This is Lon Mishler…

I wanted to provide some additional comments, and another view regarding the viability of the variable option.

First, the implication is that a larger portfolio exposure to stocks provides minimal benefit to investors. In the June 10 memo it was stated "The potential additional return produced by the Variable Fund over long periods is marginal, when compared to the diversified core fund." Wayne says: "…the potential of out performance by the Variable Fund is small and possible only with the acceptance of significant additional downside risk."

While I agree that risk, as measured by standard deviation, increases along with more equities in the portfolio, performance also increases. Ibbotson data for the period extending from 1926 to 2005 shows the historical average annual return for the following portfolio configurations (percentages in stocks/bonds):

50/50	8.16%
70/30	9.20%
85/15	9.91%

Although the increase in each percentage return does not look significant…moving from a 70/30 mix to an 85/15 mix will result in about 15% more money after 20 years.

Modern portfolio theory shows that for any given value of standard deviation, there is a portfolio that provides the higher possible rate of return. The efficient frontier curve is, nevertheless, upward sloping which indicates annual returns do increase with higher standard deviations, e.g. more stocks. While it is true that the returns increase at a decreasing rate, they still increase.

Do we want to limit the ability to younger teachers to take on more risk, perhaps appropriate risk given the number of years before they retire?

If we provide a money purchase option, where the value of the account can increase the level of a retirement benefit, do we owe participants an opportunity to enhance their account values by accepting more risk?

A more paternalistic approach is to decide how much risk is appropriate and to make investment decisions for the participants as a single group. Settling on a specific mix, however, removes the opportunity to vary risk, and results, on an individual basis.

In the private sector, many plans are changing from defined benefit plans to defined contribution plans. The benefits to the employers are obvious as investment risk and costs are shifted to the participants. In the process, however, some employees will appreciate the opportunity to be more involved in the investment decisions.

I want to quickly add that I am not proposing a defined contribution approach. We all love and appreciate our defined benefit plan.

Thanks.

Lon Mishler