Financial Report*. PERS issues a publicly available financial report for the plans. The report may be obtained by writing to PERS, 277 E. Town St., Columbus, Ohio 43215-4642.

PERS also provides postemployment health care coverage to age and service retirees with 10 or more years of qualifying Ohio service credit and to primary survivor recipients of such retirees. Health care coverage for disability recipients is available. The health care coverage provided by the retirement system is considered an Other Postemployment Benefit (OPEB) as described in

GASB Statement No. 12. A portion of each employer's contribution to PERS is set aside for the funding of postemployment health care. The Revised Code provides statutory authority for employer contributions. The 2000 employer contribution rate for local government employees was 10.84% of covered payroll; 4.30% was the portion that was used to fund health care for the year.

PERS expenditures for OPEB during 2000 were \$559,606,000.

11. Required Supplemental Schedules and Additional Information

The schedule of funding progress, the schedule of employer contributions and the related notes are required supplemental schedules. These schedules are presented on Page 27 and are designed to provide information about STRS Ohio's progress in accumulating sufficient assets to pay benefits when due. The schedule of administrative expenses and the schedule of investment expenses are included as additional information. These schedules are presented on Pages 28 and 29.

STRS Ohio Required Employer Contributions to PERS		
Year Ended June 30	Annual Required Contributions	Percentage Contributed
2001	\$ 3,968,000	100%
2000	\$ 4,151,000	100%
1999	\$ 3,472,000	100%

Required Schedule of Employer Contributions For the Years Ending June 30, 1996–2001 (in thousands)

Year Ended June 30	Annual Required Contributions*	Percentage Contributed
2001	\$ 777,416	100%
2000	470,343	100%
1999	446,655	100%
1998	746,773	100%
1997	816,696	100%
1996	786,437	100%

* The amounts reported in this schedule do not include contributions for postemployment health care benefits.

As an investments accountant, Judy provides accurate figures to the STRS Ohio Retirement Board, auditors and senior staff to help them make sound decisions.



Required Schedule of Funding Progress For the Years Ending June 30, 1996–2001 (dollar amounts in thousands)

Valuation Year	Actuarial Accrued Liability (AAL)*	Valuation Assets*	Unfunded Actuarial Accrued Liability (UAAL)*	Ratio of Assets to AAL	Covered Payroll**	UAAL as % of Covered Payroll
2001	\$ 59,425,300	\$ 54,194,672	\$ 5,230,628	91.2%	\$ 8,256,683	63%
2000	55,774,052	51,293,815	4,480,237	92.0%	7,845,021	57%
1999	51,979,974	46,341,436	5,638,538	89.2%	7,444,243	76%
1998	48,972,084	41,709,903	7,262,181	85.2%	7,112,124	102%
1997	44,704,237	36,883,739	7,820,498	82.5%	6,805,797	115%
1996	41,128,062	32,930,801	8,197,261	80.1%	6,553,642	125%

* The amounts reported in this schedule do not include assets or liabilities for postemployment health care benefits.

** Covered payroll includes salaries for alternative retirement plan participants. For 2001 and 2000, alternative retirement plan participant payroll totaled \$186,332 and \$149,376, respectively.

Notes to the Trend Data

Valuation date	July 1, 2001	July 1, 2000
Actuarial cost method	Entry age	Entry age
Amortization method	Level percent closed	Level percent closed
Remaining amortization period	27.5 years	23.1 years
Asset valuation method	4-year smoothed market with 91%/109% corridor	4-year smoothed market with 91%/109% corridor
Actuarial assumptions:		
Investment rate of return	7.75%	7.75%
Projected salary increases	9.25% at age 20 to 3.25% at age 65	9.25% at age 20 to 3.25% at age 65
Inflation assumption	3.50%	3.50%
Cost-of-living adjustments	3% simple	3% simple

The information presented in the required supplemental schedules was determined as part of the actuarial valuations at the dates indicated. The information in the table is from the latest actuarial valuations.

Financial

Kevin oversees the STRS Ohio refund process, ensuring members receive the correct amount if they withdraw their account.



Schedule of Administrative Expenses For the Years Ending June 30, 2001 and 2000

	2001	2000
Personnel		
Salaries and wages	\$ 25,957,912	\$ 20,601,552
Retirement contributions	2,753,803	2,853,638
Benefits	3,862,264	2,689,260
Total personnel	32,573,979	26,144,450
Professional and technical services		
Computer support services	10,212,356	9,005,571
Health care services	1,548,734	1,645,420
Actuary	239,083	283,480
Auditing	71,329	69,733
Legal	358,059	232,803
Temporary employment services	143,627	168,592
Total professional and technical services	12,573,188	11,405,599
Communications		
Postage and courier services	1,936,578	1,939,015
Printing and supplies	3,799,746	2,625,742
Telephone	869,822	697,262
Total communications	6,606,146	5,262,019
Other expenses		
Equipment repairs and maintenance	2,718,681	1,826,506
Building utilities and maintenance	1,351,114	1,023,487
Transportation and travel	627,349	704,510
Recruitment fees	238,320	307,977
Equipment rental	4,510,381	3,322,708
Depreciation	8,924,630	6,282,680
Member and staff education	408,420	172,696
Insurance	354,910	300,205
Memberships and subscriptions	190,328	132,078
Retirement study commission	318,430	286,943
Miscellaneous	881,525	644,742
Total other expenses	20,524,088	15,004,532
Total administrative expenses	\$ 72,277,401	\$ 57,816,600

Schedule of Investment Expenses For the Years Ending June 30, 2001 and 2000

	2001	2000
Personnel		
Salaries and wages	\$ 13,031,461	\$ 10,726,151
Retirement contributions	1,214,519	1,297,401
Benefits	1,254,054	797,897
Total personnel	15,500,034	12,821,449
Professional and technical services		
Legal	94,066	36,373
Investment research	851,936	507,168
Real estate and international advisors	579,753	491,933
Investment advisors	420,000	478,114
Banking fees	3,791,643	4,102,679
Total professional and technical services	5,737,398	5,616,267
Other expenses		
Printing and supplies	23,925	5,955
Equipment repairs and maintenance	460	1,606
Building utilities and maintenance	729,831	641,836
Travel	714,646	649,895
Equipment rental	167,869	150,004
Memberships and subscriptions	108,228	95,893
Miscellaneous	62,319	68,148
Total other expenses	1,807,278	1,613,337
Total investment expenses	\$ 23,044,710	\$ 20,051,053



Katherin verifies that each member's service credit matches employers' annual reports.



Suchit tracks international economies and investments to take advantage of opportunities to strategically diversify STRS Ohio's portfolio. Providing for members' retirements is the "single focus" of his decision-making.



Investment Review

For Fiscal Year July 1, 2000, through June 30, 2001
Prepared by STRS Ohio's Investments Associates

Economic growth decelerates from deteriorating business conditions

A significant slowing of economic activity throughout fiscal year 2001 left real gross domestic product (GDP) growing at a 1.2% rate — well below the fiscal year 2000 growth rate of 5.2% and the economy's long-term potential growth rate of roughly 3%. Excessive inventory building in prior years led to a huge inventory liquidation in the last half of the fiscal year. Capital equipment spending by businesses collapsed, falling by more than 4% after averaging better than a 12% annualized gain over the prior eight years. The combination of less business spending and a decline in inventories was reflected in a significant plunge in manufacturing production and, subsequently, severe job slashing. Furthermore, a negative wealth effect brought about by a nearly 16% dive in stock prices eroded consumer confidence and consumer spending. Real consumer spending grew 3.2% during fiscal 2001, below both the 4.9% growth rate of fiscal 2000 and the average annual growth of 5.0% from the previous three years. Meanwhile, housing and auto sales remained robust — largely due to low interest rates and auto dealer incentive programs — even as the unemployment rate moved to 4.5% at the end of fiscal 2001 from 4% the year before. Foreign trade of

goods and services continued to be a drag on GDP as growth in the rest of the world began to slow along with the United States. Exports posted a decline of nearly 2% due to slower demand abroad along with a strengthening dollar while imports declined at a 0.6% rate. Finally, federal, state and local government expenditures grew by 2.9%, a bit below the 4% pace from the prior year.

Consumer prices moved lower during fiscal 2001 due to the slowing economy. The consumer price index increased by 3.3%, down from 3.7% the prior year. Energy costs remained high during the year, recording an 8.5% increase due to a surge in gasoline prices during the spring quarter. Excluding energy prices, inflation indicators showed more modest gains in fiscal 2001. The core consumer price index, which excludes food and energy costs, rose 2.8% during the fiscal year while the GDP price index, which is the broadest measure of inflation, remained stable over the year as it posted a 2.3% gain.

After raising interest rates for an extended period in fiscal 2000, the Federal Reserve began lowering interest rates in January 2001. The federal funds rate started fiscal 2001 at 6.5% and finished the year at 3.75%. Meanwhile, the 10-year Treasury bond began the fiscal year at roughly 6%, declined below 5% in January 2001 (and again in March) and then gradually moved back up toward 5.4% by the end of the fiscal year. Mortgage rates declined from around

8% at the start of the year into January before stabilizing within a narrow range of roughly 6.9% to 7.25%. The conventional 30-year mortgage rate ended the fiscal year at 7.1%.

The bear market in stocks gathers strength

The bear market in stocks that began in spring 2000 continued throughout the fiscal year. The final deflation of the tech-driven stock bubble, combined with increasing concerns over the economy and earnings, drove from the market the remaining optimists who believed the downturn would be short-lived. The S&P 500 began the fiscal year around 1450 before sliding in late September. The drop continued with only minor bounces until early April 2001 when the index bottomed at just over 1100. A rally through the remainder of the spring brought the index to a fiscal-year close of 1225. The NASDAQ Composite, which has had more exposure to the "tech wreck," was hit even harder. From a high of 4275 in July 2000 (already down from the all-time high of 5048 in March 2000), the NASDAQ dropped an additional 62% while hitting a low of 1639 in early April 2001.

By sector, information technology and telecommunications were the big losers with both falling more than 50%. Utilities performed well, as would be expected in a

Investments

down market, returning a robust 21%. More surprising, however, was the best performing sector — financials. This is likely explained by the quality of financial companies being overlooked during the long tech run and, subsequently during the tech decline, being viewed as relatively safe havens.

STRS Ohio performance reports follow the industry convention of reporting on a calendar-year basis. During calendar year 2000, STRS Ohio domestic equities returned -6.27% while the S&P 1500 returned -6.98%. Domestic equities accounted for \$24.2 billion, or 45.8% of total STRS Ohio assets at the end of fiscal 2001. The top 20 STRS Ohio common stock holdings are shown in the schedule of largest investment holdings starting on Page 50. Equity investment results are on Page 48.

International stock markets collapse

During fiscal 2001, equity markets around the world tumbled. The developed markets, represented by the Morgan Stanley Capital International (MSCI) Europe, Australasia, Far East (EAFE) Index (50% hedged), fell 17.8%. The weakness was widespread with only one small market producing positive results. The major markets were all off sharply.

Emerging markets also produced negative returns for the year. The emerging markets, represented by the MSCI Emerging Markets Free (EMF) Index, fell 25.8%. Weakness was seen in every region throughout the world, with the Far East experiencing the most damage.

STRS Ohio performance reports follow the industry convention of reporting on a calendar-year basis. The STRS Ohio international

portfolio returned -16.17% during calendar 2000. Meanwhile, the benchmark STRS Ohio international hybrid index, consisting of 75% of the MSCI EAFE Index (50% hedged) and 25% of the MSCI EMF Index, returned -15.69% in 2000. The STRS Ohio international portfolio exceeded the benchmark for the two-year, three-year and since-inception time periods through calendar 2000. Performance results of the international equities portfolio on a calendar-year basis are on Page 48.

The international portfolio was valued at \$10.7 billion at the end of fiscal 2001, which represented 20.2% of total STRS Ohio assets. Developed market investments totaled \$7.5 billion, or 14.2% of total assets, and emerging market investments were \$3.2 billion, or 6.0% of total assets. External managers were responsible for managing 52% of the international portfolio; the remaining 48% was internally managed.

The failing economy leads to lower interest rates

The 10-year Treasury yielded 6% at the beginning of fiscal 2001, starting the year close to the highest level for the entire period. In the year preceding fiscal 2001, economic growth was strong, inflation was low and the stock market was perched at all-time highs. The Federal Reserve raised short-term interest rates 1-3/4 percentage points during that period to slow economic growth and avoid excessive inflation. This had more than the desired effect as economic growth slowed roughly four percentage points to 1.2% during fiscal 2001 and inflation remained well contained.

With the economy slowing, in early January 2001 the Federal Reserve reversed policy and aggressively began reducing short-term interest rates. The bond market responded favorably and 10-year Treasury yields began to decline — eventually hitting a low of 4.75% in March. During the remainder of the fiscal year, Treasury yields moved higher in anticipation of stronger economic growth in the future. The 10-year Treasury finished the fiscal year at a 5.4% yield.

Effective Oct. 1, 2000, the State Teachers Retirement Board approved a new benchmark — the Lehman Universal Index — for the fixed-income portfolio. This is a broad index of all U.S. dollar-pay fixed-income securities around the world. The prior benchmark, the Lehman Aggregate Index that consists of high quality government, agency, corporate and mortgage-backed securities, comprises 85% of the new index. The remaining 15% of the new index includes high yield, emerging market and dollar-pay debt issued in foreign markets. Due to the more credit-intensive aspect of this index, an increasingly important contributor to relative returns will be determined through sector rotation and security selection rather than shifting the portfolio's exposure to anticipated changes in interest rates.

During the first half of the fiscal year, the fixed-income portfolio was underweighted to credit-sensitive securities because a slowing economy was expected to dampen corporate earnings. As credit-sensitive sectors underperformed, exposure to this segment was overweighted versus the benchmark. This positioned the portfolio to earn higher returns relative to the benchmark should the outlook for economic growth improve. Indeed, after the Federal Reserve changed

its policy to reduce short-term interest rates, credit-sensitive securities improved, helping the fixed-income portfolio to outperform its benchmark.

Performance measurement follows industry convention of reporting on a calendar-year basis. The benchmark closely resembles the characteristics of investments for the STRS Ohio fixed-income portfolio and is used as a comparison for relative performance. The STRS Ohio fixed-income portfolio returned 12.53% versus the benchmark's return of 11.09%. The primary reasons for the out-performance relative to the benchmark were properly positioning the portfolio for a decline in interest rates and underweighting credit-sensitive securities (which significantly underperformed the benchmark late in the calendar year). A more complete report of STRS Ohio performance appears on Page 48. The fixed-income market performed well during the fiscal year. Sales of fixed-income securities to fund other asset classes lowered the share of the total fund allocated to fixed income to 19% from 20%.

Real estate market provides solid returns

The real estate market turned in another year of solid performance and surprisingly stronger returns than those found in a robust 1999. While the economy showed signs of weakening, the real estate markets worked with a lag that kept the impact from being felt. The supply side of the physical space market is generally at appropriate levels and not considered a real risk. The demand side of the equation is where most of the risk is currently and will continue to be over the next 12 to 18 months.

Given the economic uncertainty at fiscal year-end, the capital markets for private real estate have begun pulling back, with this trend expected to gain momentum and continue in the near term. The public equity market showed a dramatic turnaround in 2000 with a return of 26.4% for the year. This market had a negative return of almost 5% in 1999. The public real estate market is heavily influenced by the broader equity market and, thus, experiences greater fluctuations year over year than does the private market. Returns in both the private and public sector are expected to weaken for 2001.

STRS Ohio's returns exceeded the composite benchmark for calendar year 2000, marking the fourth consecutive year of out-performance. STRS Ohio's portfolio returned 15.43% compared to the benchmark return of 12.43%. During the calendar year, the portfolio increased in size by 15% to \$6.2 billion. This growth is attributable to net new investments in excess of \$350 million and very strong appreciation of almost 8% on the existing base of assets. At the end of fiscal 2001, the real estate portfolio represented 12% of total assets and had a market value of \$6.3 billion. Performance results for the real estate portfolio are on Page 48.

Total fund return exceeds benchmark

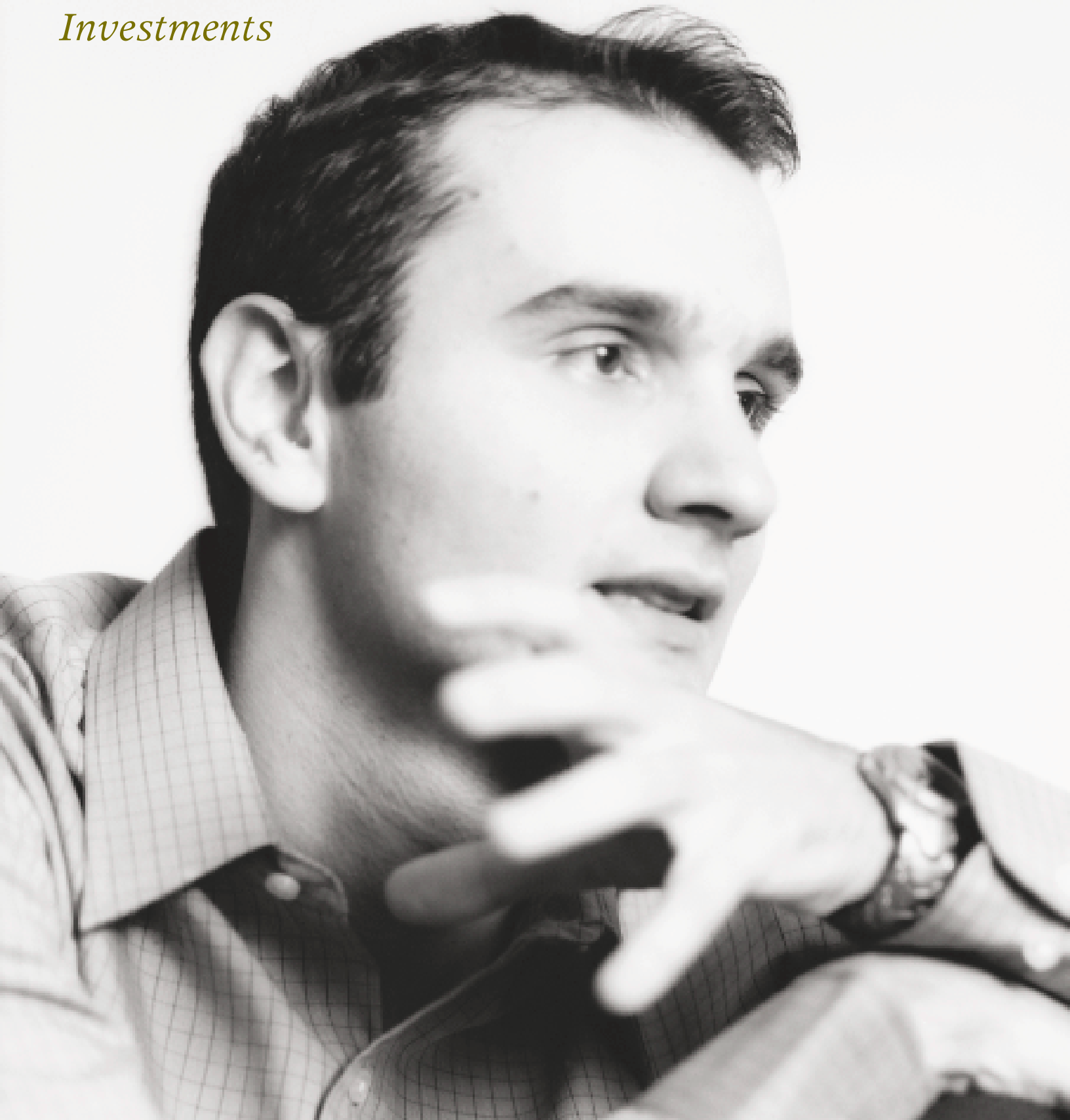
During calendar year 2000, the STRS Ohio fund returned -2.43%. (STRS Ohio performance is more appropriately calculated on a calendar-year basis for adequate comparisons with other performance publications.) The hybrid index of industry benchmarks returned -2.60% during 2000. STRS Ohio's rate of return for the five-year period ending

Dec. 31, 2000, was 10.97%, more than the 8% absolute long-term return goal but below the relative hybrid index of industry benchmarks, which rose by 11.78%. Over the past three calendar years, the STRS Ohio fund returned 9.44%, while the hybrid index of industry benchmarks rose 9.77%.

The relative performance of most STRS Ohio asset categories compared to their benchmarks continued to fare well. Over the past three years, the STRS Ohio domestic equities portfolio grew 10.31% versus the S&P 1500's 12.23% average annualized gain. The STRS Ohio international portfolio returned an annualized 7.78% through the past three calendar years, while the benchmark grew 5.76%. Fixed-income investments over the past three years returned 6.62% versus 6.19% for the benchmark. The return from real estate investments outpaced its benchmark over the past three years, growing at an annualized 13.07% versus the benchmark increase of 11.14%.

The total return on STRS Ohio investment assets over the preceding five-year period exceeded the rate of inflation, as measured by the GDP deflator, by 9.21 percentage points. Over the three-year period, the return on STRS Ohio investment assets has exceeded the inflation rate by 7.75 percentage points.

Investments



Igor helps balance STRS Ohio's portfolio by investing in emerging markets. While this asset class involves more risk, it can add incremental returns to enhance retirement income for Ohio's educators.



Investment Objective and Policy

Effective Sept. 20, 2001

General Policy Statement

Introduction

The State Teachers Retirement System of Ohio is governed by a board of nine members with broad statutory powers. The investment function is vested in the board as set forth in Section 3307.15 of the Ohio Revised Code. Section 3307.15 of the Ohio Revised Code requires the board to "...adopt in regular meeting, policies, objectives or criteria for the operation of the investment program ..." These policies, objectives and criteria are adopted under this authority.

It is the intent of the board to give consideration to investments that enhance the general welfare of Ohio provided such investments offer quality return and safety comparable to other investments currently available to the board. The board also will give consideration to investments that involve minority-owned and minority-controlled firms and firms owned or controlled by women.

Sections 3307.04 and 3307.15 of the Ohio Revised Code empower the board to authorize its administrative officers and committees to act for it in accord with its policies. In addition to the investment function, Section 3307.15 of the Ohio Revised Code also sets

forth the fiduciary responsibility of the board and other fiduciaries in discharging their duties with respect to the fund. Section 3307.01 (K) of the Ohio Revised Code defines a fiduciary, and Sections 3307.151, 3307.181, 3307.15 and 3307.18 of the Ohio Revised Code list specific items a fiduciary shall and shall not do. This Investment Objective and Policy incorporates and is subject to all of the above-mentioned sections of the Ohio Revised Code.

Staff and Board

Participation in the affairs of any public body demands high personal integrity and conduct. This is especially true when funds of others are involved. Members of the board and staff must discharge their responsibilities without prejudice or favor, avoiding at all times any conduct that could create or appear to create a conflict of interest.

Staff members shall carry out the duties and responsibilities delegated by the board in the best interest of members of the system and in accordance with the code of ethics of the Association for Investment Management and Research. No staff member shall engage in any activity in his or her official position or in a personal investment program that will in any way create a conflict of interest.

Organization

Investment Committee

An Investment Committee is established and consists of all nine members of the board. The Investment Committee is empowered to advise the board in all investment matters.

Investment Advisors/Consultants

The board shall employ competent, well-qualified organizations to assist in carrying out its fiduciary responsibility. Duties of the investment advisors/consultants shall include but not be limited to:

1. Recommending long-term investment objectives and review of these objectives at least annually.
2. Monitoring performance of the investment program.
3. Availability to counsel with in-house staff, executive director or members of the board.
4. Participation in bimonthly meetings of the Investment Committee.
5. Review and advise on detailed investment criteria for all investments.
6. Review of Annual Investment Plan.
7. Performance of such other duties as may be provided by contract.

Investments

Executive Director

Subject to this Investment Objective and Policy, the executive director is authorized by the board under Sections 3307.04 and 3307.15 to act for and on behalf of the board and the system in all purchases, sales or other investment transactions. Investment transactions since the last report will be reviewed by the Investment Committee at each meeting and upon such review shall be deemed accepted, ratified and adopted by the board. The Investment Committee may act at the time of such review to direct the subsequent sale or disposal of any investment.

Deputy Executive Director — Investments

The deputy executive director — Investments shall have the following responsibilities:

1. Supervise activities of the in-house staff.
2. In cooperation with the investment advisor and the executive director, formulate an Annual Investment Plan.
3. Make recommendations to the executive director and board concerning periodic modification of the Annual Investment Plan.
4. Assure that the portfolios comply with established parameters and risk levels.
5. Supervise execution of orders to buy and sell securities (including options) seeking always to maintain reasonable costs for such services.
6. Report in required detail to the executive director and the Investment Committee and/or the board on all activities of the investment staff.

Objectives, Guidelines and Policies: Total Fund

Objectives

In many if not most instances, payments from the pension fund are the major sources of income to retirees and a principal protection against the contingencies of death and disability for active workers. Therefore, the basic policy of the board is preservation of the capital investment and realization of sufficient return to secure and facilitate payment of the statutory benefit requirements of the system to its participants and beneficiaries. In this connection, it is recognized that the fund will achieve some protection against erosion of principal value through inflation if the actuarially assumed interest rate is achieved.

Maximization of return, from both current income and capital appreciation consistent with the overall risk parameters described below, is an important objective. With the insight gained from careful studies of the benefits of diversification and asset return potential, the board sets a total return objective of 8% per annum. This is a long-term objective, and this total return expectation assumes a modest rate of inflation. The objective should be pursued consistent with prudent management.

The board anticipates that contributions to the pension fund and income from existing assets will exceed disbursements for the foreseeable future. Therefore, there is no special need for liquidity in the portfolio, other than that deemed necessary to accomplish investment objectives and strategies.

Asset Class	Asset Mix General Policy Ranges at Market	Average Long-Term Weightings at Market
Liquidity Reserves	0-4%	1%
Fixed Income	13-28%	23%
Domestic Equities	43-50%	45%
International	15-25%	20%
Real Estate	6-12%	9%
Alternative Investments	1-3%	2%
		100%
Asset Class	Total Return Objective	Benchmarks
Liquidity Reserves	4-5%	90-Day Treasury Bills
Fixed Income	6-7%	Lehman Universal Bond Index
Domestic Equities	8-10%	S&P 1500
International	8-10%	75% EAFE*/25% EMF
Real Estate	8-9%	NCREIF Adjusted
Alternative Investments	14-16%	Absolute Return

* 50% hedged

Given the expected contribution income, forecast of benefit obligations and acceptable actuarial asset value smoothing techniques, the risk level of the pension fund, meaning the tolerance for fluctuations in market value of the total investment fund, can match that of the global stock market. This should protect the beneficiaries from any undue risk while capturing the desired return potential from the preferred asset mix.

The asset mix policy ranges and the average long-term weights for the major asset classes are listed on Page 36. The investment staff has the authority to operate within the policy ranges for each asset class. The average long-term weights were derived from the 2000 Asset Allocation Report, discussions with the board's consultants and staff input, and are based on each asset's long-term (five- to 10-year) expected rate of return and volatility.

It is expected that in each year's Annual Investment Plan, the board will adopt a current strategy which may deviate from the average long-term weights shown here based upon short- and intermediate-term expected returns of each asset.

Objectives, Guidelines and Policies: Fixed Income

Objectives

It is the board's policy to invest in fixed-income investments to diversify the investment portfolio. A total return objective of 6–7% per year over a five-year period is expected on these assets. Total returns in

excess of the Lehman Brothers Universal Bond Index is the fixed income relative objective.

Restrictions

It is the board's policy to maintain a normal invested position of 23% of total fund assets with a range of 13–28%. External management of fixed-income assets may be utilized. The staff will select and the board, through its consultant, will monitor performance of all outside money management firms used for fixed-income investments. Internally managed fixed-income assets will be U.S. dollar-denominated debt obligations. For externally managed portfolios, non-U.S. dollar-denominated debt securities may be purchased and currencies will be hedged at the discretion of the manager. The portfolio will seek diversification by market sector, quality and issuer. Emerging market and high-yield debt combined will be within 50% and 175% of the Lehman Brothers Universal Bond Index weights. The maximum investment in the securities of any one issuer shall not exceed 3% of the fixed-income portfolio at the time of purchase with the exception of U.S. Government and related agency securities. The portfolio will have a duration level between 80% and 120% of the index. Portfolio turnover will be moderate and a function of relative value changes of the securities comprising the portfolio. Directly negotiated private placements by staff are prohibited investments.

Derivatives may be used in management of both the internal and external fixed-income portfolios as long as the underlying security is suitable for the portfolios. The use of leverage to enhance portfolio returns is pro-

hibited. A mortgage that has an expected negative duration is also prohibited. Derivatives may be used to adjust the exposure to interest rates, individual securities or to various market sectors in the portfolio. All strategies must be of a hedging or positioning nature rather than speculative. Underlying exposure of derivatives for internally managed fixed-income investments will not exceed 5% of total fund assets.

Objectives, Guidelines and Policies: Liquidity Reserves

Objectives

It is the board's policy to hold liquidity reserves to fund the normal business needs of STRS Ohio. The portfolio seeks to preserve principal value and maintain a high degree of liquidity. The return objective of the portfolio is to exceed the return of a 90-day U.S. Treasury bill.

Restrictions

It is the board's policy to maintain a normal invested position of 1% of total fund assets with a range of 0–4%. Liquidity reserves will be a portfolio of high quality short-term securities generally of A1/P1 quality. To preserve the principal value of the portfolio, interest rate risk will be low. The portfolio will consist of large marketable issuers in the short-term markets to provide the necessary liquidity.

Investments

Objectives, Guidelines and Policies: Domestic Equities

Objectives

For the domestic equity sector of the portfolio, a total return objective of 8–10%, averaged over a period of five years, is desired. Should the investment advisor believe attainment of this objective at any time is not possible without undue risk, it is the advisor's responsibility to recommend to the board a revised figure. The equity portfolio should reduce nonmarket risk by being diversified.

Restrictions

It is the board's policy to maintain an investment in domestic equities in the range of 43–50% of assets. The amount invested at any time is determined by the long-term objectives established by the board in conjunction with the investment advisor/consultant and by the Annual Investment Plan and its periodic modifications.

No more than 6% of assets of the system invested in the equity sector may be invested in equities of any one corporation. The board shall not generally take a position constituting more than 5% of the outstanding equity of a corporation (except investments approved under the "Alternative Investments" section).

All American depository receipts and foreign stocks listed on a domestic stock exchange are eligible for purchase under this section.

Derivatives may be used in management of the equity portfolio. The use of leverage to

enhance a derivative's effect is prohibited. Derivatives are typically, but not exclusively, options, futures and options on futures for market indices such as the S&P 500, S&P 400, S&P 100 and the S&P 600 index. Options on individual stocks, stock baskets and unleveraged equity-linked notes are further examples. Strategies permitted must be of a hedging or positioning nature rather than speculative. Underlying exposure of equity derivatives cannot exceed 10% of total STRS Ohio assets.

Quality Standards and Portfolio Construction

Domestic equity portfolios are normally invested in securities selected from a universe of more than 6,000 publicly traded issues. The investment style of individual portfolios follows STRS Ohio guidelines, as described in the Annual Investment Plan, and are monitored based on appropriate portfolio characteristics and risk levels. Stocks are selected for each portfolio based on a set of criteria appropriate for each style. The board's investment advisor/consultant must review each equity portfolio to measure the degree of compliance with STRS Ohio established parameters and risk levels. The investment advisor/consultant must report the results to the board at least annually.

Portfolio Allocation

The allocations across the various domestic stock portfolios will be tied to the weights of the respective sectors in the S&P 1500 for the following sectors: growth versus value, and large, mid and small capitalization. Since

Twila diligently checks the accuracy of reports submitted by employers — which document their contributions to STRS Ohio member accounts — and expedites the resolution of any discrepancies.

these sector weights shift over time, the portfolio rebalancing will be a dynamic and ongoing process. At least quarterly, allocations will be reviewed and adjusted so that no sector is less than 75% nor more than 125% of the respective index weight.

External Managers

The staff will select and the board, through its consultant, will monitor the performance of all external money managers used to provide supplemental active management.



Objectives, Guidelines and Policies: International

Objectives

It is the board's policy to invest in international investments in order to diversify the investment portfolio. A total return objective of 8–10% per year over a five-year period is expected on these assets. The primary emphasis will be on international equity securities, but some international debt instruments may also be included.

Restrictions

It is the board's policy to maintain an exposure in international investments in the range of 15–25%. The staff will select and the board, through its consultant, will monitor performance of all outside money management firms used for international investments. Internal management of international assets will also be utilized. International assets will be a diversified portfolio including both developed and emerging countries. The targeted normal weighting of international investments will be comprised of 15% developed countries and 5% emerging countries. The staff may deviate from this weighting by plus or minus 2% on

the emerging market weighting and plus or minus 3% on the developed market weighting. The neutral position for currencies will be 50% hedged for the developed markets. Currencies will be hedged at the discretion of the manager. For the internally managed portfolio, currency will not be a primary investment tool and will be used for non-speculative purposes.

Derivatives may be used in management of both the internal and external international portfolios as long as the underlying security is suitable for the portfolios. The use of leverage to enhance a derivative's effect is prohibited. Derivatives may be used to adjust the exposure to countries or markets, to individual securities or to currencies in the portfolios. All strategies must be of a hedging or positioning nature rather than speculative. Underlying exposure of derivatives for international investments will not exceed 10% of total STRS Ohio assets.

Objectives, Guidelines and Policies: Alternative Investments

Objectives

The chief objective of the alternative investment program is to provide an attractive risk-adjusted rate of return to benefit the STRS Ohio membership. Most alternative investment options inherently possess a long-term investment horizon, illiquidity and a high standard deviation (volatility in the timing of returns). For these reasons, expected financial returns exceed those of other asset classes. Alternative asset returns are expected to be approximately 15% annualized over the life of the asset pool.

Investments

Restrictions

Total value of alternative assets invested will not normally exceed 3% of total assets.

Timber and farmland, often classified as alternative assets, are considered by the board as real estate for this policy statement and are managed under the real estate section of this statement.

Potential alternative investments will be analyzed for possible STRS Ohio investment.

In addition to meeting the legal requirements, underwriting criteria include: experienced general partners, solid track record and appropriate partnership terms. The Annual Investment Plan will set forth strategies, desirable types and specific current goals for alternative assets.

The executive director shall report any investment under consideration pursuant to this section to the Investment Committee prior to making any legally binding commitment to such investment.

The deputy executive director — Investments will inform the board of an individual

to serve on a company board and to face election by shareholders of that company. If the named individual is an STRS Ohio associate, that individual must sign a letter of agreement with the State Teachers Retirement Board indicating that, should the staff member terminate employment at STRS Ohio, resignation from any and all company board seats would occur if the State Teachers Retirement Board so directs. The STRS Ohio associate can be reimbursed for actual expenses incurred in serving on a board of directors, but no director's fees will be accepted.

Objectives, Guidelines and Policies: Real Estate

Objectives

It is the board's policy to invest in real estate in order to diversify and reduce the volatility of the overall investment portfolio. Consequently, real estate investments will be

acquired to provide a return commensurate with investment risk. Income yields shall be a key objective of the portfolio with long-term appreciation also a factor in real estate selection. A total return objective of 8–9% per year over a five-year period is expected for the portfolio.

Guidelines

It is the board's policy to maintain an investment in real estate in the range of 6–12% of total assets, diversified within the following guidelines:

1. **Property Type:** The value for any one property type shall generally not exceed 50% of real estate assets. However, the specialty type shall not exceed 25% of real estate assets. Five such types are:
 - a. Office buildings;
 - b. Retail properties;
 - c. Distribution centers, warehouses and industrial parks;



In addition to helping members pay for service credit purchases, Jama often works with the Ohio Attorney General's office to resolve outstanding payments due to STRS Ohio.

- d. Multifamily housing; and
 - e. Specialty, including but not limited to, timberland, farmland, senior living and hotels.
2. **Geographical Concentration:** The maximum value for any one of the four regions as defined by the National Council of Real Estate Investment Fiduciaries (NCREIF) will generally be 50% of real estate assets. Investments in international real estate will be limited to 10% of real estate assets. When properties located within Ohio offer quality, return and safety comparable to properties outside Ohio, the Ohio investment will be given preference.
 3. **Investment Structure:** Equity-oriented ownership structures will be used such as direct ownership, participating or convertible mortgages, joint ventures, externally managed accounts, real estate securities and derivatives. Publicly traded real estate securities will be limited to 25% of real estate assets. Derivatives may be used in the management of the real estate portfolio. All derivative strategies must be of a hedging or positioning nature rather than speculative. Underlying exposure of real estate derivatives must not exceed 1% of total assets. The staff will search for innovative structures for real estate investments to enhance STRS Ohio's total investment strength. To manage the overall volatility of the real estate portfolio, the amount of leverage on the portfolio will generally be limited to 35% of real estate assets.
 4. **Investment Size Guidelines:** The minimum size for individual real estate properties will be generally: \$10 million

for properties within Ohio and \$15 million for properties outside Ohio. Exceptions to this guideline are appropriate in areas where STRS Ohio has an existing concentration of real estate assets or is actively building a concentration. The maximum investment amount for an individual property will be limited to approximately 1% of total assets.

5. **Investment Style:** The real estate portfolio will contain individual real estate investments along the risk/return continuum. However, the portfolio will generally limit "non-core" (i.e., relative higher risk) real estate investments to 30% of real estate assets.

Procedures

Due Diligence

The real estate investment management process will be subject to a number of procedures to safeguard STRS Ohio assets. New investments will have the following documentation:

1. A building and systems evaluation by a qualified engineering firm in the case of an existing building.
2. A review of plans, specifications and construction progress by a qualified architectural firm in the case of developmental properties.
3. An environmental review by a qualified consultant in accordance with the Environmental Policy described below.
4. A financial analysis including, but not limited to, holding period, internal rate of return, initial yield and sensitivity to critical assumptions.

5. Legal review and approval of appropriate documents.

Environmental Policy

Real estate investments will be subject to the requirements of an Environmental Policy addressing hazardous materials, wetlands, endangered species and other environmental issues affecting real property. The policy shall be reviewed by the board's real estate consultant for comparability to other institutional investor practices. The policy will ensure that STRS Ohio will be prudent and diligent in its evaluation of potential real estate investments having environmental issues. STRS Ohio will not make any real estate investment having environmental issues that, in all reasonable likelihood, would subject STRS Ohio to a material liability or would have a materially adverse impact on the value of the real estate investment that has not been taken into account in the underwriting decision, including without limitation, a prudent plan for diligently handling such environmental issues.

Valuations

A combination of internal valuations and external appraisals will be used on a rotating basis for valuing the internally managed assets (except the sale-leaseback portfolio will be valued on an internal basis only). Each property will be valued annually, with an independent external appraisal no less than every third year. Additionally, a sample of internally valued properties will have external appraisals each year to validate the internal results. At acquisition, each property will have an external appraisal, although carried at the purchase price for the first

Investments

year. Externally managed investments are valued and reported to STRS Ohio by the external manager. The methodology used for internal valuations shall be reviewed by the board's real estate consultant in conjunction with the operational audit.

Performance

Real estate investment performance will be reported to the board on a quarterly basis. The real estate portfolio shall have as its benchmark, a composite index consisting of 80% of the NCREIF Property Index, 10% of the NCREIF Timberland Index and 10% of the NAREIT Equity Index (effective Jan. 1, 2001).

Board Consultant

The role of the real estate consultant is specifically outlined in the contract scope of services. The scope of services includes, but is not limited to, the following:

1. Report to the board on a semiannual basis regarding the investment performance of the system's real estate portfolio.
2. Review and comment on the real estate strategy as presented in the Annual Investment Plan and any revisions to the plan recommended during the year. Review and comment on the five-year real estate strategy prepared by staff.
3. Review triennially, the general internal management of real estate and its efficiency, with the objective of completing an overall operational audit.
4. Review certain predefined property-specific transactions.

Real Estate Investment Committee (REIC)

A committee composed of a combination of internal staff and external industry professionals will review proposed transactions for recommendation to the deputy executive director — Investments and the executive director. Transactions to be reviewed by the REIC include new acquisitions, dispositions and significant modifications in existing deal structures. The following transactions will not be subject to REIC review for recommendation to the executive director:

1. Ancillary purchases, sales, exchanges and capitalized expenditures which are valued at less than 20% of the total property value;
2. Public real estate securities;
3. Actions allowed under existing investment documents (e.g., conversion options, loan prepayments, buy-sell agreements, etc.);
4. Sales of individual sale-leaseback properties, or properties that have a market value of \$5 million or less at the time of disposition recommendation;
5. Temporary mortgage restructurings, which limit the restructuring to no more than four years and revert back to original terms;
6. Settlement of actual or potential real estate litigation;
7. Investment in international real estate funds and securities;
8. Investment in externally managed accounts such as timber, agriculture and "opportunity" funds.

Board Review

The board adopts policy and monitors performance with the assistance of the real estate consultant. These responsibilities include review of the:

1. Investment Objective and Policy;
2. Long-term real estate strategy;
3. Annual Investment Plan;
4. Individual transactions outside policy and/or strategy;
5. Monthly Investment Activity Reports; and
6. Semiannual performance reports from the consultant.

Objectives, Guidelines and Policies: Procedures

Long-Term Objectives

The investment advisor shall recommend long-term objectives for the total plan and for each segment of the portfolio. These long-term objectives, many of which are incorporated into this policy, shall be reviewed by the Investment Committee and/or the board at least annually. The objectives for staff-managed domestic portfolios of financial assets shall incorporate statements of investment criteria for both publicly traded bonds and stocks, as recommended by the investment advisor/consultant and approved by the board.

As an investments securities analyst at STRS Ohio, George's work directly contributes to preserving and increasing the capital base from which STRS Ohio's members receive their retirement benefits.



Investments

Annual Investment Plan

By January of each calendar year, or at such other time as the board may designate, an Annual Investment Plan shall be proposed to the Investment Committee. This proposed plan shall be based upon recommendations of the Investment Department and the investment consultants, with approval of the executive director. The Annual Investment Plan shall be based upon:

1. The long-term objectives and normal asset weights set by the board.
2. General economic outlook for the short and long term.
3. Expected relative outlook for asset types.
4. Short- and long-term interest rates.
5. Such other factors as seem indicated.

The Annual Investment Plan will serve as a guide for the investment staff in its day-to-day operation. Any changes proposed to the plan are to be presented to and accepted by the board before adoption.

The plan as modified will become the operational plan for the investment staff until subsequent modification.

Reporting

The Investment Committee shall be furnished with the following:

Monthly



Jenny works in STRS Ohio's Member Services Center, answering members' questions about a wide range of benefits. She enjoys "making life easier" for members.

1. Monthly Activity Report that includes:
 - a. Domestic Equities
 - (1) Summary of the equity markets
 - (2) Domestic equity performance comparisons
 - (3) Top 20 holdings
 - (4) Portfolio diversification — past, present and planned
 - (5) Status of special projects
 - b. International
 - c. Fixed Income
 - (1) Summary of fixed-income markets
 - (2) Summary of trading markets
 - d. Real Estate
 - e. Cash Flow
 - f. Performance
2. Portfolio Summary, classified by asset type, at market and as percentages of the total.
3. Investment purchases and sales since the last report.

Bimonthly

Appropriate commentary and reports on the progress with the Annual Investment Plan.

Semiannually

All exposure in derivatives for all asset classes.

Proxy Voting

The State Teachers Retirement Board believes that common stock proxies are valuable and should be voted in the best interest of the members and retirees. To this end, the Retirement Board shall maintain stock proxy voting policies and the staff and all outside managers will use them as guides in meeting the fiduciary responsibility of the State Teachers Retirement Board in voting common stock proxies. Common stock proxies may be executed by the executive director, the deputy executive director — Administration, the deputy executive director — Investments or outside money managers.

Ohio Investments

It is the policy of the board to give consideration to investments that enhance the general welfare of the state and its citizens, provided the funds are invested solely in the interest of participants and beneficiaries. This goal will be pursued to the greatest extent possible within the limits of fiduciary responsibility. Preference will be given to Ohio investments offering competitive returns at risk levels comparable to similar investments currently available to the board. To meet this objective an Ohio Investment

Plan, incorporating all provisions of the STRS Ohio Investment Objective and Policy Statement, shall be maintained and implemented by the investment staff. This plan shall set forth procedures to assure that a special effort will be made by the investment staff to examine and evaluate all legal investment opportunities in the state and, where policy objectives are met, to acquire such investments.

Broker-Dealers

Purchases and sales of publicly traded securities shall be executed with broker-dealers from a list reviewed by the Investment Committee. The list shall be limited, as practicable, to 65 firms plus those in the Ohio and emerging firms sublist. Selection shall be based on an evaluation by the investment staff as to financial soundness, underwriting capabilities, research services, execution capabilities and other factors required by the staff to fulfill its assigned investment responsibilities. Specific transactions will be directed to the broker on that list most capable of providing brokerage services necessary to obtain both the best available price and the most favorable execution.

The board shall give equal consideration to minority-owned and controlled firms and to firms owned and controlled by women. The board shall be proactive in its intent to include: firms that have an operating office located in Ohio; minority-owned and controlled firms; and firms owned and controlled by women.

Each firm listed shall file with the State Teachers Retirement Board on an annual basis such evidence of financial responsi-

bility as required by the board. This information shall include, but not be limited to, an audited financial statement.

When stocks are purchased during an underwriting, allocations may be made to dealers not on the approved list provided the managing underwriter is so listed. Bond purchases may be made either at underwriting or in the secondary market from any firm holding membership in the National Association of Securities Dealers.

When entering into real estate transactions, the board shall give equal consideration to Ohio firms providing associated professional services, minority-owned and controlled firms, and firms owned and controlled by women.

Securities Lending

The board may operate a securities lending program to enhance the income of the fund. The program must be operated by a bank trustee who follows the custodial requirements of the Treasurer of State and each security lent must be fully collateralized. Results of the program must be reported to the board annually.

Measurement

The primary goal of the fund shall be to achieve the absolute return targets described in the "Total Fund" section of this policy. However, a secondary measurement objective of the board is to relate the fund's performance to various indices. The relative measurement of the total fund shall be made against a hybrid index consisting of weightings from liquidity reserves, equity, fixed-income, real estate and international

Investments

indices.

Relative measurement of performance shall be made on a quarterly and annual basis. The primary time period for such comparisons shall be three years, although one-, five- and 10-year comparisons shall also be examined.

The benchmark against which investment return of the publicly traded bond sector will be measured is the Lehman Universal Bond Index and the GDP Deflator. The primary time period for such comparisons shall be three years, although one-, five- and 10-year comparisons shall also be examined.

The domestic equity portfolio shall be compared against the Standard & Poor's 1500 Average. The board's objective is to match or exceed performance of the yardsticks, subject to the volatility level expressed in the "Total Fund" section of this policy. The primary time period for such comparisons shall be three years, although one-, five- and 10-year comparisons shall also be examined.

The real estate portfolio shall have as its benchmark a composite index consisting of 80% of the NCREIF Property Index, 10% of the NCREIF Timberland Index and 10% of the NAREIT Equity Index. The primary time period for such comparisons shall be three years, although one-, five- and 10-year comparisons shall also be examined.

The international equity portfolio shall have as its benchmark a composite index, consisting of 75% of the Morgan Stanley's Capital International Europe, Australasia, Far East Index (EAFE) 50% hedged and 25% of the Morgan Stanley Emerging Markets Free Index. The board's objective is to match or

exceed performance of this composite index. The primary time period for such comparisons shall be three years, although one-, five- and 10-year comparisons shall also be examined.


In addition, the board and its investment advisors/consultants will maintain a performance monitoring system for individual asset categories and total fund.



Security Valuation

Valuation of investments shall be the total of:

1. The primary closing price on the principal registered stock exchange for all common and preferred stocks so listed.
2. The last sale as reflected by NASDAQ for common and preferred stocks not listed on a registered stock exchange.
3. The current value as determined by a qualified independent service for all bonds, notes and certificates of indebtedness.
4. Amortized cost for commercial paper, certificates of deposit, repurchase agreements and other short-term investments with a maturity of 270 or fewer days.
5. Real estate valued through a combination of independent appraisals and in-house valuations. Methodology underlying internal valuations will be reviewed by the real estate consultant. REIT shares are valued at primary closing prices on the principal registered stock exchange.
6. The most recent valuation for venture capital and alternative investments.
7. International investments valued by the subcustodian using relevant closing market prices and exchange rates.



Steven monitors and evaluates the performance of STRS Ohio's prescription drug and health care program providers, and resolves issues on behalf of our benefit recipients.

Investments

Investment Performance (total returns, annualized on a calendar basis)

1-Year Returns (2000)			
Asset Category	STRS Ohio Return	Index Name	Index Return
Domestic Stocks	(6.27%)	Standard & Poor's (S&P) 1500*	(6.98%)
International	(16.17%)	EAFE/Emerging Composite	(15.69%)
Fixed Income	12.53%	Lehman Universal**	11.09%
Real Estate	15.43%	Real Estate Composite***	12.43%
Total Fund	(2.43%)	S&P/Lehman/RE/International Inflation (GDP Deflator)	(2.60%) 2.43%
3-Year Returns (1998–2000)			
Asset Category	STRS Ohio Return	Index Name	Index Return
Domestic Stocks	10.31%	Standard & Poor's (S&P) 1500*	12.23%
International	7.78%	EAFE/Emerging Composite	5.76%
Fixed Income	6.62%	Lehman Universal**	6.19%
Real Estate	13.07%	Real Estate Composite***	11.14%
Total Fund	9.44%	S&P/Lehman/RE/International Inflation (GDP Deflator)	9.77% 1.69%
5-Year Returns (1996–2000)			
Asset Category	STRS Ohio Return	Index Name	Index Return
Domestic Stocks	15.43%	Standard & Poor's (S&P) 1500*	18.31%
International	5.92%	EAFE/Emerging Composite	3.91%
Fixed Income	6.86%	Lehman Universal**	6.35%
Real Estate	12.82%	Real Estate Composite***	11.83%
Total Fund	10.97%	S&P/Lehman/RE/International Inflation (GDP Deflator)	11.78% 1.76%

STRS Ohio Long-Term Policy Objective (5 Years)

Equities: 8%–10%

Fixed Income: 6%–7%

Real Estate: 8%–9%

Total Fund: 8%

* The domestic stocks benchmark is calculated using the S&P 1500 Index for all periods beginning on or after Jan. 1, 1998, and using the S&P 500 Index for all periods before Jan. 1, 1998.

** The fixed-income benchmark is calculated using the Lehman Universal Index for all periods beginning on or after Oct. 1, 2000, and using the Lehman Aggregate Index for all periods before Oct. 1, 2000.

*** The Real Estate Composite benchmark is calculated using the STRS Ohio Composite Index for all periods beginning on or after Jan. 1, 1996, and using only the NCREIF Property Index for all periods before Jan. 1, 1996.

State Teachers Retirement System of Ohio is defined and created by the Ohio Revised Code, Chapter 3307.15. The STRS Ohio Total Fund performance results consist of all assets of the fund, including both internally and externally managed accounts. All results are expressed in U.S. dollars and net of brokerage commissions, expenses related to trading, and applicable foreign withholding taxes on dividends, interest and capital gains. Performance results are generally gross of fees. Net of fees results are available upon request. Investment management fees vary among asset class. Dispersion data is not applicable. STRS Ohio has prepared and presented this report in accordance with the Performance Presentation Standards of the Association for Investment Management and Research (AIMR-PPS), the U.S. and Canadian version of the Global Investment Management Performance Standards (GIPS). AIMR has not been involved in the preparation or review of this report.

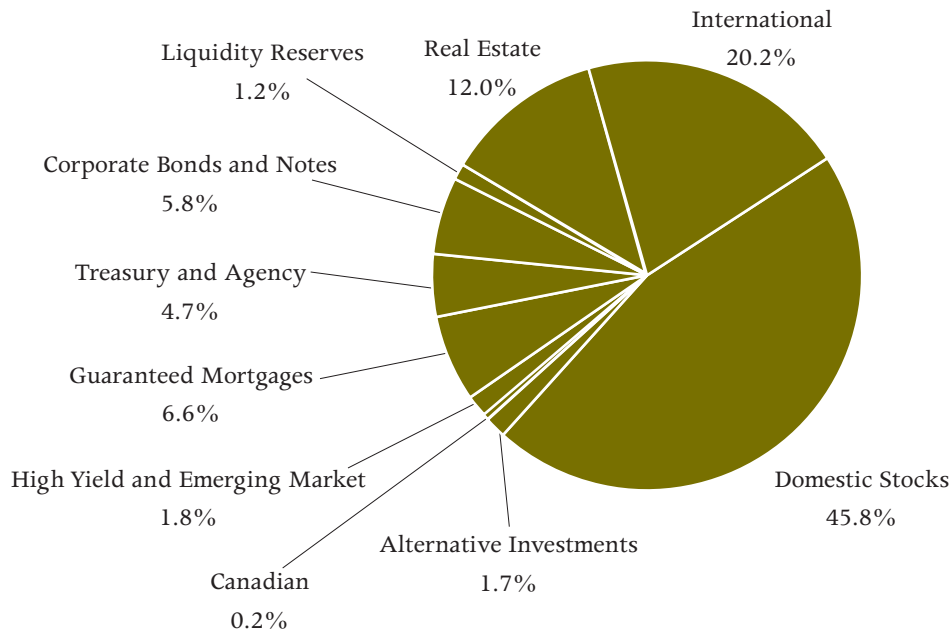
Summary of Investment Assets				
As of June 30, 2001 and 2000 (dollar amounts in thousands)				
	June 30, 2001 Fair Value	%	June 30, 2000 Fair Value	%
Short term				
Commercial paper	\$ 608,286	1.2%	\$ 730,163	1.3%
Government notes	10,000	0.0%	10,000	0.0%
Corporate notes		0.0%		0.0%
Short-term investment funds	5,000	0.0%	4,000	0.0%
Total short term	623,286	1.2%	744,163	1.3%
Fixed income				
Guaranteed mortgages	3,457,429	6.6%	4,078,061	7.1%
U.S. government and governmental agencies	2,492,022	4.7%	4,059,652	7.0%
Corporate bonds	3,086,300	5.8%	3,046,803	5.3%
Canadian bonds	110,632	0.2%	116,559	0.2%
Municipal bonds		0.0%	293	0.0%
High yield and emerging markets	940,562	1.8%		0.0%
Total fixed income	10,086,945	19.1%	11,301,368	19.6%
Common and preferred stock	24,174,337	45.8%	26,708,135	46.4%
Real estate				
East region	1,260,205	2.4%	1,118,422	1.9%
Midwest region	939,894	1.8%	1,006,963	1.8%
South region	927,093	1.8%	931,457	1.6%
West region	1,602,373	3.0%	1,407,536	2.4%
REITs	636,360	1.2%	492,718	0.9%
Other	969,194	1.8%	896,546	1.6%
Total real estate	6,335,119	12.0%	5,853,642	10.2%
Alternative investments	923,253	1.7%	747,525	1.3%
International	10,667,911	20.2%	12,171,055	21.2%
Total investments	\$ 52,810,851	100.0%	\$ 57,525,888	100.0%

Investment asset schedule excludes invested securities lending collateral.

For purposes of this schedule, certain U.S.-based short-term and fixed-income securities have been classified as international investments in order to approximate the investment exposure of international equity swaps.

Investments

Investment Distribution by Fair Value — as of June 30, 2001



STRS Ohio continues to engage in quality Ohio investments. As of June 30, 2001, STRS Ohio investments in companies with headquarters in Ohio are valued at more than \$1.7 billion.

Ohio Investment Profile

as of June 30, 2001 (in thousands)

Liquidity reserves	\$ 44,985
Fixed income	132,322
Common stock	750,635
Alternative investments	147,310
Real estate	630,600
Total Ohio-headquartered investments	\$ 1,705,852

Schedule of Largest Investment Holdings* (As of June 30, 2001)

Common Stocks — Top 20 Holdings		
	Shares	Fair Value
General Electric Co.	18,579,674	\$ 905,759,108
Microsoft Corp.	10,748,728	\$ 784,657,144
Exxon Mobil Corporation	6,773,388	\$ 591,655,442
Citigroup Inc.	10,227,089	\$ 540,399,383
Pfizer Inc.	12,801,577	\$ 512,703,159
AOL Time Warner Inc.	8,673,995	\$ 459,721,735
Wal-Mart Stores Inc.	8,755,778	\$ 427,281,966
American International Group	4,558,258	\$ 392,010,188
International Business Machines Corp.	3,415,134	\$ 385,910,142
Intel Corp.	12,971,653	\$ 379,420,850
Verizon Communications	5,449,120	\$ 291,527,920
Merck & Co., Inc.	4,415,663	\$ 282,205,022
Johnson & Johnson	5,632,220	\$ 281,610,995
Cisco Systems	14,672,773	\$ 267,044,469
SBC Communications Inc.	6,482,017	\$ 259,669,601
Philip Morris Co.	5,012,440	\$ 254,381,330
Royal Dutch Petroleum	4,175,685	\$ 243,317,165
Coca-Cola Co.	4,916,515	\$ 221,243,175
Home Depot Inc.	4,598,936	\$ 214,080,471
Oracle Systems Corp.	11,166,926	\$ 212,171,594

* A complete list of investment holdings is available from STRS Ohio.

Schedule of Largest Investment Holdings (continued)

International Investments — Top 20 Holdings		
	Shares	Fair Value
Royal Dutch Petroleum (Netherlands)	1,902,547	\$ 109,522,521
GlaxoSmithKline (United Kingdom)	3,430,987	\$ 96,511,589
BP AMOCO Capital (United Kingdom)	11,668,688	\$ 95,926,134
Total Fina (France)	611,894	\$ 85,703,504
Novartis AG (Switzerland)	2,291,280	\$ 82,951,783
Honda Motor Co. (Japan)	1,594,000	\$ 70,049,078
Telefonos Mexico (Mexico)	1,855,800	\$ 65,120,022
Canon Inc. (Japan)	1,463,000	\$ 59,130,072
AstraZeneca (United Kingdom)	1,248,552	\$ 58,177,957
Aventis (France)	716,201	\$ 57,191,764
Samsung Electronics (South Korea)	368,216	\$ 54,466,465
Taiwan Semiconduct (Taiwan)	27,454,044	\$ 51,107,005
UBS AG (Switzerland)	350,860	\$ 50,281,862
Nomura Securities (Japan)	2,539,000	\$ 48,662,470
Vodafone Group (United Kingdom)	21,689,341	\$ 48,046,009
China Mobile Ltd. (Hong Kong)	9,068,184	\$ 47,901,684
Sanofi-Synthelab (France)	726,012	\$ 47,646,651
ING Group (Netherlands)	703,771	\$ 46,008,232
BHP Limited (Australia)	8,216,223	\$ 43,383,929
Elan Corporation, ADR (Ireland)	682,000	\$ 41,602,000

Fixed Income — Top 20 Holdings		
	Par Value	Fair Value
U.S. Treasury, 8.875%, due 02/15/2019, AAA+	\$ 151,800,000	\$ 206,287,478
U.S. Treasury, 8.75%, due 08/15/2020, AAA+	\$ 136,960,000	\$ 185,809,924
U.S. Treasury, 8.75%, due 05/15/2017, AAA+	\$ 131,774,000	\$ 172,509,991
U.S. Treasury, 10.375%, due 11/15/2009, AAA+	\$ 111,230,000	\$ 131,338,235
U.S. Treasury, 5.75%, due 11/15/2005, AAA+	\$ 117,000,000	\$ 121,341,139
U.S. Treasury, 7.25%, due 08/15/2022, AAA+	\$ 89,555,000	\$ 106,303,358
U.S. Treasury, 12.00%, due 08/15/2013, AAA+	\$ 70,000,000	\$ 100,061,701
U.S. Treasury, 6.25%, due 02/15/2003, AAA+	\$ 58,400,000	\$ 61,627,807
U.S. Treasury, 5.75%, due 10/31/2002, AAA+	\$ 59,630,000	\$ 61,495,077
U.S. Treasury, 6.875%, due 05/15/2006, AAA+	\$ 53,920,000	\$ 58,621,855
U.S. Treasury, 6.125%, due 08/15/2007, AAA+	\$ 54,648,000	\$ 58,582,167
FHLMC Gold, 6.50%, due 07/01/2029, AAA+	\$ 58,284,354	\$ 57,937,951
Wal Mart, 6.875%, due 08/10/2009, AA2	\$ 53,325,000	\$ 56,786,703
U.S. Treasury, 6.625%, due 05/15/2007, AAA+	\$ 52,000,000	\$ 56,271,346
FNMA Benchmark, 6.25%, due 05/15/2029, AAA+	\$ 58,000,000	\$ 55,908,874
U.S. Treasury, 6.50%, due 02/15/2010, AAA+	\$ 50,350,000	\$ 55,311,987
Asian Development, 7.50%, due 05/31/2005, AAA	\$ 50,000,000	\$ 53,858,417
Deutsche Aus, 7.00%, due 06/23/2005, AAA	\$ 50,000,000	\$ 52,857,778
FNMA Benchmark, 5.25%, due 01/15/2009, AAA+	\$ 53,000,000	\$ 51,841,862
FHLMC Gold, 6.50%, due 03/01/2029, AAA+	\$ 51,484,340	\$ 51,178,352



Terry manages a forecasting model that helps STRS Ohio monitor the financial status of its health care program.



Connie quickly responds to members' requests to update tax and benefit payment information — her goal is to provide same-day service.

November 2, 2001

The Retirement Board
State Teachers Retirement System of Ohio
275 East Broad Street
Columbus, Ohio 43215

Ladies and Gentlemen:

This report presents the results of the annual actuarial valuation of the assets and liabilities of the State Teachers Retirement System of Ohio (STRS Ohio) as of July 1, 2001, prepared in accordance with Section 3307.51 of Chapter 3307 of the Ohio Revised Code. The valuation takes into account all of the promised benefits to which members are entitled, including pension and survivor benefits.

The valuation was based on the actuarial assumptions and methods as adopted by the Board of Trustees, including a valuation interest rate of 7 3/4 % per annum compounded annually. The assumptions and methods are unchanged from the prior valuation.

The actuarial assumptions and methods comply with the parameters set forth in Governmental Accounting Standards No. 25.

Assets and Membership Data

STRS Ohio reported the individual data for members of the System as of the valuation date to the actuary. While we did not verify the data at their source, we did perform tests for internal consistency and reasonableness. The amount of assets in the trust fund taken into account in the valuation was based on statements prepared for us by STRS Ohio.

Funding Adequacy

The total contribution rate from employers and members is 23.3%. The Board allocates this contribution between pension and survivor benefits and health care. For fiscal 2001 and after, the Board has allocated 4.5% toward health care, leaving 18.8% for pension and survivor benefits. The valuation indicates that a contribution rate of 18.8% is sufficient to provide for the payment of the promised pension and survivor benefits, with a 27.5-year funding period to amortize the unfunded accrued liability. The funding period has increased 4.4 years from last year's funding period (i.e., increased from 23.1 years to 27.5 years). The funding period increased because of the actuarial and investment losses.

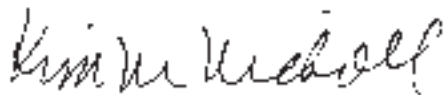
The valuation indicates that for the fiscal year ending June 30, 2001, the actuarial experience of STRS Ohio was unfavorable and generated net actuarial losses of \$716 million. This loss includes a loss of \$65 million due to the decrease in the employer contribution rate on payroll for alternative retirement plan members and a loss of \$5 million for the elimination of state reimbursement for prior ad hoc cost-of-living increases under House Bills 204 and 284.

Financial Results and Membership Data

Detailed summaries of the financial results of the valuation and membership data used in preparing the valuation are shown in the valuation report. The actuary prepared supporting schedules included in the Actuarial and Statistical Sections of the STRS Ohio Comprehensive Annual Financial Report. The actuary prepared the trend data schedules included in the Financial Section of the STRS Ohio Comprehensive Annual Financial Report.

Qualified actuaries completed the valuations in accordance with accepted actuarial procedures as prescribed by the Actuarial Standards Board. The qualified actuaries are members of the American Academy of Actuaries and are experienced in performing actuarial valuations of public employee retirement systems. To the best of our knowledge, this report is complete and accurate and has been prepared in accordance with generally accepted actuarial principles and practice.

Respectfully submitted,



Kim M. Nicholl, F.S.A.
Consulting Actuary

Actuarial



Sean leads a team of associates who assist in benefits processing. Their diligence ensures that retirees receive their benefit payments on time.

Statement of Actuarial Assumptions and Methods

The assumptions below have been adopted by the State Teachers Retirement Board after consulting with the actuary.

Financing Objective: To establish contributions as a level percentage of active member payroll which, when invested, will be sufficient to provide specified benefits to STRS Ohio members and retirees.

Interest Rate: 7.75% per annum, compounded annually. (Adopted 2000)

Death After Retirement: According to the 1983 Group Annuity Mortality Table (Projection 1994 –Scale H), with one-year setback in age for males and one-year set forward in age for females. Special mortality tables are used for the period after disability retirement. (Adopted 1998)

Future Expenses: The assumed interest rate is net of the anticipated future administrative expenses of the fund.

Actuarial Cost Method: Projected benefit method with level percentage entry age normal cost and open-end unfunded accrued liability. Gains and losses are reflected in the accrued liability.

Asset Valuation Method: A four-year moving market average value of assets that spreads the difference between the actual investment income and the expected income (based on the valuation interest rate) over a period of four years. The actuarial value shall not be less than 91% or more than 109% of market value. (Adopted 1997)

Payroll Growth: 4.5% per annum compounded annually. Included in the total payroll growth assumption is a 3.50% increase as a result of inflation. (Adopted 1998)

Separations From Active Service: Representative values of the assumed rates of separation and annual rates of salary increase are shown in the table below. (Adopted 1993)

Replacement of Retiring Members: The majority of members who retire do so effective July 1. These members are replaced by new members who are hired after July 1. As a result, new members are not reported on the census data. To compensate for this, assumed payroll for these new members is equal to the difference between actual total system payroll for the fiscal year just ended and reported payroll for members reported on the valuation date.

Census and Assets: The valuation was based on members of the system as of July 1, 2001, and does not take into account future members. All census and asset data was supplied by the system.

Superannuation								
Age	Non-Vested Withdrawal	Vested Withdrawal	Death	Disability	30 Years Service Retirement	25–29 Years Service Retirement	Under 25 Years Service Retirement	Salary Increase*
MEN								
20	.1900	.0900	.0003	—	—	—	—	.0925
30	.1500	.0400	.0005	.0004	—	—	—	.0725
40	.1375	.0175	.0008	.0018	.2800	—	—	.0525
50	.1340	.0085	.0023	.0049	.2800	—	—	.0405
55	.1340	.0085	.0039	.0062	.3100	.0600	—	.0375
60	.1340	.0085	.0061	.0068	.3600	.0600	.1300	.0350
65	.1340	.0085	.0094	.0072	.5200	.1800	.2200	.0325
70	.1340	—	.0168	.0072	.4200	.2500	.2000	.0325
WOMEN								
20	.1500	.0450	.0002	—	—	—	—	.0925
30	.1175	.0480	.0003	.0005	—	—	—	.0725
40	.0900	.0165	.0005	.0018	.2700	—	—	.0525
50	.0900	.0125	.0012	.0036	.2700	—	—	.0405
55	.0900	.0125	.0019	.0058	.2900	.1000	—	.0375
60	.0725	.0125	.0032	.0064	.4000	.1600	.2200	.0350
65	.0725	.0125	.0053	.0072	.4900	.3100	.2100	.0325
70	.0725	—	.0090	.0072	.5000	.3500	.2000	.0325

* Includes an inflation adjustment of 3.50%.

Actuarial

Benefit Recipients Added to and Removed From the Rolls, 1996–2001				
Fiscal Year Ended	Beginning	Additions	Deletions	Ending
2001	99,011	6,436	3,315	102,132
2000	95,796	6,536	3,321	99,011
1999	91,999	6,922	3,125	95,796
1998	88,718	6,329	3,048	91,999
1997	86,132	5,777	3,191	88,718
1996*	83,136	6,188	3,192	86,132

* Data not available for fiscal years before 1996.

Schedule of Valuation Data — Active Members, 1992–2001				
Valuation Date	Number	Annualized Salaries (in thousands)	Annual Average Pay	% Increase in Average Pay
2001	177,013	\$7,721,258	\$43,620	3%
2000	174,072	7,386,122	42,431	3%
1999	170,854	7,040,902	41,210	3%
1998	170,126	6,834,060	40,171	3%
1997	168,943	6,564,294	38,855	3%
1996	166,927	6,307,142	37,784	3%
1995	166,623	6,110,218	36,670	3%
1994	167,770	5,986,084	35,680	3%
1993	165,711	5,742,577	34,654	2%
1992	162,898	5,509,947	33,825	3%

Schedule of Valuation Data — Retirees/Beneficiaries, 1992–2001				
Valuation Date	Number	Annual Allowances (in thousands)	% Increase in Annual Allowances	Average Annual Allowances
2001	102,132	\$2,595,549	9%	\$25,414
2000	99,011	2,391,680	14%	24,156
1999	95,796	2,103,139	9%	21,954
1998	91,999	1,929,988	12%	20,978
1997	88,718	1,722,037	9%	19,410
1996	86,132	1,579,771	10%	18,341
1995	83,136	1,434,032	17%	17,249
1994	77,405	1,230,671	10%	15,899
1993	74,230	1,120,770	9%	15,099
1992	72,599	1,029,952	10%	14,187

Solvency Test, 1992–2001 (dollar amounts in thousands)

Valuation Date	Accrued Liability for:			Valuation Assets*	Portion of Accrued Liabilities Covered by Valuation Assets		
	(1) Active Member Contributions*	(2) Retirees and Beneficiaries*	(3) Active Members (Employer-Financed Portion)*		(1)	(2)	(3)
2001	\$7,445,894	\$30,145,012	\$25,090,334	\$57,450,612	100%	100%	79%
2000	7,174,675	27,604,436	24,414,047	54,712,921	100%	100%	82%
1999	6,867,910	25,152,626	22,742,804	49,124,802	100%	100%	75%
1998	6,569,783	22,994,697	21,563,608	43,865,907	100%	100%	66%
1997	6,222,725	20,249,628	20,091,418	38,743,272	100%	100%	61%
1996	5,862,250	18,420,595	18,484,067	34,569,651	100%	100%	56%
1995	5,533,684	16,745,090	17,708,401	31,416,677	100%	100%	52%
1994	5,158,561	14,025,124	17,688,124	28,543,410	100%	100%	53%
1993	4,798,350	12,869,723	16,820,904	26,259,447	100%	100%	51%
1992	4,434,876	11,506,994	14,858,368	22,536,343	100%	100%	44%

* The amounts reported include funds set aside to pay postemployment health care benefits.

Analysis of Financial Experience

Gains and Losses in Accrued Liabilities Resulting From Differences Between Assumed Experience and Actual Experience (dollar amounts in thousands)

Type of Activity:	Gain (or loss) for year ended June 30:				
	2001	2000	1999	1998	1997
Investment income. If there is greater investment income than assumed, there is a gain. If less, there is a loss.	\$ (52,901)	\$ 2,656,964	\$ 2,432,975	\$ 2,505,273	\$ 2,486,916
Payroll growth. If more contributions from payroll growth are received than expected, there is a gain. If less, there is a loss.	32,051	138,966	0	0	(108,545)
Salary increases. If there are smaller salary increases than assumed, there is a gain. If greater increases, there is a loss.	(554,162)	(472,983)	(368,504)	(266,140)	(275,172)
Retirement and other separation experience. If members retire from service at an older age or with a lower final average salary than assumed, there is a gain. If separation claims are less than expected, there is a gain.	184,272	(64,386)	35,715	(109,263)	(272,366)
Death after retirement. If retirees live shorter than expected, there is a gain. If retirees live longer than assumed, there is a loss.	(254,890)	(150,951)	120,664	(204,876)	(48,397)
Gain (or loss) during year from financial experience	(645,630)	2,107,610	2,220,850	1,924,994	1,782,436
Nonrecurring items adjustment for plan amendments	(70,159)	0	0	(220,259)	(671,174)
Composite gain (or loss) during the year	\$ (715,789)	\$ 2,107,610	\$ 2,220,850	\$ 1,704,735	\$ 1,111,262

Actuarial

Summary of Benefit and Contribution Provisions

Eligibility for Membership

Immediate upon commencement of employment.

Service Retirement

Eligibility

Any age with 30 years of service, age 55 with 25 years of service, or age 60 with five years of service. Members retiring before age 65 with less than 30 years of service credit receive a percentage reduction in benefit amounts.

Amounts

Annual amount equal to the greater of (a) 2.2% of final average salary for the three highest paid years, multiplied by years of total Ohio service credit, or 2.5% of final average salary for the three highest paid years if the member has 35 or more years of contributing service credit, multiplied by years of total service credit — except that for years of Ohio contributing service credit in excess of 30 the following formula percentage will apply:

Year	Percentage
31	2.5%
32	2.6%
33	2.7%
34	2.8%
35	2.9%
36	3.0%
37	3.1%
38	3.2%
39	3.3%

or (b) \$86 multiplied by years of service credit, and adjusted by the following percentage:

Attained Age	Years of Ohio or Service Credit	Percentage of Base Amount
58	25	75%
59	26	80%
60	27	85%
61		88%
	28	90%
62		91%
63		94%
	29	95%
64		97%
65	30 or more	100%

Annual salary is subject to a limit of \$200,000 as adjusted under Section 401(a)(17).

Maximum benefit — The lesser of: (a) 100% of average annual salary for the three highest paid years, or (b) the limit as established by Section 415 of the Internal Revenue Code.

Minimum benefit — The sum of the annuity provided by: (a) the member's contribution with interest, (b) a pension equal to the annuity, and (c) an additional pension of \$40 multiplied by the number of years of prior and military service.

Disability Retirement

Eligibility

A member may qualify if the following criteria are met: membership before July 30, 1992, and election of this benefit; completion of five or more years of service; under age 60; and incapacitated for the performance of normal job duties for at least 12 months.

Amount

- (1) Annuity with a reserve equal to the member's accumulated contributions, plus
- (2) The difference between (1) (noted above) and the greater of 2% of the average salary during the three highest paid years or \$86 times total service plus years and months from date of disability to age 60. Maximum allowance is 75% of final average salary. Minimum allowance is 30% of final average salary.

Disability Allowance

Eligibility

A member may qualify if the following criteria are met: membership after July 29, 1992, or membership on or before July 29, 1992, and election of this benefit; completion of five or more years of service; and incapacitated for the performance of normal job duties for at least 12 months.

Amount

The amount is 2.2% of the average salary during the three highest paid years times total service. Maximum allowance is 60% of final average salary. Minimum allowance is 45% of final average salary. The disability allowance payment terminates at age 65 (or later if payment begins after age 60). After termination of the disability allowance, the member may apply for service retirement.

Death After Retirement

Lump-sum payment of \$1,000 upon death after service or disability retirement.

Survivor's Benefit

Eligibility

A member may qualify for this benefit after at least 1-1/2 years of credit for Ohio service with at least 1/4 year of such service in the 2-1/2 years preceding death; or upon death of a disability retiree.

Amount

If member was eligible for retirement, spouse or other sole dependent beneficiary may elect to receive Option 1 benefits in lieu of return of contributions. If member was not eligible for retirement, certain designated beneficiaries may elect to receive dependent-based benefits in lieu of return of contributions (see chart below) or service-based benefits, which provide a minimum benefit of a percentage of final average salary based on years of credited service ranging from 29% with 20 years of service to 60% with 29 years of service.

Qualified beneficiaries are spouse, dependent children and/or dependent parents over age 65.

Number of Qualified Dependents	% of Average Annual Salary for Three Highest Paid Years	Minimum Annual Benefit
1	25%	\$ 1,152
2	40%	2,232
3	50%	2,832
4	55%	2,832
5 or more	60%	2,832

Lump-Sum Withdrawal Option

In lieu of any other pension or survivor benefits, a member who leaves the system can receive his or her member contributions with interest in a lump sum according to the following schedule:

Credited Service	Lump-Sum Amount
Less than three years	Member contributions with 4% interest
Three or more years but less than five years	Member contributions with 5% interest
Five or more years	150% of member contributions with 5% interest

The board has the authority to modify the interest credited to member contributions.

Actuarial

Summary of Benefit and Contribution Provisions (cont.)

Optional Forms of Benefit

Option 1 — 100% joint and survivorship. Reduced retirement allowance payable to the member and continuing for life to the member's sole beneficiary (named at retirement) after the member's death.

Option 2 — A joint and survivorship annuity payable during the lifetime of the member, with the member's sole beneficiary (named at retirement) to receive some other portion of the member's annuity after the member's death.

Option 3 — The member's reduced retirement allowance provided under Option 1 or Option 2 paid for life to the member's sole beneficiary (named at retirement) after the member's death. In the event of the death of the sole beneficiary or termination of

marriage between the retiree and the sole beneficiary, the retiree may elect to return to a single lifetime benefit equivalent, available for an actuarially computed charge as determined by the Retirement Board. In the case of termination of marriage, the election may be made with the written consent of the beneficiary or by court order.

Option 4 — A life annuity payable during the lifetime of the member with a guarantee that, upon the member's death before the expiration of a certain period, the benefit will continue for the remainder of such period to the beneficiary. Joint beneficiaries may receive the present value of any remaining payments in a lump-sum settlement. If all beneficiaries die before the expiration of the certain period, the present value of all remaining payments is paid to the estate of the beneficiary last receiving benefits.

Option 5 — A plan of payment established by the Retirement Board combining any of the features of Options 1, 2 and 4.

Refund of Contributions

A member's contributions with interest are refunded upon termination of employment where no other benefit is payable. Upon death after retirement or upon death of a survivor in receipt of benefits, the member's accumulated contributions, less payments made, are returned to the designated beneficiary.

Cost-of-Living Benefits

The basic benefit is increased by the increase in the Consumer Price Index each year, but not to exceed 3% of the original base benefit.

Health Care

Retirees, their spouse and dependents have access to a comprehensive medical expense health care plan as may be offered by the Retirement Board and which is subject to changes in terms and conditions from time to time.

Contribution

By members: 9.30% of salary effective July 1, 1994.

By employers: 14% of salaries of their employees who are members.



Mary gathers background data and maps of STRS Ohio-owned properties that are critical for making important real estate investment decisions.

Expenses by Type Years Ending June 30, 1992–2001 (in thousands)

Fiscal Year	Benefits	Refunds	Administration	Total
2001	\$2,855,859	\$93,868	\$72,277	\$3,022,004
2000	2,634,484	105,759	57,817	2,798,060
1999	2,307,449	91,037	48,967	2,447,453
1998	2,088,869	87,705	42,489	2,219,063
1997	1,880,129	32,313	42,884	1,955,326
1996	1,718,861	24,118	37,747	1,780,726
1995	1,563,757	21,233	38,926	1,623,916
1994	1,438,446	18,235	38,770	1,495,451
1993	1,347,827	16,386	35,870	1,400,083
1992	1,237,969	17,488	28,956	1,284,413

Revenues by Source Years Ending June 30, 1992–2001 (in thousands)

Fiscal Year	Member Contributions	Employer Contributions	Net Investment Income	Health Care Premiums	State Appropriations	Other	Total
2001	\$785,009	\$1,167,830	\$(3,694,121)	\$68,582	\$0	\$9,610	\$(1,663,090)
2000	755,146	1,128,314	5,504,137	60,375	1,514	6,487	7,455,973
1999	716,551	1,076,879	6,003,597	47,819	1,780	7,896	7,854,522
1998	697,404	1,036,223	6,039,679	39,682	2,067	4,994	7,820,049
1997	679,499	1,005,354	6,143,363*	38,347	2,377	6,281	7,875,221
1996	635,716	1,002,441	3,664,683	37,224	2,698	6,782	5,349,544
1995	624,812	956,284	2,340,907	36,842	3,035	6,008	3,967,888
1994	589,186	902,299	2,231,241	34,603	3,396	4,805	3,765,530
1993	564,005	869,862	2,394,523	24,184	3,755	5,180	3,861,509
1992	548,841	862,655	2,294,646	11,126	4,099	4,540	3,725,907

* Effective July 1, 1996, net investment income includes the net (depreciation) appreciation in fair value of investments.

Statistical

Number of Benefit Recipients by Type, 1992–2001

As of July 1	Service Retirement	Disability Retirement	Beneficiaries Receiving Optional Allowances	Survivor Benefits	Total
2001	83,918	6,449	6,340	5,425	102,132
2000	81,111	6,367	6,152	5,381	99,011
1999	78,341	6,259	5,948	5,248	95,796
1998	75,482	6,157	5,675	4,685	91,999
1997	72,601	6,000	5,486	4,631	88,718
1996	70,448	5,923	5,206	4,555	86,132
1995	67,989	5,711	4,941	4,495	83,136
1994	63,182	5,217	4,739	4,267	77,405
1993	61,515	5,020	4,478	3,217	74,230
1992	59,994	4,830	4,274	3,501	72,599

Average Monthly Allowances by Type, 1992–2001

As of July 1	Service Retirement	Disability Retirement	Beneficiaries Receiving Optional Allowances	Survivor Benefits	Average
2001	\$2,238	\$2,168	\$1,396	\$1,047	\$2,118
2000	2,124	2,101	1,340	1,003	2,013
1999	1,938	1,961	1,086	894	1,830
1998	1,844	1,887	1,031	893	1,748
1997	1,705	1,764	974	822	1,618
1996	1,608	1,688	931	779	1,528
1995	1,510	1,603	886	732	1,437
1994	1,388	1,504	843	707	1,325
1993	1,304	1,433	803	748	1,258
1992	1,227	1,359	770	682	1,182

Benefit Expenses by Type, 1992–2001 (in thousands)

Fiscal Year Ended	Service Retirement	Disability Retirement	Survivor Benefits	Supplemental Benefit	Health Care*	Other	Total
2001	\$2,203,280	\$160,775	\$65,591	\$50,386	\$369,354	\$6,473	\$2,855,859
2000	2,019,521	152,365	62,346	48,493	343,512	8,247	2,634,484
1999	1,764,172	139,296	52,863	46,448	297,748	6,922	2,307,449
1998	1,601,143	130,429	47,920	44,876	258,906	5,595	2,088,869
1997	1,440,163	118,893	43,539	43,278	230,424	3,832	1,880,129
1996	1,307,482	109,250	40,283	41,750	176,773	6,099	1,681,637
1995	1,185,066	100,805	37,756	34,567	165,767	2,954	1,526,915
1994	1,083,335	92,091	35,198	33,586	157,276	2,357	1,403,843
1993	985,024	83,888	32,804	32,489	187,318	2,120	1,323,643
1992	897,259	76,378	30,726	28,815	189,784	3,881	1,226,843

* Health care premiums prior to fiscal 1997 were netted against health care expenses. Starting in fiscal 1997, health care premiums are reflected as revenue.

Selected Funding Information, 1992–2001 (dollars in thousands)

As of July 1	Contribution Rate		Interest Assumption	Payroll Growth Assumption	Unfunded Accrued Liability*	Funding Period
	Member	Employer				
2001	9.30%	14.00%	7.75%	4.500%	\$5,230,628	27.5 Yrs.
2000	9.30%	14.00%	7.75%	4.500%	4,480,237	23.1 Yrs.
1999	9.30%	14.00%	7.50%	4.500%	5,638,538	16.3 Yrs.
1998	9.30%	14.00%	7.50%	4.500%	7,262,181	24.2 Yrs.
1997	9.30%	14.00%	7.50%	4.500%	7,820,498	26.9 Yrs.
1996	9.30%	14.00%	7.50%	4.500%	8,197,261	28.4 Yrs.
1995	9.30%	14.00%	7.50%	5.000%	8,570,498	29.3 Yrs.
1994	9.30%	14.00%	7.50%	5.000%	8,328,399	30.5 Yrs.
1993	9.25%	14.00%	7.50%	5.000%	8,229,529	31.5 Yrs.
1992	9.25%	14.00%	7.75%	5.875%	8,263,895	32.5 Yrs.

* Excluding health care

Number of Reporting Employers by Type, 1992–2001

Fiscal Year Ended	City School Districts	Local School Districts	County Educational Service Centers	Exempted Village Districts	Vocational & Technical Schools	Colleges & Universities	County MR/DD Boards	Community Schools*	Other	Total
2001	194	369	61	49	49	37	80	72	8	919
2000	194	369	61	49	49	37	82	51	8	900
1999	192	371	63	49	49	37	82	16	7	866
1998	192	372	65	49	49	37	82	*	8	854
1997	192	371	73	49	49	37	82	*	8	861
1996	192	371	80	49	49	37	82	*	8	868
1995	192	371	80	49	49	37	82	*	9	869
1994	192	371	81	49	49	37	82	*	6	867
1993	192	372	81	49	51	35	82	*	3	865
1992	193	370	85	49	51	35	88	*	2	873

* Community schools were added as reporting employers in fiscal year 1999.

Badu helps employers submit payroll reporting information electronically — saving time and improving accuracy.



Copies of this report are available from:
State Teachers Retirement System of Ohio
275 E. Broad St.
Columbus, OH 43215-3771
614-227-4090

