

SERS PLAN 3 REPORT

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Contribution rate flexibility awaits IRS approval

The 2003 Legislature passed House Bill 1206 giving Plan 3 members an opportunity each January to select a different retirement contribution rate option. However, before the legislation can be implemented for the School Employees' Retirement System (SERS) Plan 3, Internal Revenue Service (IRS) approval is required. DRS requested, but has not yet received, the necessary approval to provide this option to SERS and the Public Employees' Retirement System. Until the IRS grants approval for SERS Plan 3 rate flexibility, your contribution rate selection can only be changed when you change employers. If the IRS approves the request during the 2004 calendar year, the first rate flexibility period for SERS Plan 3 members will be in January 2005.

The IRS has approved a similar contribution rate flexibility option for the Teachers' Retirement System (TRS) Plan 3. The first rate change period for TRS was January 2004.

New socially responsible fund to be available April 1

In response to requests from members, the Washington State Investment Board will introduce a new socially responsible fund to the Plan 3 investment line-up. The fund, managed by Walden Asset Management, allows investors to align their financial objectives and social concerns. This fund will become available April 1. DRS will mail additional details to members in March.

Horizon Funds feature a new international fund component

In January 2004 the Washington State Investment Board (WSIB) replaced the current International Stock Index component of the Horizon Funds with a new International Stock Index

SERS PLAN 3 WSIB TOTAL ALLOCATION PORTFOLIO (TAP)

AS OF 12/31/2003

	AVERAGE ANNUAL RETURNS			
	4th Qtr 2003	1-Year	3-Year	5-Year
TOTAL ALLOCATION PORTFOLIO	7.49%	19.24%	1.55%	4.50%

The Washington State Investment Board (WSIB) periodically reviews and adjusts the TAP Fund's asset allocation. Over the last five years, the TAP Fund has shifted to a more aggressive asset mix. These returns reflect the actual asset mixes during the time periods shown.

SERS PLAN 3 SELF-DIRECTED FUNDS

AS OF 12/31/2003

	4th Qtr 2003	1-Year	3-Year	5-Year
MONEY MARKET FUND	0.23%	1.08%	2.43%	N/A
WASHINGTON STATE BOND FUND	0.30%	6.30%	7.97%	N/A
U.S. LARGE STOCK INDEX FUND	12.16%	28.46%	-4.17%	N/A
U.S. STOCK MARKET INDEX FUND	12.34%	30.62%	-3.24%	N/A
U.S. SMALL STOCK INDEX FUND	14.42%	46.54%	6.06%	N/A
INTERNATIONAL STOCK INDEX FUND	16.58%	35.06%	-4.87%	N/A
SHORT-HORIZON FUND	4.07%	12.14%	3.61%	N/A
MID-HORIZON FUND	7.38%	20.17%	2.40%	N/A
LONG-HORIZON FUND	10.93%	27.21%	-0.55%	N/A

The SERS Plan 3 Self-Directed Funds were available for investment on September 1, 2000 and have no performance history prior to this date. Actual inception dates (start of fund activity) are: U.S. Stock Market Index, U.S. Large Stock Index, Mid-Horizon and Money Market on October 6, 2000; International Stock Index, U.S. Small Stock Index, Washington State Bond, Short-Horizon and Long-Horizon on October 10, 2000.

All returns are net of fees. Self-Directed funds are valued daily; your account balance and rate of return will vary accordingly. Past performance is no guarantee of future results. For more information about the funds, please see the *Plan 3 Investment Guide* or the Web site at <http://www.icmarc.org/sers/investing>.

Returns cover the period ending December 31, 2003.

N/A - Not Applicable

component fund. The new fund component is expected to provide Plan 3 members with improved performance opportunities.

The WSIB expects the new fund to provide stronger returns that more closely mirror the Morgan Stanley Capital International Europe, Australia, Far East (MSCI EAFE) index. This anticipated increase in fund performance will benefit all members who invest in the Horizon Funds.

There are currently no trading restrictions on the Horizon Funds.

Gain sharing will not occur in 2004

There will be no gain sharing payments made to Plan 3 members in 2004. Gain sharing occurs only when the retirement fund's four-year annual earnings average experiences "extraordinary gains" by exceeding the 10 percent benchmark. The four-year average ending in fiscal year 2003 did not exceed this benchmark.

When applicable, gain sharing payments are deposited in Plan 3 member accounts in January of even-numbered years. The four-year average is based on the four fiscal years preceding a payment year.

WSIB moves quickly to make sure your investments are secure

As soon as the issue of market timing and late trading of mutual funds broke, the Washington State Investment Board (WSIB) took immediate, pre-emptive measures to ensure that public employee retirement and Plan 3 investments are safe and secure.

Here is what has been done by the WSIB to protect your Plan 3 investments:

- WSIB contacted all the managers of the self directed funds and all have provided written assurances that they do not permit late trading of mutual fund shares and have policies in place to limit and restrict market timing activities.
- The WSIB does not permit late trading on the options managed internally.
- Putnam Investments manages the international equity fund component of Plan 3's Total Allocation Portfolio (TAP). In October, when charges were filed against some managers at Putnam Investments, Putnam was immediately placed on WSIB's Watchlist and daily contact between the WSIB and Putnam's senior management team was established. In November, WSIB directed staff to conduct an immediate search to replace Putnam Investments as the WSIB's core international equity fund manager. The expedited search could be completed as early as January 2004.

Going forward, it is possible that other managers or funds with similar late trading issues will be identified. The WSIB continues to monitor the

situation closely and will immediately factor any significant changes into the next steps. The bottom line for Plan 3 members is that your investments are being prudently and carefully managed and the WSIB is doing everything in its power to make sure that does not change.

Market outlook

In the three months ending November 30, 2003, the U.S. economy continued to take significant strides towards recovery. Robust growth in U.S. Gross Domestic Product (GDP) topped all other economic news as analysts estimated that the U.S. economy is growing faster than at any other time in the past 20 years. Monetary and fiscal stimulus in the form of tax cuts and continued low mortgage rates were the key reasons behind the phenomenal growth. News of improved corporate earnings, increased business spending and a continued decline in unemployment levels also demonstrated that the economic environment has improved enormously since the beginning of the year.

Bonds

After a more difficult time for bonds in the late summer months, the bond market rebounded over the three months. As signs of economic recovery became more apparent, bond investors have increasingly put their money in lower quality, higher yielding segments of the bond market. As a result, corporate bonds and high-yield bonds experienced a much stronger quarter than government bonds.

At the October meeting, the Federal Reserve Board reiterated its view that the predominant risk to the U.S.

economy is a fall in inflation. Even with strong growth in GDP, Chairman Alan Greenspan warned that deflationary forces are still prevalent, leading the Reserve Board to leave interest rates steady at 1.00 percent.

Stocks

Although the stock market slipped in September, it quickly rebounded in October as positive outlooks for earnings improvements and GDP growth stimulated investor confidence. Enthusiasm was slightly dampened during October with the investigation into alleged trading abuses in several high profile mutual fund companies. The broad impact from these allegations appeared to be limited to the specific companies in question. The month of November saw stocks continue to march their way toward the first year of gains since 1999. Leading the markets upward again were small companies and technology-related stocks. Both growth and value stocks provided strong performances overall, but investors tended to favor value stocks, which have trailed growth stocks so far in 2003.

Overall, international stocks outperformed U.S. stocks over the three-month period. Optimism concerning the influential U.S. economy helped drive overseas markets. Emerging markets added to their remarkable year with their eighth consecutive month of positive gains. Asia continued to be the strongest region among the emerging markets, benefiting from increasing demand from the U.S., Europe, China and Japan.

*By Arnerich Massena & Associates
Due to printing requirements, this article
includes market activity as of November 2003.*

Washington State Self-Directed Investment Program Fees and Expenses

The Washington State Investment Board (WSIB) adjusts its advisor fee for all Plan 3 Self-Directed funds annually. For 2003, the WSIB advisor fee was 1.45 bps. For 2004, the WSIB advisor fee decreases to 1.29 bps.

NEW FEES AS OF JANUARY 2004

Money Market	Bond Fund	US Large Stock Index	US Stock Market Index	US Small Stock Index	International Stock Index	Short Horizon	Mid Horizon	Long Horizon
.2629%	.1655%	.1670%	.1680%	.1724%	.2229%	.2164%	.1762%	.1804%

If you have any questions, please contact ICMA-RC (1-888-711-8773) or visit the Web site (<http://www.icmarc.org/sers>).