INVESTMENT REPORT

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

Second Quarter
Fiscal Year 2011 – 2012

October 1, 2011 – December 31, 2011

Prepared for:
Board of Trustees

March 30, 2012

Investment Advisory Council

Pursuant to T.C.A. Section 8-37-108, the State Treasurer shall nominate, with the advice and consent of the Board of Trustees, the Investment Advisory Council, compromised of five senior investment professionals in the Tennessee investment community, who shall have at least five years professional experience as a portfolio manager, economist or an investment advisor in any field of which investments of TCRS funds are authorized. The term of appointment is for five years. Also, the treasurer may nominate two (2) additional members for three year terms.

The TCRS investment staff consults quarterly with the Advisory Council on a formal basis for strategy and guidance, and on an informal basis as needed.

The current members are as follows:

Council Member	Expiration of Term	Appointed Term
Frederick S. Crown, Jr., CFA 124 Longwood Place Nashville, TN 37215 Phone: 615-385-3753 E-mail: **crownfl@gmail.com**	June 30, 2012	5 year
Henry J. Delicata Park Street Capital One Federal Street, 24th Floor Boston, MA 02109 Phone: (cell) 617-347-8854 / (office) 617-897-9252 E-mail: **hdelicata@parkstreetcapital.com**	June 30, 2014	5 year
Susan Logan Huffman, CFA Managing Director Reliant Investment Management, LLC 6077 Primacy Parkway, Suite 130 Memphis, TN 38119 Phone: 901-843-0600 / Fax: 901-843-0325 E-mail: **shuffman@reliantllc.com**	June 30, 2016	5 year
George B. Stadler, CFA 95 White Bridge Road, Suite 414 Nashville, TN 37205 Phone: 615-416-3455 cell E-mail: **george@hmscm.com**	June 30, 2015	5 year
Chuck Webb, CFA Chief Investment Officer Weaver C. Barksdale & Associates One Burton Hills Boulevard, Suite 100 Nashville, TN 37215 Phone: 615-665-1088 E-mail: **cwebb@wcbarksdale.com**	June 30, 2013	5 year

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

Board of Trustees Meeting
Second Quarter
Fiscal Year 2011 – 2012

October 1, 2011 – December 31, 2011

TABLE OF CONTENTS **Page**

Minutes from the Investment Advisory Council Meeting
March 6, 2012

Mr. Michael Brakebill, Chief Investment Officer, convened the meeting at 10:00 a.m. in the 11th Floor conference room of the Andrew Jackson State Office Building. Investment Advisory Council (IAC) members present were Mr. Fred Crown, Mr. Chuck Webb, and Mr. George Stadler. Ms. Susan Huffman and Mr. Henry Delicata participated via conference call. Investment staff members present were Michael Brakebill, Andy Palmer, Mike Keeler, Peter Katseff, Lamar Villere, Tim McClure, Roy Wellington, Jim Robinson, Derrick Dagnan Carrie Green, Rachel Roberts, Daniel Crews, Kushal Gupta, Ken McDowell, Matthew Haitas, Michael Giggie, and Rhonda Myers.

Mr. Brakebill reviewed investment performance which was illustrated in the Investment Report for December 31, 2011 and in the Strategic Investment Solutions (SIS) quarterly performance report. He noted the total return of TCRS was 5.9% for the quarter and 5.0% for the year. He highlighted the equity transactions in the second half of 2011 and the first quarter of 2012 of $1.35 billion in purchases during the market lows in August and September and the sale of $250 million in February after the equity market recovered. Mr. Brakebill then provided an overview of the strategic initiatives underway. Strategic lending is an initiative that will provide a broader lending platform. It will focus on strategies that provide high current income with limited risk of principal largely due to dislocations in the markets for traditional lenders. The real estate portfolio will seek to increase its exposure to higher risk and higher return real estate. Finally, Mr. Brakebill reviewed the potential to increase international equity exposure by investing in emerging markets. He stated that TCRS could customize its exposure to emerging markets by including and excluding specific countries if they did not meet TCRS's goals. He noted that this strategy could be achieved by using exchange traded funds. All the members of IAC affirmed their support of the proposed strategic initiatives.

Mike Keeler moved the discussion to domestic equities. The rather odd combination of small capitalization and value factors dominated returns during the period, essentially a "risk on" quarter but heavily loaded toward the early part of the quarter and featuring a somewhat surprising quality quirk. Domestic Equities outperformed the S&P 1500 composite in the quarter due to strong relative performance by the Quant Fund and a slight overweight to small cap stocks, somewhat offset by an underweight to mid cap stocks. The Fund's overall bias toward quality also likely helped relative returns during the period. Stock selection provided all of the excess return above the benchmark during the quarter as industry sector contribution was actually negative, mostly due to an overall underweight of the Industrial sector.

The Mid Cap portfolio outperformed the S&P Mid Cap 400 primarily due to good stock selection in the Consumer Staples sector (particularly not owning Green Mountain Coffee Roasters), overweight positions and good stock picking in Specialty Chemicals (Ashland and RPM) and Energy as well as underweights in the Paper and Container industries. Relative performance was negatively affected by largely missing the rally in Apparel/Luxury goods during the period and less than stellar stock selection in the Industrial sector. Stock selection was responsible for all of the excess return against the benchmark with industry sector allocation contributing a slight negative.

Looking ahead, expectations for 2012 are pretty reasonable or even a bit pessimistic as several pundits noted going into the December quarter reporting season. However, early results have been mixed. Although the economy is still dealing with the usual suspects globally, the domestic US economy seems to be slowly improving. Combined with an improving valuation spread between small and large cap stocks, the case for the fund's small and mid cap underweight is rapidly eroding and the fund will be looking to increase exposure to those areas going forward.

Jim Robinson noted that almost everything went right for the Quant Fund in the December quarter. Trading, group allocation, and stock selection each added value; a total of +164 basis points of relative performance. Recent tactical developments include correcting some computational problems in the multi-factor models. Residual reversal effects were not properly accounted for in some relative strength calculations. He noted that Staff has also started generating efficient frontier curves before major portfolio rebalances to explicitly consider a wide range of risk and reward trade-offs and their expected execution costs.

Roy Wellington said the Sector Fund continues to expect economic recovery, favoring the Consumer Discretionary and Technology sectors. Markets responded to monetary stimulus in Europe while the Greek debt crises continued at a slow speed. The labor markets are responding to stimulus here at home, one of the last elements of economic recovery. There were no changes to the futures holdings but small cap as described by the S&P Index continues to outperform the Russell Small Cap Index.

The externally managed international equity portfolio came out on the plus side of mixed in the fourth quarter. Beating the benchmark likely required an overweight to Europe which is tough to do given the uncertainty. However, it was a factor in the results of two outperforming and two underperforming managers. Stock selection was the factor most often cited by managers to explain relative performance. TCRS continues to hold out for its price before it moves to eliminate the underweight to international equities.

Andrew Palmer presented the fixed income products. For the fourth quarter, the Domestic Fixed Income portfolio underperformed the Citigroup LPF by 10 basis points while providing an absolute return of 1.73%. The Credit portfolio contributed to the underperformance because it began the period with less credit risk than the index and was overweight positions with somewhat less liquidity. During the quarter credit spreads narrowed but liquidity spreads widened as dealers' balance sheets were constrained by new capital rules. Duration positioning negatively impacted the returns of the Government 5+ portfolio. The inflation protected portfolio underperformed by 4 bps as real rates continued to fall during the quarter. With interest rates at historically low levels and interest rate sensitivity high in the Domestic and Inflation Linked portfolios, staff is maintaining a slight underweight to interest rates and using interest rate volatility to minimize the impact on performance if rates fall.

The International Fixed Portfolio had a strong relative quarter as an underweight to the Euro in favor of British Pound, Norwegian Kroner and Canadian Dollar was rewarded during the quarter. The portfolio added 42 basis points of relative return for the quarter.

Mr. Palmer reviewed the Fixed Income Derivatives activity in the quarter. For interest rate futures, no new strategies were initiated and most of the activity involved rolling positions and small adjustments. The impact of the strategies on performance was as expected. There were no currency forwards employed during the quarter. MBS TBA activity was discussed to describe the risk management for extended settlements. Staff was active in reviewing counterparty risk throughout the quarter and closed out exposures to MF Global as the company's struggles became apparent.

Peter Katseff provided an update on the Real Estate portfolio. He noted that the last two apartment acquisitions are performing as expected. He stated that Staff is focusing on adding apartments to the portfolio. He added that this will be accomplished through acquisitions and potentially by adding a "build to core" strategy to develop apartments with joint venture partners. In addition, Staff is currently pursuing two student housing opportunities. Mr. Katseff reported that TCRS is in due diligence with a closed-end commingled fund that specializes in non-core real estate. He noted that this transaction should close by the end of the first quarter. Finally, he stated that year-end appraisals were complete and should show a total return of above 10 percent in 2011. As real estate performance is reported one quarter in arrears, these returns will be reported next quarter.

Lamar Villere provided an update on the Private Equity program. He explained that while it is too early to be meaningful, performance has actually been quite good, with the portfolio exceeding its benchmark over the quarter, one year, and since inception. He reiterated that he expects performance to turn negative due to the well-documented j-curve effect within private equity, although he noted that some early successes in the portfolio seem to be mitigating that effect thus far. He also reviewed the portfolio's sub-asset allocations, which are still significantly different from targets. Mr. Villere pointed out that with the program still in its infancy, it would take time for the allocations to shift toward the long term targets.

Tim McClure stated that there were $7.5 billion in equity trades for the quarter. Brad Pritchett and Dianne Willocks delivered a strong trading performance during this challenging quarter by adding value of 1.5 basis points as compared to the Abel Noser universe of equity trades.

Mr. Brakebill and the IAC members discussed their outlook for the economy and for investments. The meeting adjourned at 12:00 p.m.

Page is intended to be blank

Performance Review
December 2011

Absolute comparison

- 1 quarter return of 5.9%
- 1 year return of 5.0%
- 10 year return of 4.8%

Benchmark (relative) comparison

- Qtr return lagged allocation index by 0.3%
- 1 year return beat allocation index by 0.9%
- 3 year return trails allocation index by 0.3%
    - TAA subtracted 42 bps for quarter
    - DFI down 10 bps in quarter, down 45 bps for year
        - 14.3% return for year!
    - DE up 41 bps in quarter, up 215 bps for year
        - Excellent relative year
    - IE up 23 bps in quarter, up 175 bps for year
    - RE down 146 bps for year
        - 14.6% for year, vs. median fund 12.5%

Peer comparison

- 1 quarter return ranked at 40% (0% = best)
- 1 year return ranked at 4%
    - 5% 2011 return may be the best return for a large pension fund
    - Beat median fund (0.9%) by 4.1%
- 3 year return ranked at 72% (10.2% vs. 11.1% median)
- 5 year return ranked at 18% (2.8% vs. 2.0% median)

Key Initiatives
December 2011

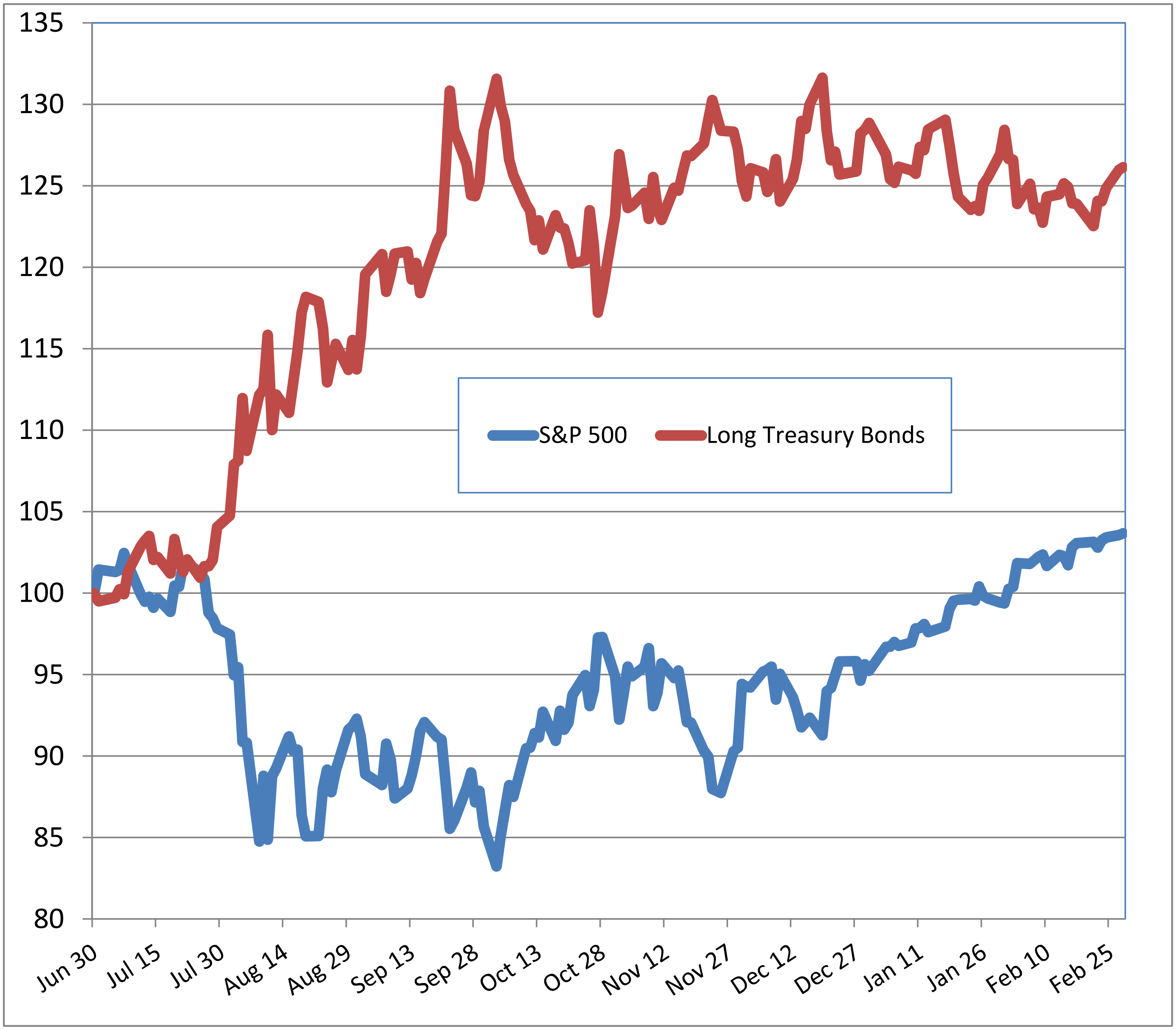
- Asset Allocation Review
  - Strategic lending
  - Real estate strategy
  - Global equities

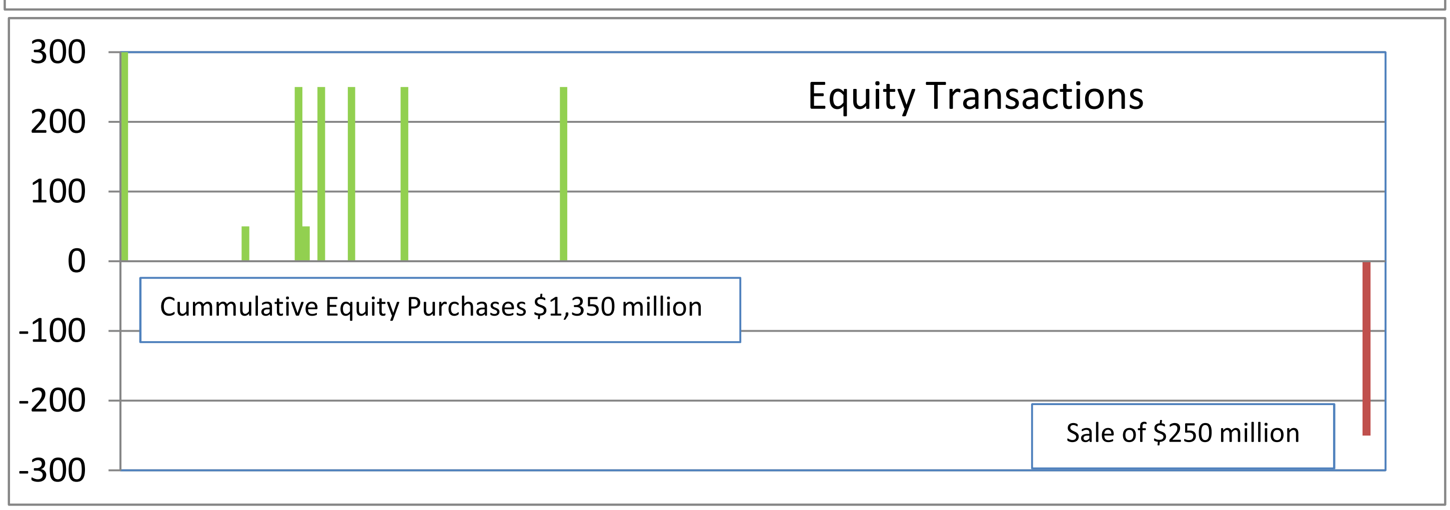
- SIS Asset/Liability Study

- Private Equity Due Diligence

- Tactical Allocation

TCRS FY2011 YTD
Market Movements and Investment Responses

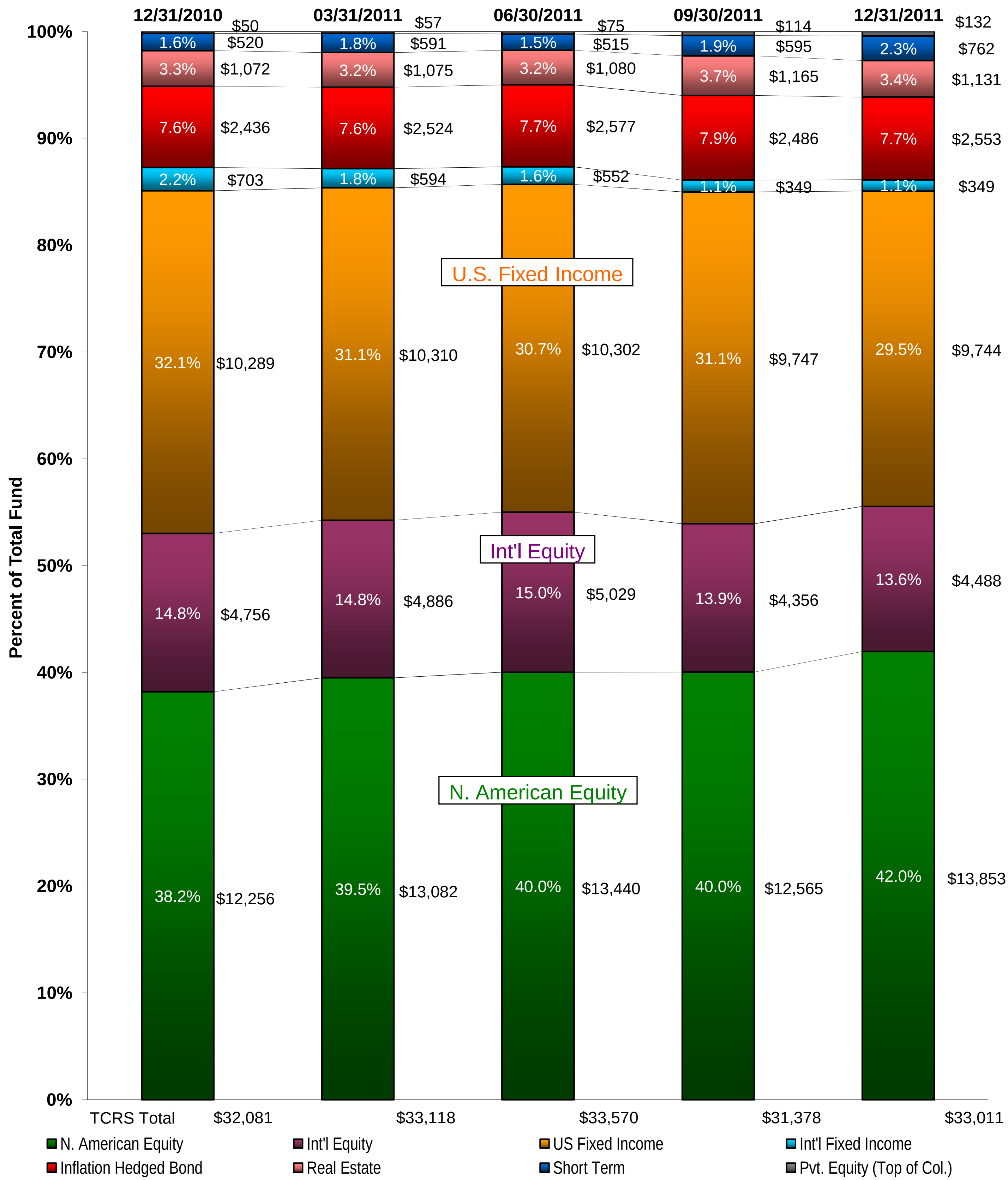




Page is intended to be blank

TCRS Asset Allocation

December 2011

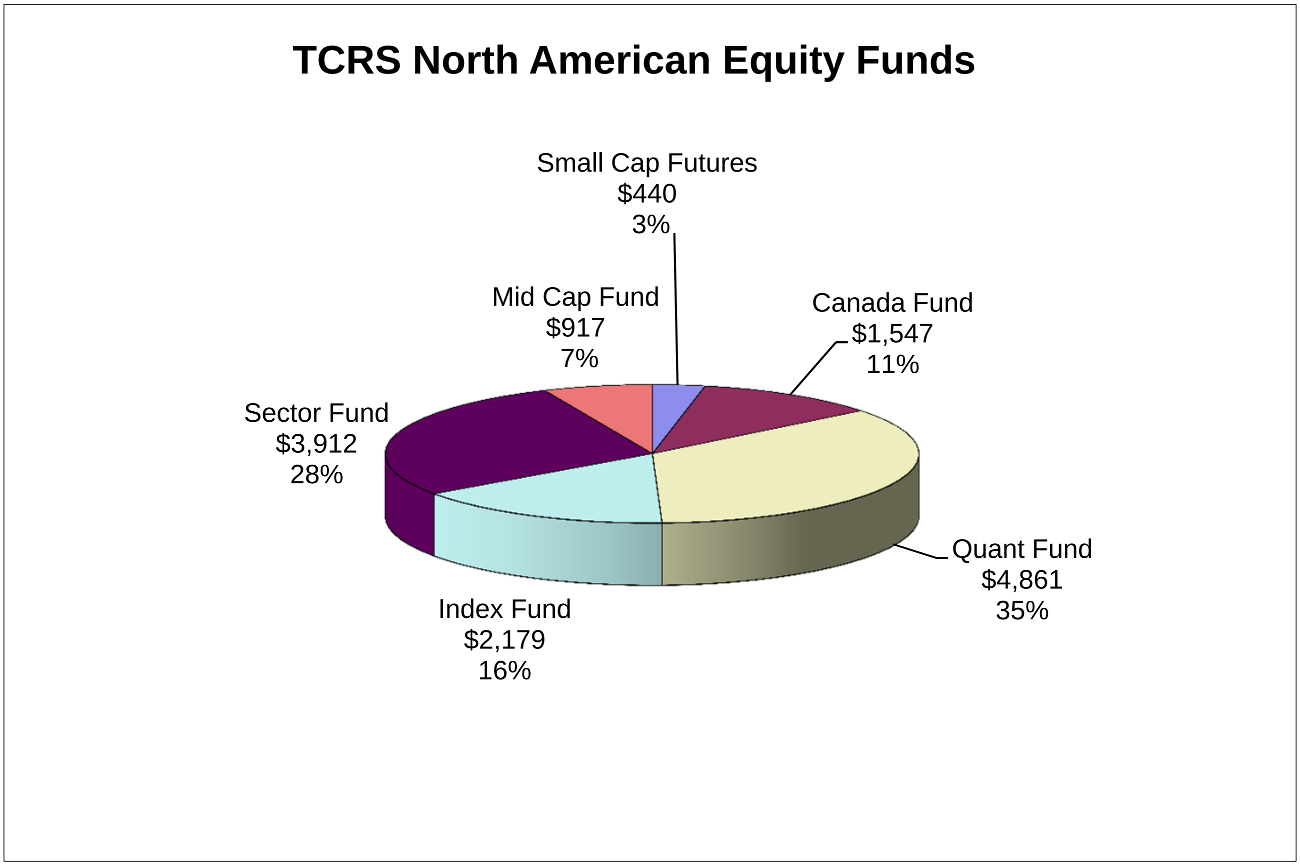


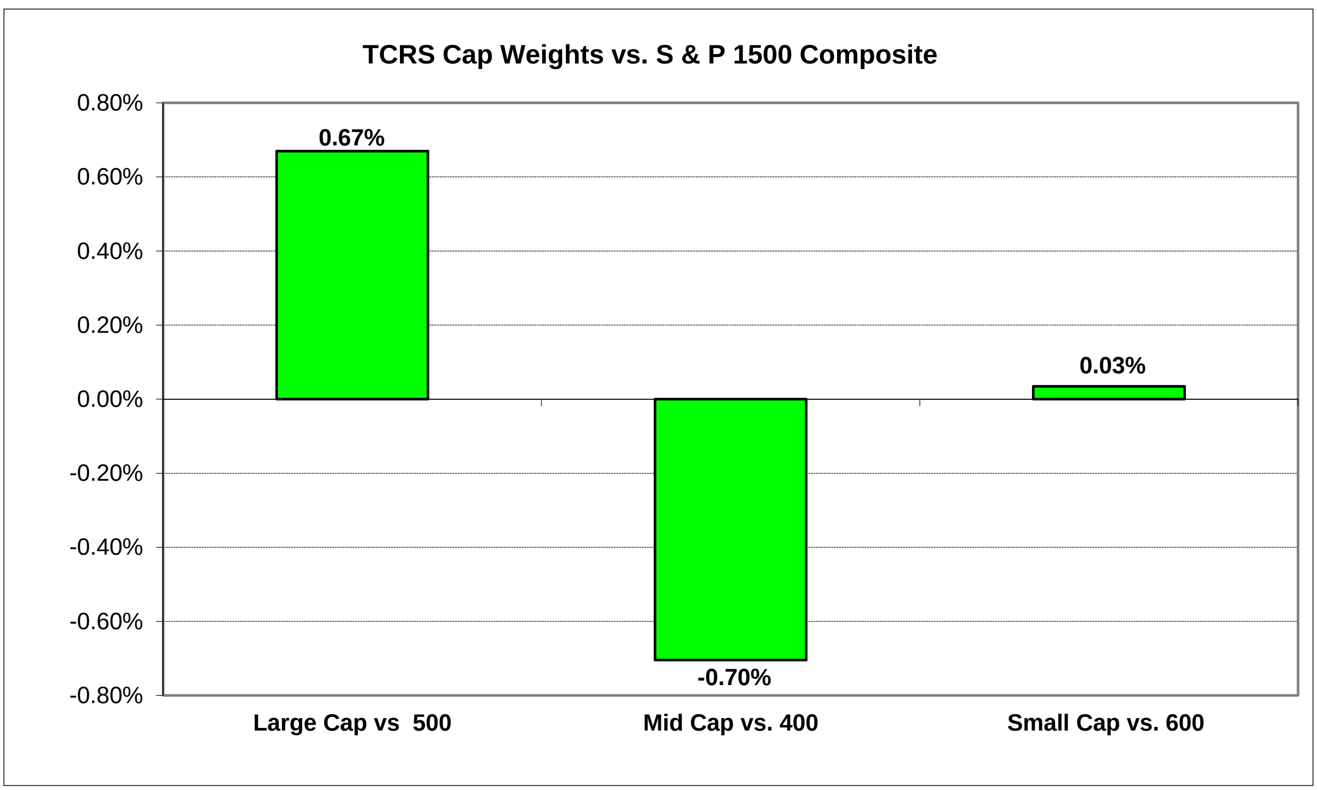
$ = millions

Source: Strategic Investment Solutions, Inc.

Domestic Equity Portfolio Overview

Michael Keeler, CFA





Large Cap Quant Fund

Jim Robinson, CFA

Factor Comparison Factor	F1-FN Return	Avg IC
Quant Rank VW	1.340	0.041
V+M	0.694	0.054
RV	1.635	0.017
EM	1.987	0.027
PM	0.284	0.054

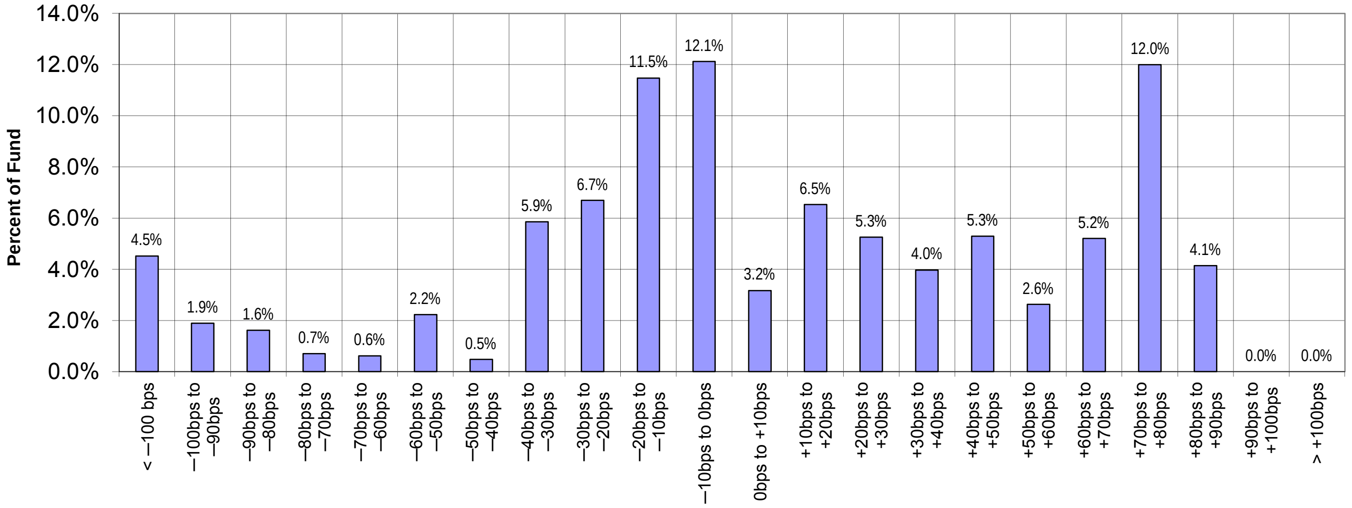
Stocks recovered in 4FQ11 on better than expected economic data and yet more central bank interventions. 3FQ11 earnings reports started off the quarter strongly and European Union leaders appeared to cook up a plan to deal with some of the sovereign debts crises. After a strong October, the markets lost a little ground in November until a positive start to the Christmas retail erased most of the month's losses. December tacked on another 1% to the S&P500's return as economic data, particularly from the U.S., came in better than expected.

Pair-wise equity return correlations remained elevated, but have been coming down since September. The stock market continues to look quite cheap versus bonds. At 817 bps, the equity risk premium generated by Merrill Lynch's DDM vs. AAA corporate yields is near its highest ever reading (data goes back to 1980). However, a "normal" recession seems no longer priced in the market. Multiples probably have an inverted "U" shaped relationship to interest rates with a peak in the 4 to 5% area.

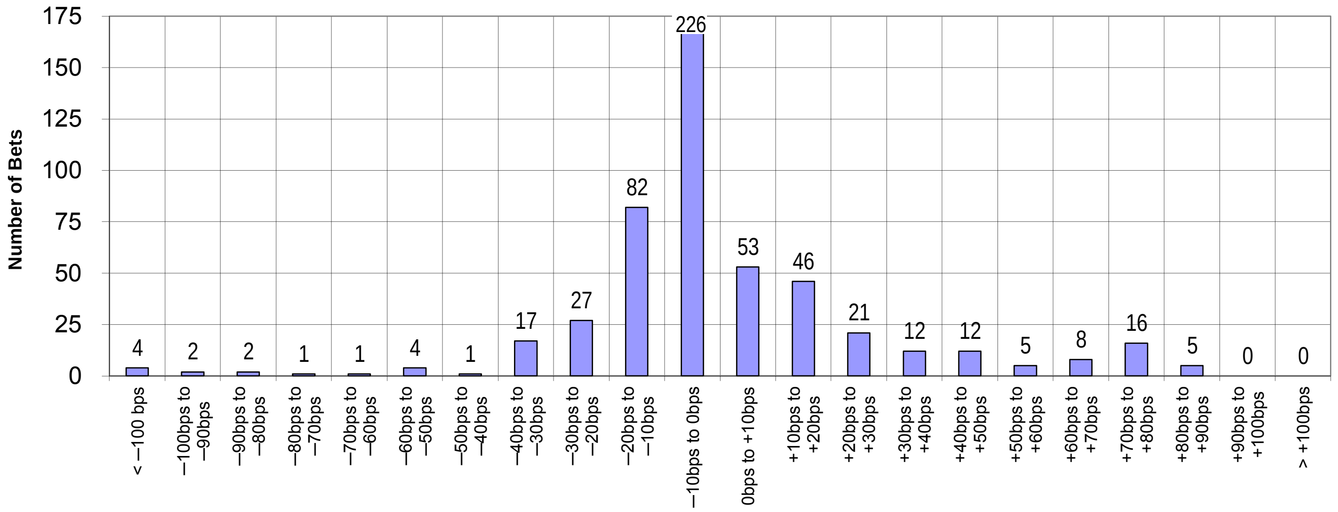
The Quant Fund turned in a +13.46% quarter, outperforming the S&P500 by +164 basis points in the three months ended December 31, 2011. The index was up +11.82%. As depicted in the insert above, the models upon which the Quant Fund relies performed well in all three months of the quarter. At the top level model, F1-F10 return spreads were +2.9%, +0.8%, and 0.3% on a month-by-month basis. By month, the monthly IC's were 0.036, 0.031, and 0.057. Trading added 33 bps to the quarter's results.

At quarter end, the Quant Fund had a projected annualized total tracking error of 1.87%, near the upper end of our comfort zone. Diversifiable or factor risk was on the high side at 1.55%. Beta was 0.999, a tad below the desired level. APE at 48.2% was within tolerance. The transfer coefficient was a very acceptable 46.6%.

Active Bets in Fund vs. S&P500, Grouped by Bet Sizes



Number of Individual Stocks in Bet Size Bins



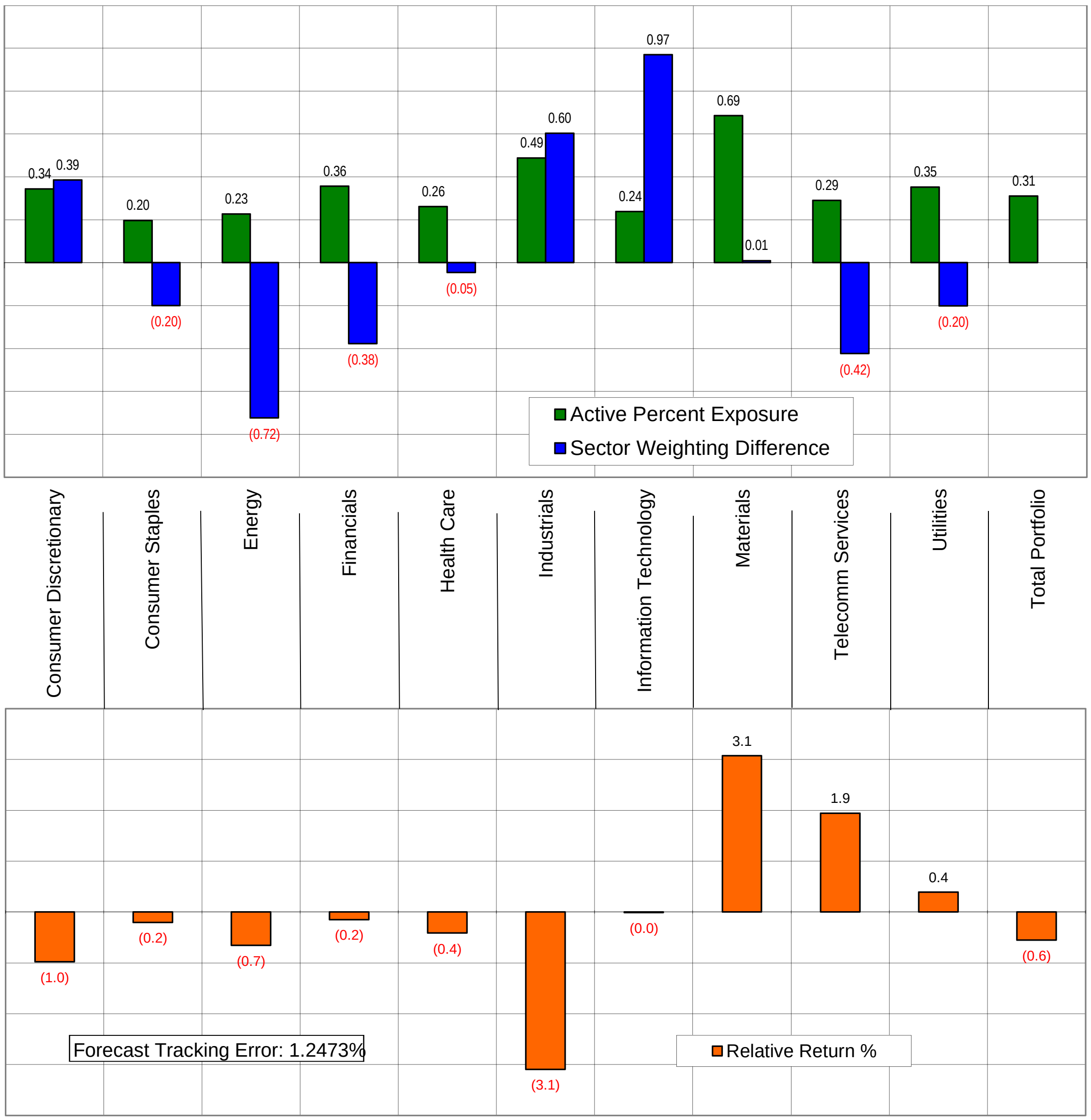
Largest Overweights by Stock in Fund

Ticker	Description	Bps Over
AMGN	Amgen Inc.	88
CELG	Celgene Corp.	83
PFE	Pfizer Inc.	82
XOM	Exxon Mobil Corp.	81
CVS	CVS Caremark Corp.	81
MO	Altria Group Inc.	78
COP	ConocoPhillips	78
LMT	Lockheed Martin Corp.	78
MCD	McDonald's Corp.	77
CVX	Chevron Corp.	77
TJX	TJX Cos.	76
ACE	ACE Ltd.	76
GD	General Dynamics Corp.	76
PM	Philip Morris International Inc.	74
TYC	Tyco International Ltd.	74
AXP	American Express Co.	73
IBM	International Business Machines Co	73
MSFT	Microsoft Corp.	73
NSC	Norfolk Southern Corp.	72
AAPL	Apple Inc.	72

Largest Underweights by Stock in Fund

Ticker	Description	Bps Under
GOOG	Google Inc. Cl A	-143
PG	Procter & Gamble Co.	-104
JNJ	Johnson & Johnson	-104
MRK	Merck & Co Inc	-101
BRK.B	Berkshire Hathaway Inc. Cl B	-98
PEP	PepsiCo Inc.	-91
QCOM	QUALCOMM Inc.	-81
SLB	Schlumberger Ltd.	-81
GE	General Electric Co.	-71
UPS	United Parcel Service Inc. Cl B	-62
DIS	Walt Disney Co.	-59
KFT	Kraft Foods Inc.	-58
AMZN	Amazon.com Inc.	-55
MMM	3M Co.	-50
BA	Boeing Co.	-48
HD	Home Depot Inc.	-39
GS	Goldman Sachs Group Inc.	-39
T	AT&T Inc.	-39
EMC	EMC Corp.	-39
LLY	Eli Lilly & Co.	-37

Large Cap Sector Fund
Roy Wellington, CFA



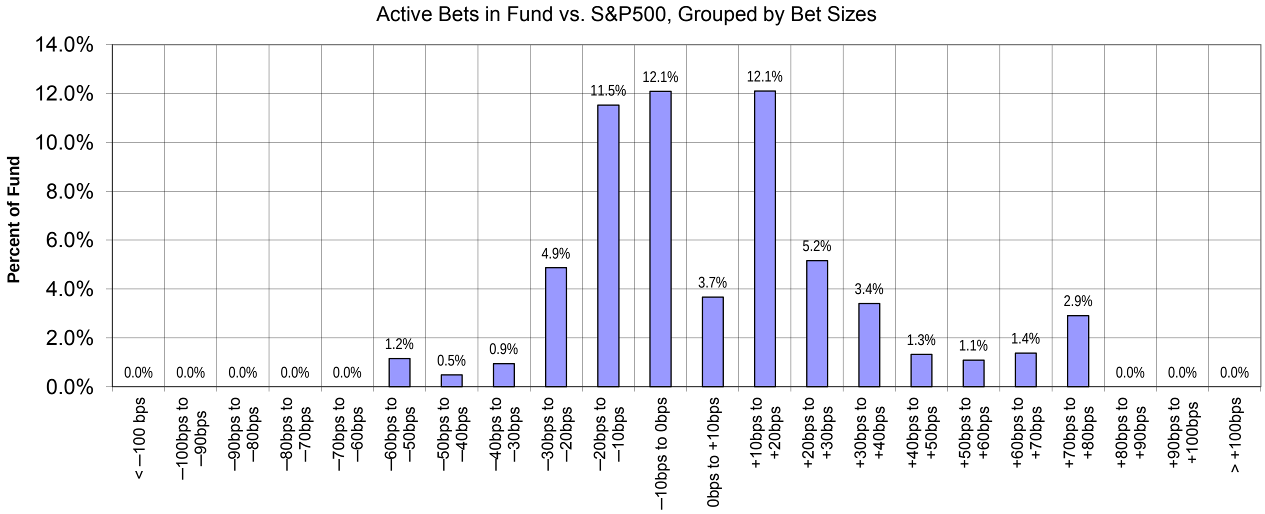
The Sector Fund had its **β** (sector exposure) meeting on February 16th. The Sector Fund is positioned for economic recovery: we neither expect a double dip nor are inflation pressures evident. Complacency continues to build toward risky assets egged on by the European Central Bank's version of quantitative easing known as "Long Term Refinancing Operation", or LTRO. LTRO, announced in December and expanded in February, is free money for banks in exchange for collateral such as illiquid loans. The main drama in asset markets is the slow, drawn out default of the Greek government, still in process. Our economy has evolved to a point where new hires can exceed layoffs, reducing the unemployment rate all the while the Obama administration and the Fed keep pushing on the "Stimulus Forever" theme. We are keeping a modest overweight to Technology and Consumer Discretionary and a modest underweight to Financials consistent with economic recovery.

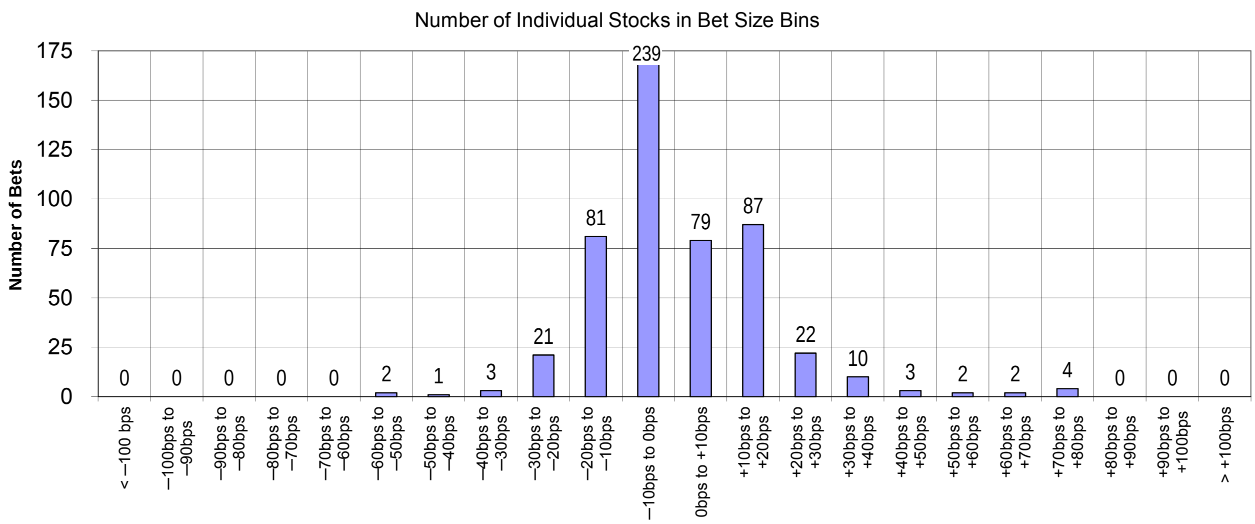
Comments around the table seemed consistent with a no recession, continued recovery, no strong feelings approach. Some sectors mentioned European exposure risk; some noted that a definite rebound from a slow 2011 is happening.

The rebound in the equity market in the fourth quarter seemed to bring a reversal of what worked in the third quarter, especially reversing fears of European recession bringing down Chinese industrial production.

A representative trade for this quarter highlights the difficulties of the quarter. TCRS owns Oracle, part of an otherwise well working Information Technology portfolio that announced trouble closing deals at the end of the quarter, going a different way from other large capitalization technology companies. TCRS was out of Parker Hannifin and other Machinery stocks most of the year while China was proving to be less of a tailwind when suddenly all seemed right with the world in October. The transition into a quality name that has worked well since the end of the quarter was messy.

Large Cap Sector Fund
Roy Wellington, CFA





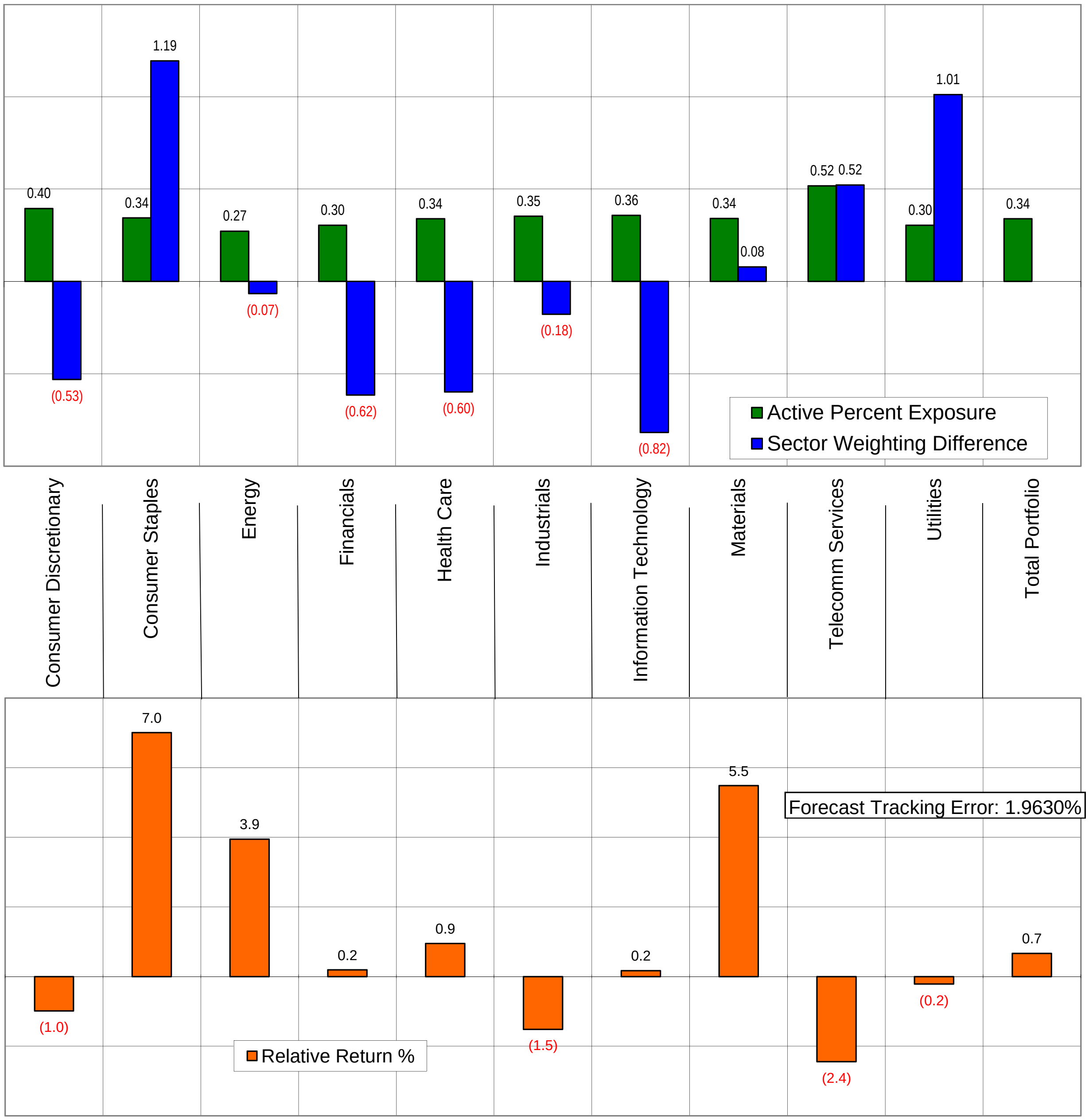
Largest Overweights by Stock in Fund

Ticker	Description	Bps Over Index Wt
UNP	Union Pacific Corp.	75
AAPL	Apple Inc.	74
HON	Honeywell International Inc.	71
TYC	Tyco International Ltd.	71
BA	Boeing Co.	69
DHR	Danaher Corp.	69
CAT	Caterpillar Inc.	58
PH	Parker Hannifin Corp.	51
NSC	Norfolk Southern Corp.	46
IBM	International Business Machines Co	45
BCE	BCE Inc.	43
INTC	Intel Corp.	39
GOOG	Google Inc. Cl A	39
IP	International Paper Co.	38
PM	Philip Morris International Inc.	37
ORCL	Oracle Corp.	34
DISH	DISH Network Corp. Cl A	33
BHI	Baker Hughes Inc.	31
AMT	American Tower Corp	31
CE	Celanese Corp. (Series A)	31

Largest Underweights by Stock in Fund

Ticker	Description	Bps Under
JNJ	Johnson & Johnson	-59
BRK.B	Berkshire Hathaway Inc. Cl B	-57
VZ	Verizon Communications Inc.	-49
V	Visa Inc.	-32
TWX	Time Warner Inc.	-32
EBAY	eBay Inc.	-31
PX	Praxair Inc.	-28
DE	Deere & Co.	-28
D	Dominion Resources Inc. (Virginia)	-27
NEM	Newmont Mining Corp.	-26
MMM	3M Co.	-26
KMB	Kimberly-Clark Corp.	-25
BAX	Baxter International Inc.	-25
FDX	FedEx Corp.	-23
EOG	EOG Resources Inc.	-23
ADP	Automatic Data Processing Inc.	-23
MON	Monsanto Co.	-22
DVN	Devon Energy Corp.	-22
PEP	PepsiCo Inc.	-21
TJX	TJX Cos.	-21

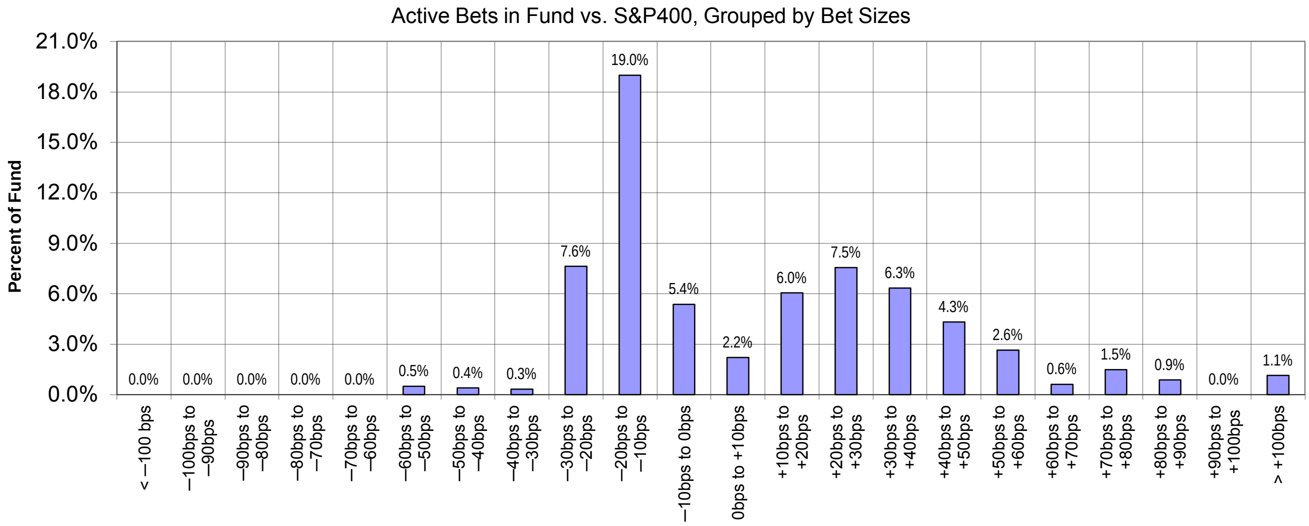
Mid–Cap Fund
Mike Keeler, CFA

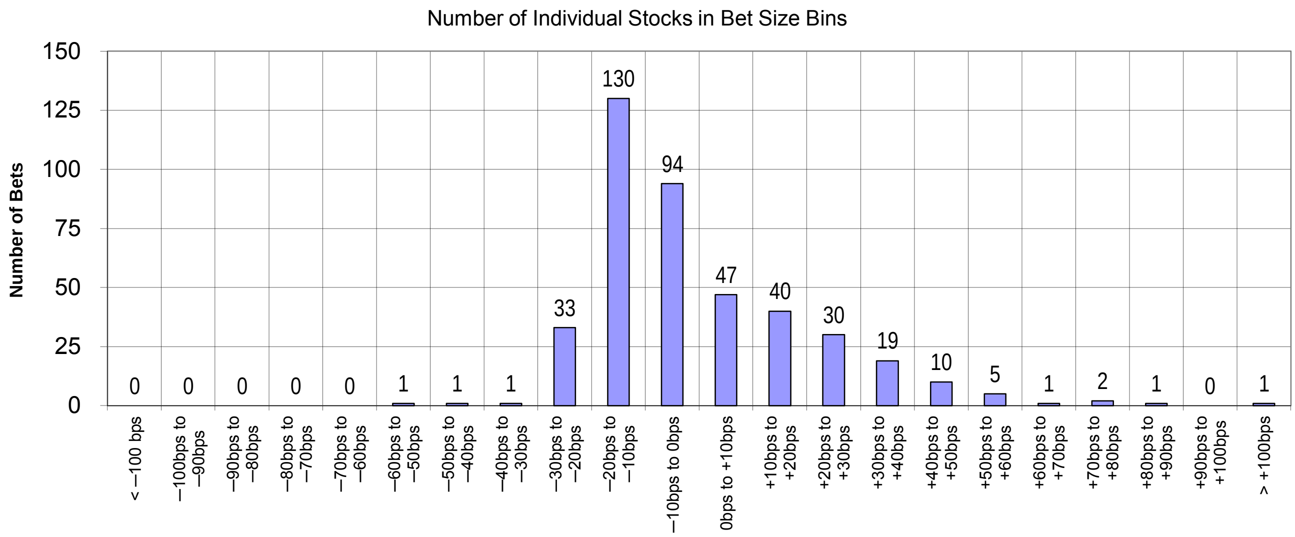


The rather odd combination of small capitalization and value factors dominated returns during the period, essentially a “risk on” quarter but heavily loaded toward the early part of the quarter and featuring a somewhat surprising quality quirk. Domestic Equities out performed the S & P 1500 composite in the quarter due to strong relative performance by the Quant Fund and a slight overweight to small caps, somewhat offset by an underweight to Mid Caps. The Fund’s overall bias toward quality also likely helped relative returns during the period. Stock selection provided all of the excess return above the benchmark during the quarter as industry sector contribution was actually negative, mostly due to an overall underweight of the Industrial sector.

The Mid Cap Fund outperformed the S & P Mid Cap 400 primarily due to good stock selection in the Consumer Staples sector (particularly not owning Green Mountain Coffee Roasters), overweight positions and good stock picking in specialty chemicals (Ashland and RPM) and Energy as well as underweights in the paper and container industries. Relative performance was negatively affected by largely missing the rally in apparel/luxury goods during the period and less than stellar stock selection in the Industrial sector. Stock selection was responsible for all of the excess return against the benchmark with industry sector allocation contributing a slight negative.

Looking ahead, expectations for 2012 are pretty reasonable, possibly a bit pessimistic as several pundits noted going into the December quarter reporting season. Early results are mixed however. Although we’re still dealing with the usual suspects globally, the domestic US economy seems to be slowly but surely improving. Combined with an improving valuation spread between small and large cap stocks the case for our small/mid cap underweight is rapidly eroding and we will be looking to add to those areas going forward.





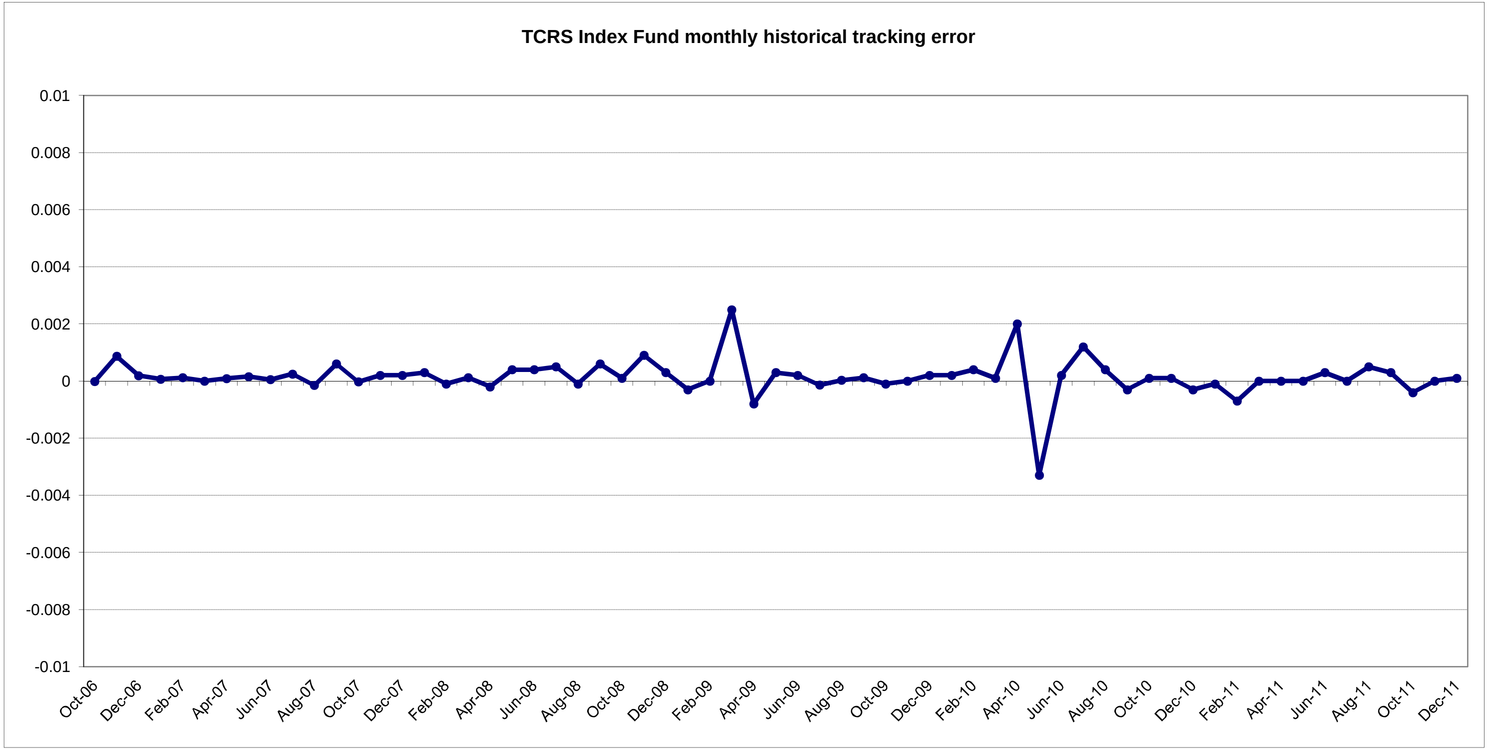
Largest Overweights by Stock in Fund

Ticker	Description	Bps Over
ADS	Alliance Data Systems Corp.	114
PRGO	Perrigo Co.	88
DLTR	Dollar Tree Inc.	75
ARW	Arrow Electronics Inc.	74
BOKF	BOK Financial Corp.	62
CHD	Church & Dwight Co.	56
PETM	PetSmart Inc.	55
KBR	KBR Inc.	51
DCI	Donaldson Co. Inc.	51
ALK	Alaska Air Group Inc.	51
ASH	Ashland Inc.	47
AAP	Advance Auto Parts Inc.	46
EQIX	Equinix Inc.	45
BWA	BorgWarner Inc.	43
DRC	Dresser-Rand Group Inc.	43
RS	Reliance Steel & Aluminum Co.	42
PXP	Plains Exploration & Production Co.	41
SFD	Smithfield Foods Inc.	41
PLT	Plantronics Inc.	41
HAIN	Hain Celestial Group Inc.	41

Largest Underweights by Stock in Fund

Ticker	Description	Bps Under
SUG	Southern Union Co.	-50
REGN	Regeneron Pharmaceuticals Inc.	-40
TIN	Temple-Inland Inc.	-33
INT	World Fuel Services Corp.	-28
UFS	Domtar Corp.	-28
JKHY	Jack Henry & Associates Inc.	-28
AMG	Affiliated Managers Group Inc.	-27
HME	Home Properties Inc.	-27
NNN	National Retail Properties Inc.	-26
HMSY	HMS Holdings Corp.	-26
FBHS	Fortune Brands Home & Security In	-25
WRI	Weingarten Realty Investors	-25
ANSS	Ansys Inc.	-25
CLC	CLARCOR Inc.	-24
TFX	Teleflex Inc.	-24
WWD	Woodward Inc.	-23
TRN	Trinity Industries Inc.	-23
CNQR	Concur Technologies Inc.	-23
CNL	Cleco Corp.	-22
FOSL	Fossil Inc.	-22

S&P 500 Index Fund
Daniel Crews, CFA



Top Ten Holdings as of December 31, 2011

Ticker	Name	Portfolio Weight	S&P 500 Weight	Difference
XOM	Exxon Mobil Corp.	3.54	3.57	-0.03
AAPL	Apple Inc.	3.30	3.31	-0.00
IBM	International Business Machines Corp.	1.95	1.90	0.05
CVX	Chevron Corp.	1.85	1.86	-0.01
MSFT	Microsoft Corp.	1.71	1.71	0.00
GE	General Electric Co.	1.65	1.66	-0.01
PG	Procter & Gamble Co.	1.60	1.61	-0.01
T	AT&T Inc.	1.56	1.57	-0.01
JNJ	Johnson & Johnson	1.56	1.57	-0.02
PFE	Pfizer Inc.	1.44	1.46	-0.02

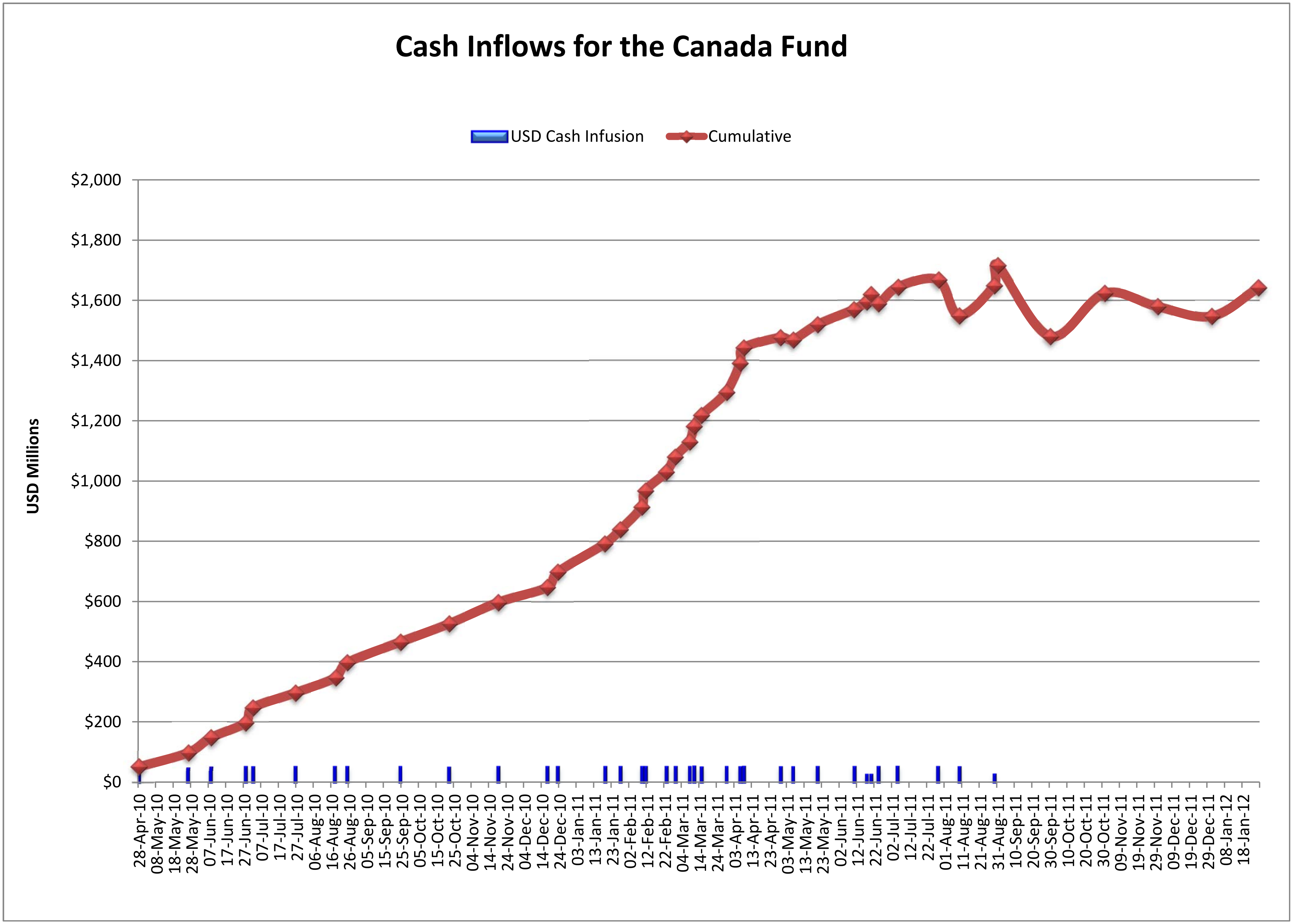
Ten Largest Overweights and Underweights as of Dec. 31, 2011

Ticker	Name	Portfolio Weight	S&P 500 Weight	Difference
ORCL	Oracle Corp.	1.01	0.89	0.12
IBM	International Business Machines Corp.	1.95	1.90	0.05
XOM	Exxon Mobil Corp.	3.54	3.57	-0.03
PFE	Pfizer Inc.	1.44	1.46	-0.02
EMR	Emerson Electric Co.	0.32	0.30	0.02
KO	Coca-Cola Co.	1.38	1.40	-0.02
WAG	Walgreen Co.	0.28	0.26	0.02
JNJ	Johnson & Johnson	1.56	1.57	-0.02
PM	Philip Morris International Inc.	1.18	1.20	-0.02
CVX	Chevron Corp.	1.85	1.86	-0.01

Tracking Error	
Forecasted Tracking Error	0.04%
Historical Tracking Error	0.23%
Value at Risk	$1,460,946

Comments:

- Index Fund experienced the following funding flows in calendar 3Q11: $250 million inflow on 8/3/11, $250 million inflow on 8/8/11, $250 million inflow on 8/12/11.
- Index Fund experienced the following funding flows in calendar 2Q11: $150 million outflow on 4/5/11.
- Fund sold $350 million in February to reduce overall plan equity allocation. February alpha number of (0.07%) was a result of trading impact for the allocation changes.
- Note on December 31 reported portfolio data: S&P made changes ot the index on the close of 12/31/10 that were not incorporated into the fund until the next liquid trading day. Therefore, the risk forecasts and underweight/overweight table from the 12/31/10 IAC report are overstated. The performance impact from the timing discrepancy was nil.
- Due to a critical trading error in the issue CF Industries (Ticker: CF) as well as two unusually beneficial portfolio trades, Index Fund realized abnormally high tracking error in the 4Q FY10 period. The trading error was unwound opportunistically and processes were established to prevent similar errors in the future.
- Index Fund experienced the following funding flows in calendar 2Q10: $200 million outflow on 4/29/10, $250 million outflow on 4/16/10.
- Index Fund experienced the following funding flows in calendar 3Q09: $100 million inflow on 9/24/09, $100 million inflow on 7/29/09.
- April 2009 witnessed relatively large negative deviation from the index (-7 bps) due to a double corporate action by Time Warner, large banks raising substantial amounts of equity following the release of the infamous "stress test" results, the exit of Noble (which did not behave according to the empirically normative pattern for S&P 500 exclusions), and the tactical holding of Citi preferred shares rather than Citi common.
- Extraordinary positive tracking error was evident in the fund during March 2009 (25 bps). The deviation from benchmark returns in March primarily relates to good timing on a trade conducted March 2 and to class action litigation income posted to the fund.


Cash Inflows for the Canada Fund
USD Cash Infusion
Cumulative
USD Millions
$2,000
$1,800
$1,600
$1,400
$1,200
$1,000
$800
$600
$400
$200
$0
28-Apr-10
08-May-10
18-May-10
28-May-10
07-Jun-10
17-Jun-10
27-Jun-10
07-Jul-10
17-Jul-10
27-Jul-10
06-Aug-10
16-Aug-10
26-Aug-10
05-Sep-10
15-Sep-10
25-Sep-10
05-Oct-10
15-Oct-10
25-Oct-10
04-Nov-10
14-Nov-10
24-Nov-10
04-Dec-10
14-Dec-10
24-Dec-10
03-Jan-11
13-Jan-11
23-Jan-11
02-Feb-11
12-Feb-11
22-Feb-11
04-Mar-11
14-Mar-11
24-Mar-11
03-Apr-11
13-Apr-11
23-Apr-11
03-May-11
13-May-11
23-May-11
02-Jun-11
12-Jun-11
22-Jun-11
02-Jul-11
12-Jul-11
22-Jul-11
01-Aug-11
11-Aug-11
21-Aug-11
31-Aug-11
10-Sep-11
20-Sep-11
30-Sep-11
10-Oct-11
20-Oct-11
30-Oct-11
09-Nov-11
19-Nov-11
29-Nov-11
09-Dec-11
19-Dec-11
29-Dec-11
08-Jan-12
18-Jan-12

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

Periods Ending December 31, 2011

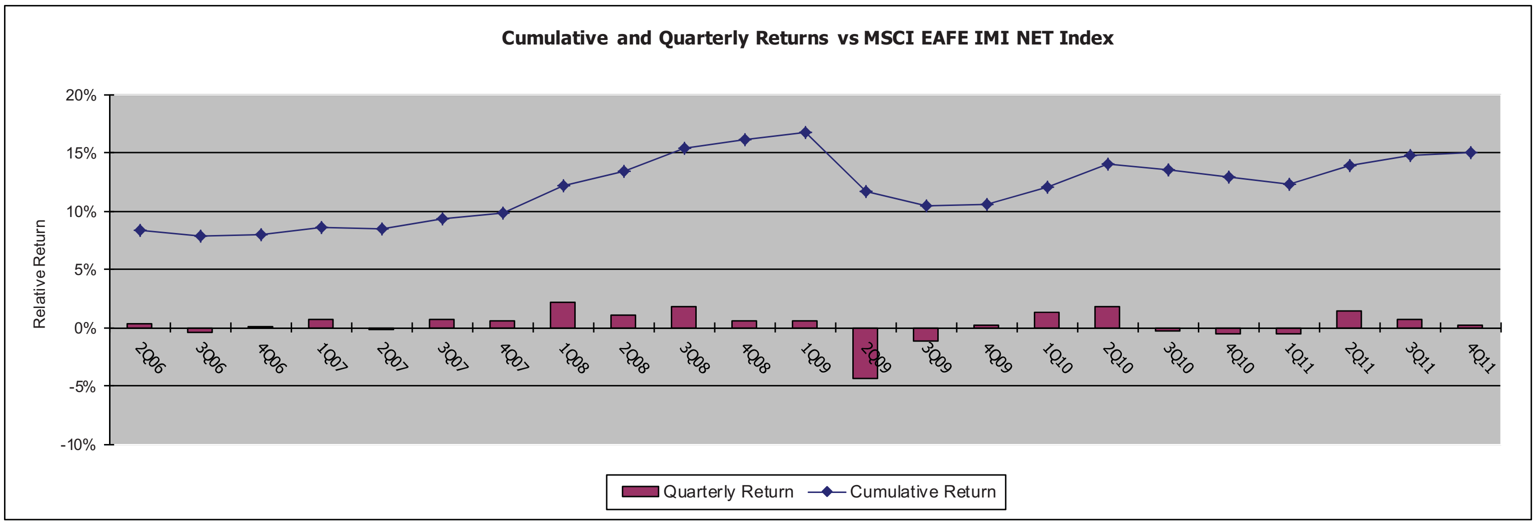
International Manager Performance Comparison

Manager returns for the quarter ending December 31, 2011

Manager	Manager Return	Benchmark	Benchmark Return
American Century	5.99	MSCI EAFE Small Cap NET	-0.56
Baring Asset Mgmt	4.29	MSCI EAFE NET Index	3.33
GE Asset Mgmt	4.93	MSCI Europe NET Index	5.39
Marathon	2.67	MSCI EAFE NET Index[2]	3.33
Pacific Indexed Port[5]	-0.29	MSCI Pacific NET Index[1]	-0.30
PanAgora	3.31	MSCI EAFE NET Index	3.33
Pyramis	0.30	MSCI EAFE Small Cap NET	-0.56
TT International	2.91	MSCI EAFE NET Index	3.33
Walter Scott	2.00	MSCI EAFE NET Index[4]	3.33
International	3.09	MSCI EAFE IM Net Index[3]	2.86

Manager returns for five years ending December 31, 2011

Manager	Manager Return	Benchmark	Benchmark Return
American Century		MSCI EAFE Small Cap NET	
Baring Asset Mgmt		MSCI EAFE NET Index	
GE Asset Mgmt		MSCI Europe NET Index	
Marathon	-0.47	MSCI EAFE NET Index[2]	-4.72
Pacific Indexed Port[5]	-3.90	MSCI Pacific NET Index[1]	-3.43
PanAgora	-3.42	MSCI EAFE NET Index	-4.72
Pyramis		MSCI EAFE Small Cap NET	
TT International		MSCI EAFE NET Index	
Walter Scott	2.07	MSCI EAFE NET Index[4]	-4.72
International	-2.39	MSCI EAFE IM Net Index[3]	-4.39



[1] *Effective as of 7/1/04; prior was MSCI AC Asia Pacific Free Index.*

[2] *Effective as of 5/19/06; prior was MSCI Europe Index.*

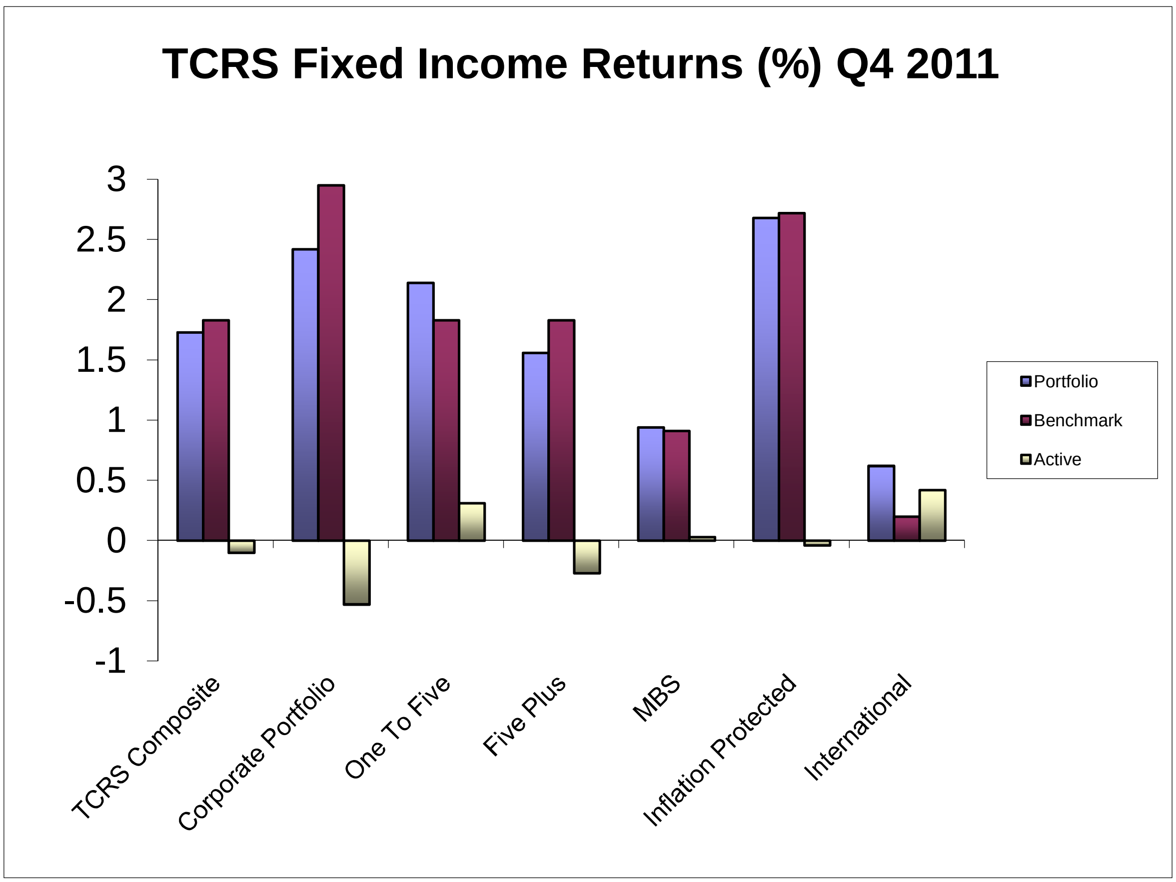
[3] *Effective as of 10/1/08; prior was MSCI EAFE NET Index.*

[4] *Effective as of 2/2/09; prior was MSCI Europe Index.*

[5] *Performance was attributable to Amundi through 9/3/10; portfolio managed by TCRS staff afterward.*

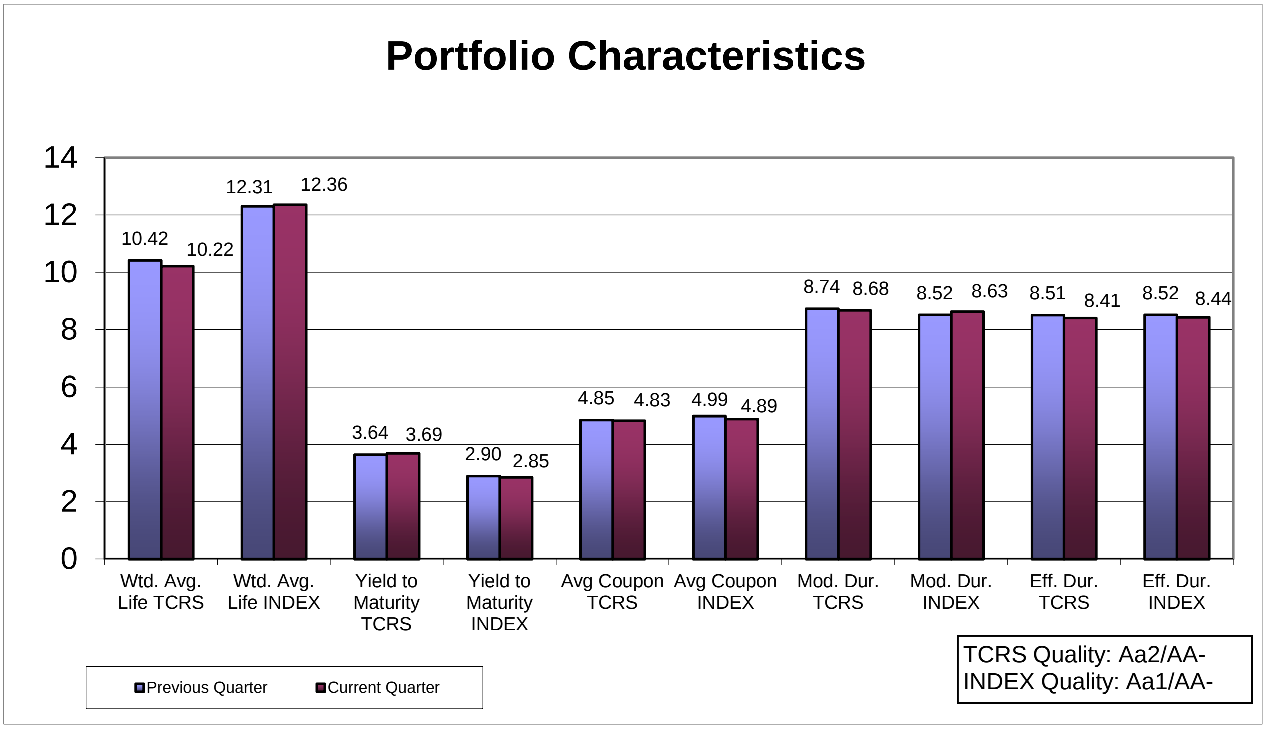
Page is intended to be blank

Portfolio	Value (Yield Book) ($MMs)	Portfolio Return Q4	Benchmark Return Q4	Active Return Q4
TCRS Domestic Fixed Income Composite	$9,834	1.73	1.83	(0.10)
Corporate Portfolio	$3,281	2.42	2.95	(0.53)
Government One To Five Years	$1,218	2.14	1.83	0.31
Government Five Plus Years	$1,822	1.56	1.83	(0.27)
Mortgage Portfolio	$3,461	0.94	0.91	0.03
TCRS Inflation Protected Securities	$2,553	2.68	2.72	(0.04)
TCRS International	$349	0.62	0.20	0.42

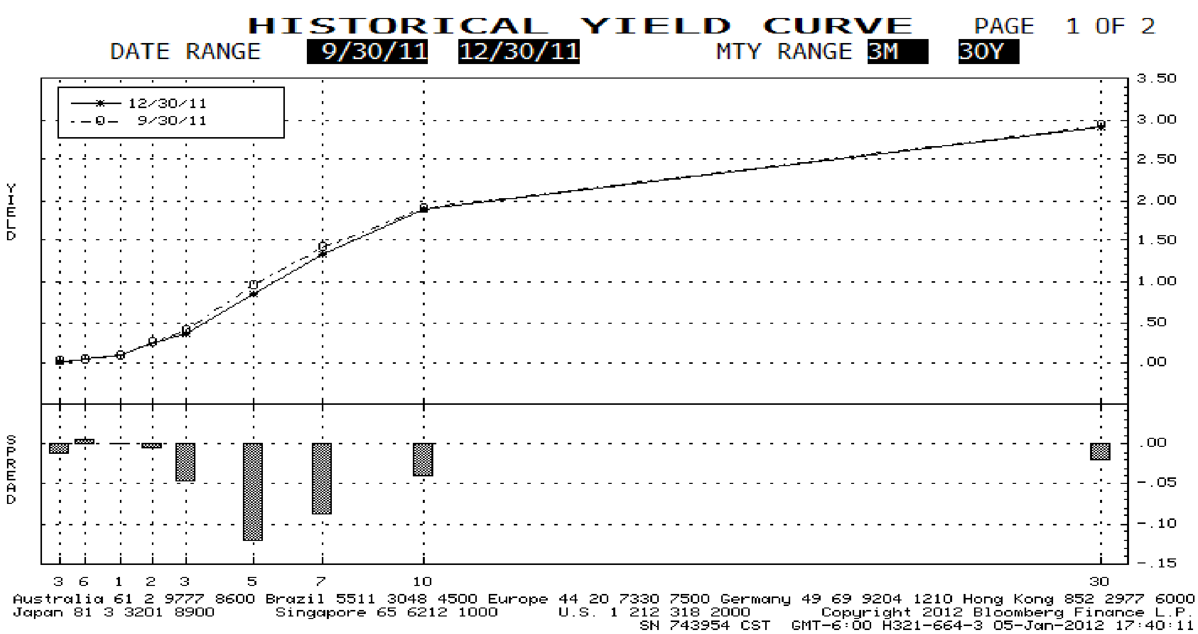


Note: All positions and market values are as of December 30, 2011

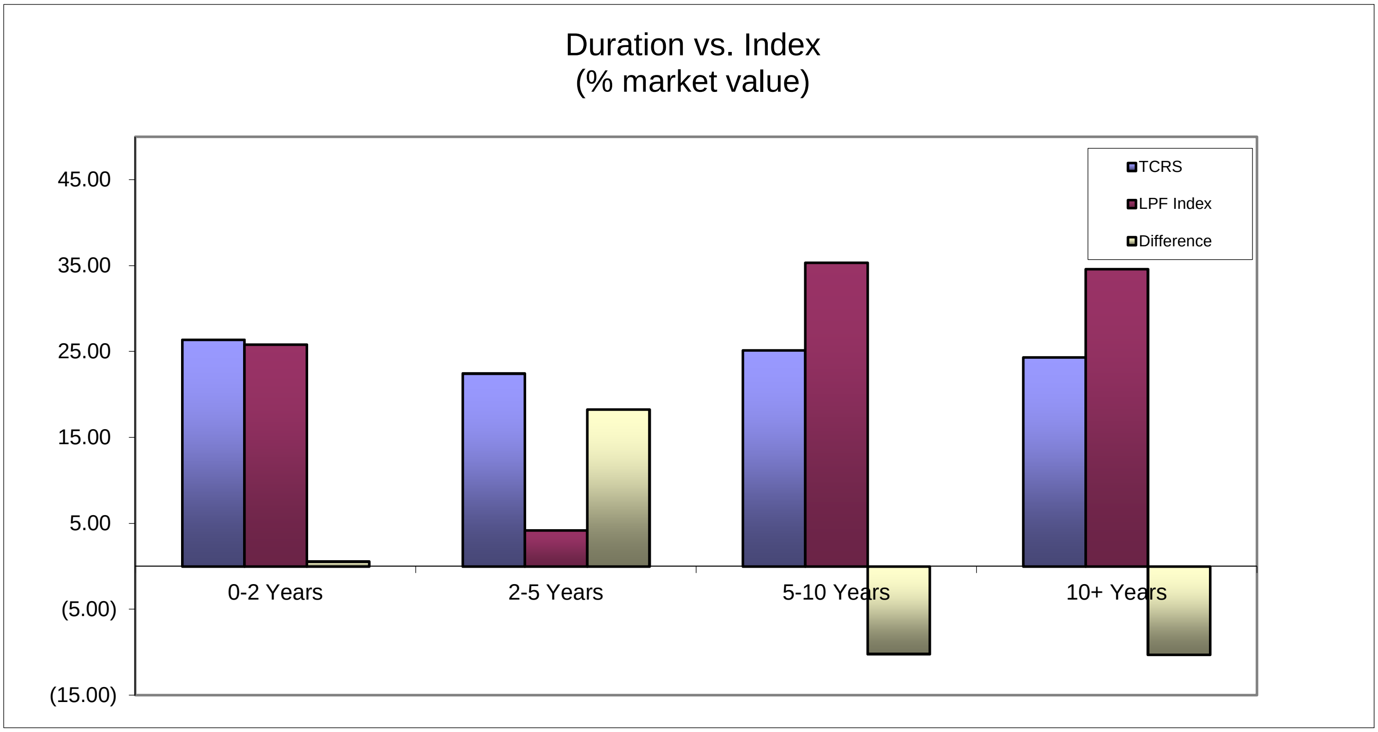
Characteristics show small bias toward yield and similar interest rate risk

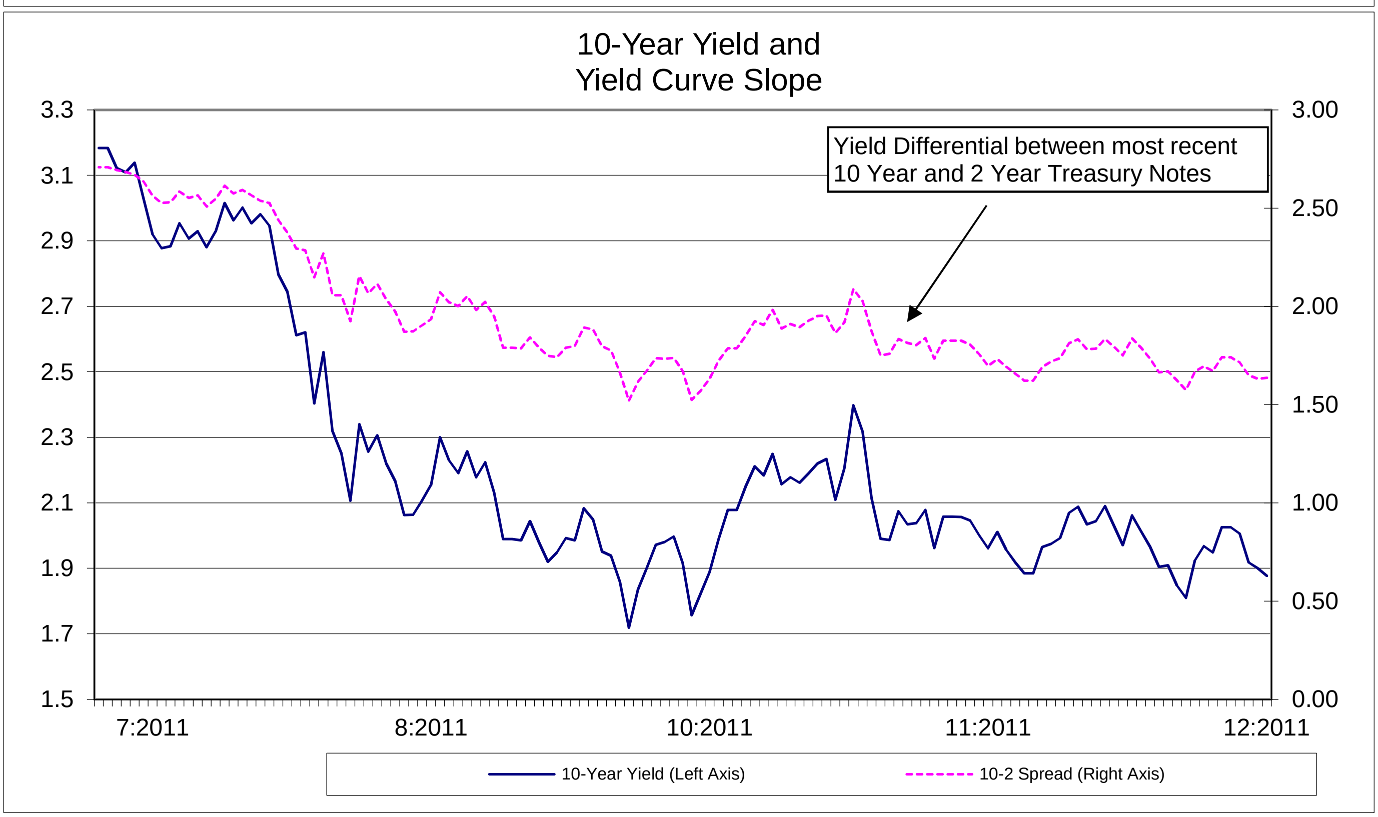


Yields fell and the curve steepened

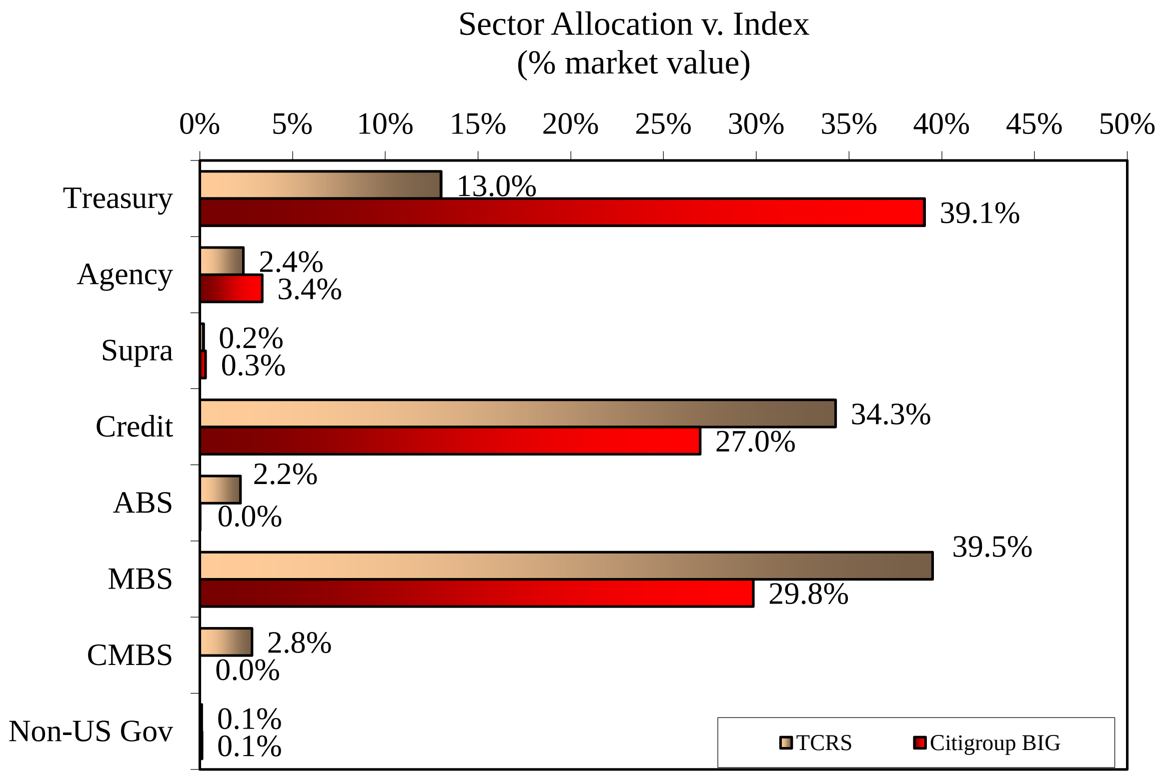


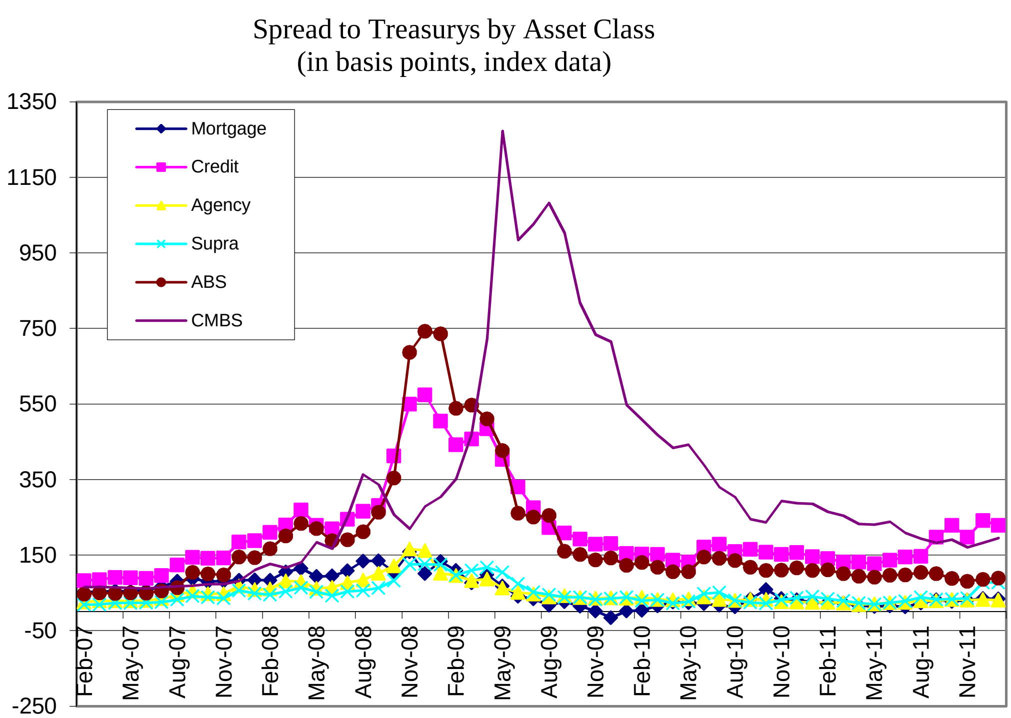
Curve positioning reflects overweight to MBS





source: Bloomberg



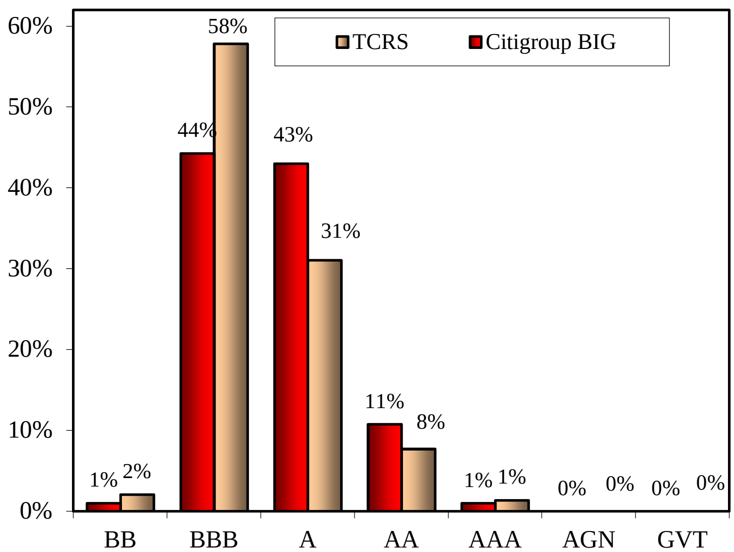


source: Yield Book

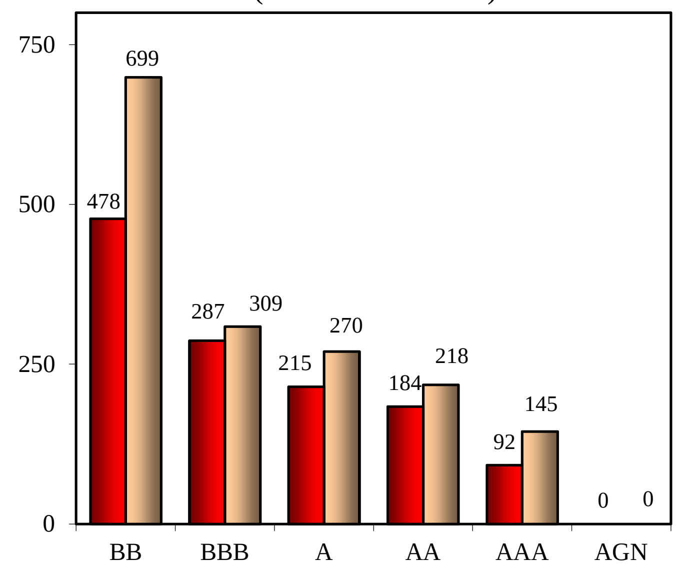
Spread widened during the quarter.

TCRS spreads vs. index were higher than the index, reflecting expectation of a lower risk environment

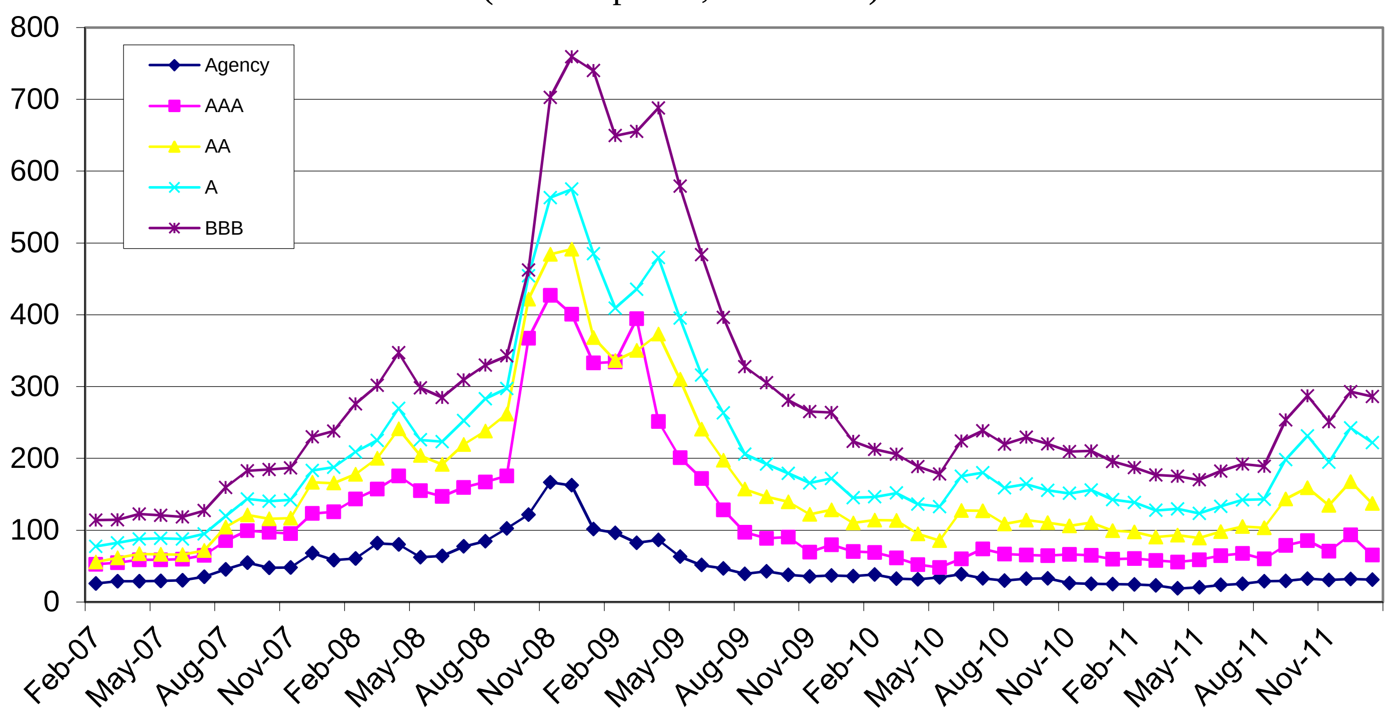
Credit Allocation v. Index
(% market value as of December 31)



OAS by Credit Allocation
(as of December 31)



Spread to Treasury by Credit Rating
(in basis points, index data)



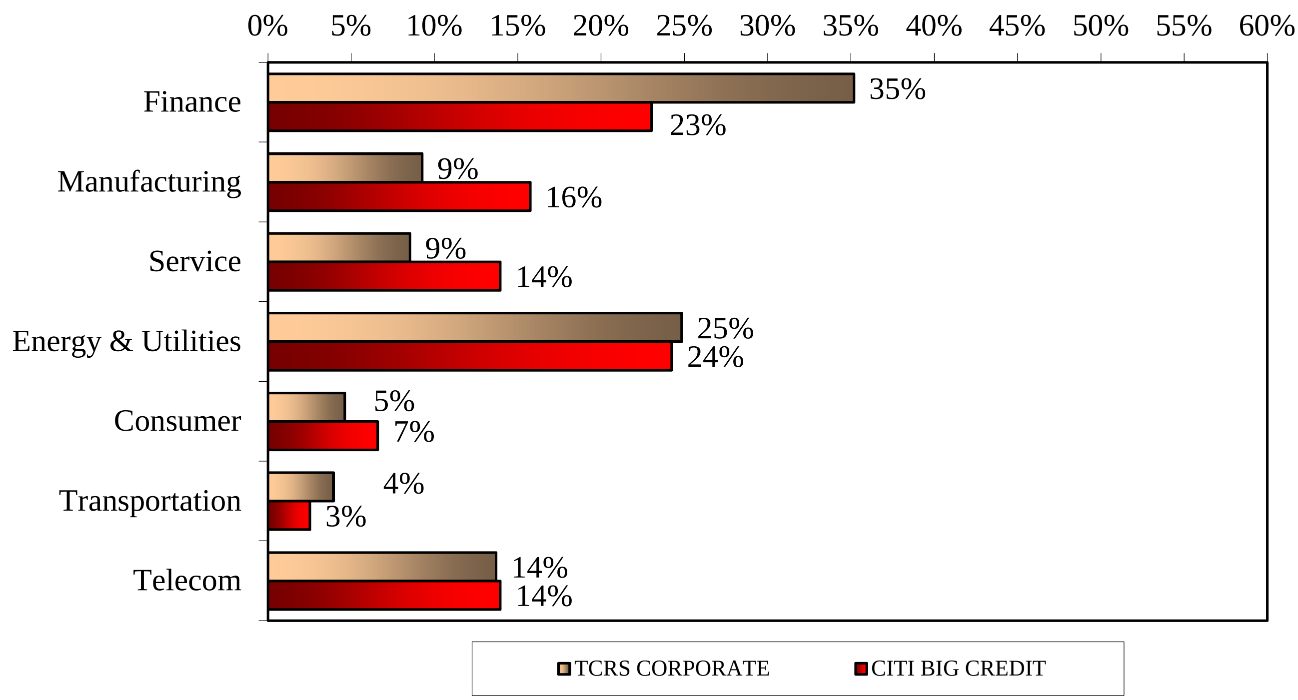
source: Yield Book

Finance exposure expanded in place of utilities and manufacturing

Top 5 Credit Holdings (by Market Value)	MktVal	% MktVal
GENERAL ELECTRIC CO	108,000	1.1
BANK OF AMERICA	87,833	0.9
GOLDMAN SACHS GROUP	84,493	0.9
TIME WARNER CABLE INC	70,577	0.7
CITIGROUP	70,447	0.7

Top 5 Credit Holdings (by Dollar Duration)	$ Duration	% $ Duration
GENERAL ELECTRIC CO	98.40	1.2
TIME WARNER CABLE INC	78.03	0.9
AT&T	71.47	0.9
GOLDMAN SACHS GROUP	68.41	0.8
COMCAST CORP	62.86	0.8

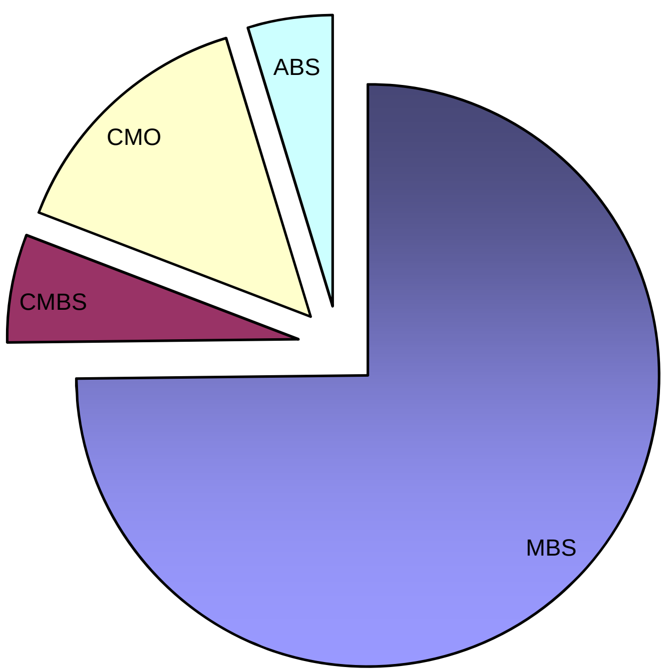
Sector Allocation v. Index
(% market value)



Securitized Product Breakdown
Andrew Palmer, CFA

	Market Value ($MM - Yield Book)	TCRS % of portfolio	CITI % of portfolio	Difference
Agency Mortgage Backed Securities	$3,444,416	35.1	29.8	5.3
GNMA				
15-Yr	$0	0.0	0.1	-0.1
30-Yr	$387,834	4.0	6.8	-2.9
FNMA				
10-, 15- & 20-Yr	$343,057	3.5	2.4	1.2
30-Yr	$1,495,523	15.2	11.5	3.7
FHLM				
15-Yr	$52,420	0.5	1.6	-1.0
30-Yr	$977,732	10.0	7.5	2.5
Agency Hybrid	$187,850	1.9	0.0	1.9
Commercial Mortgage Backed Securities	$275,772	2.8	0.0	2.8
CMO and Non Agency Passthroughs	$665,882	6.8	0.0	6.8
Asset Backed Securities	$215,992	2.2	0.0	2.2
Total Securitized Product	**$4,602,062**	**46.9**	**29.9**	**17.0**

Percent of Securitized Product



Portfolio Return:	0.62%
Citigroup Non-US G5 Index:	0.20%
Active Return:	**0.42%**

TCRS

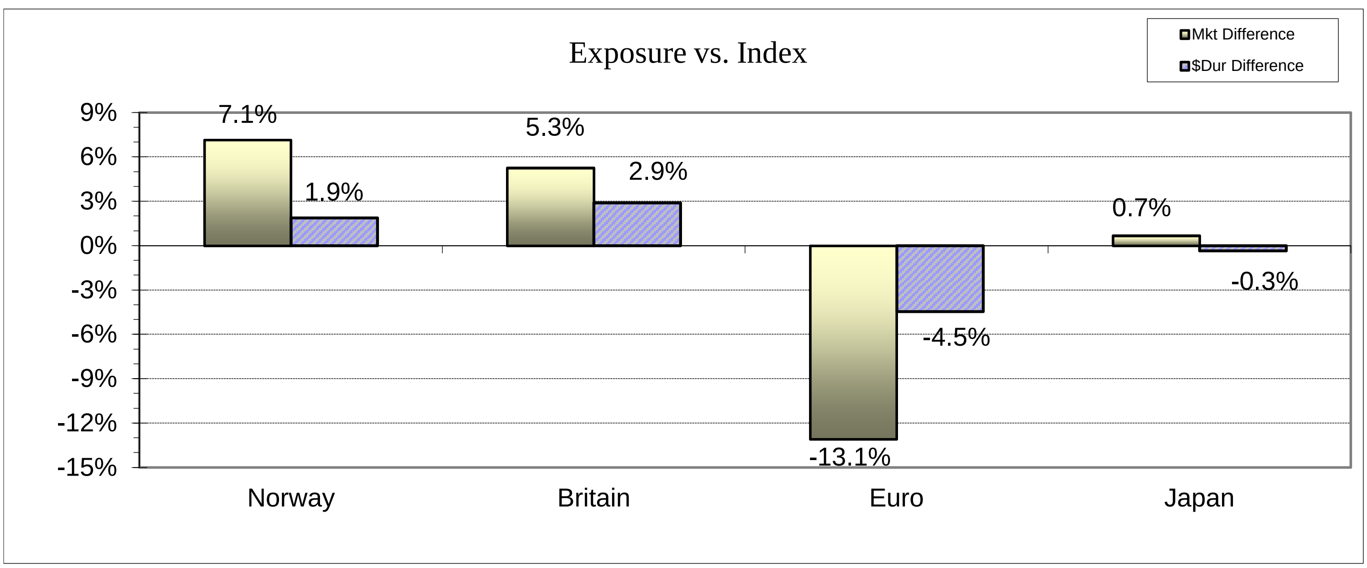
	Yield	M. Dur	Percent of Value	Percent of $Dur
Norway	2.28	2.10	7.1%	1.9%
Britain	2.27	8.54	16.6%	17.8%
Euro	2.75	11.52	11.6%	16.9%
Japan	0.76	7.78	64.6%	63.4%
	1.35	7.94	100.0%	100.0%

Citigroup G5 Sovereign Index (ex-US)

	Yield	Dur	Percent of Value	Percent of $Dur
Britain	1.87	9.97	11.3%	14.9%
Euro	1.69	6.52	24.7%	21.3%
Japan	0.72	7.52	64.0%	63.7%
	1.09	7.55	100.0%	100%

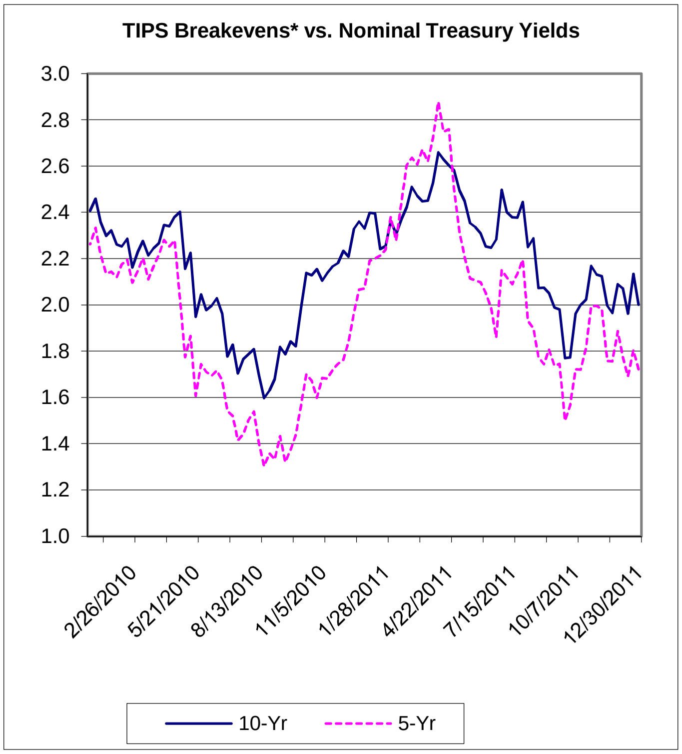
Difference

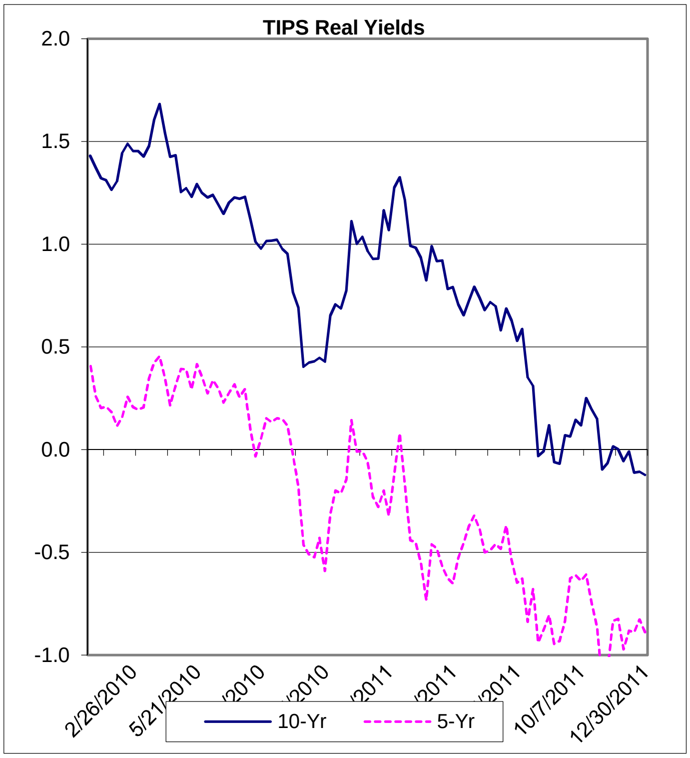
	Value Differ	M. Dur Differ	$ Dur Differ
Norway	7.1%	2.1	1.9%
Britain	5.3%	-1.4	2.9%
Euro	-13.1%	5.0	-4.5%
Japan	0.7%	0.3	-0.3%
	0.0%	0.4	0.0%



Portfolio Value (Yield Book):	$2,552,808,455
Portfolio Return:	2.68%
Citigroup ILSI Index:	2.72%
Active Return:	**-0.04%**

	% Market Value by Duration		
	TCRS	CITI	Difference
0-2	0.24	0.20	0.05
2-4	0.77	0.76	0.00
4-6	0.60	0.96	-0.36
6-8	0.50	0.45	0.05
8-10	1.63	2.08	-0.45
10+	1.68	1.07	0.61

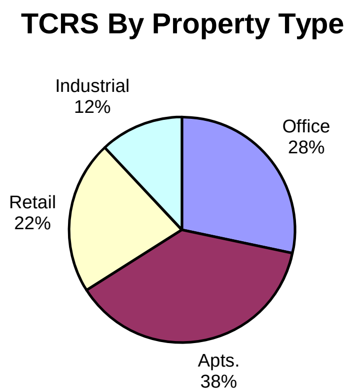


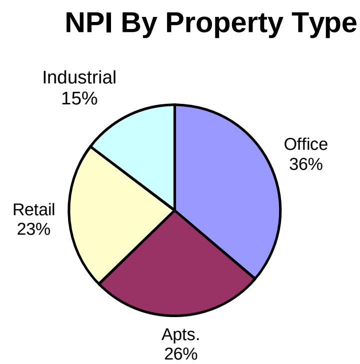


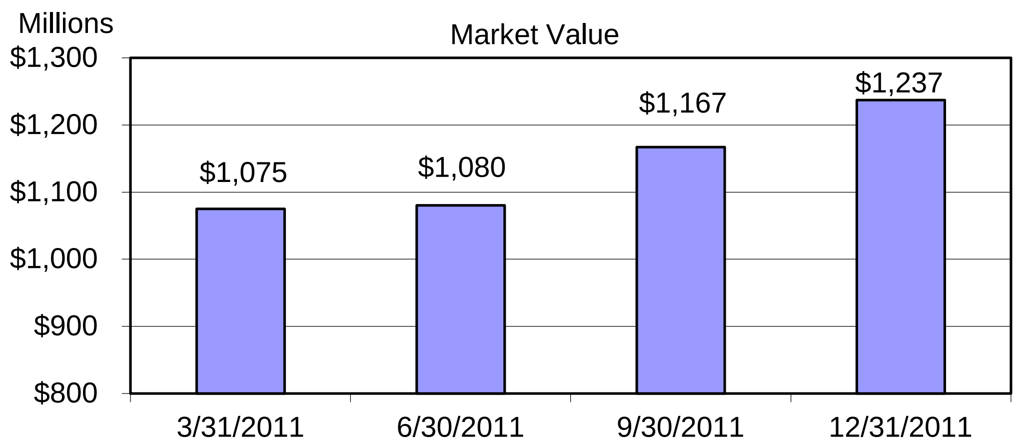
* The "breakeven" rate is the expected rate of inflation at which investment in TIPS yield the same return as investment in Treasuries

Source: Bloomberg

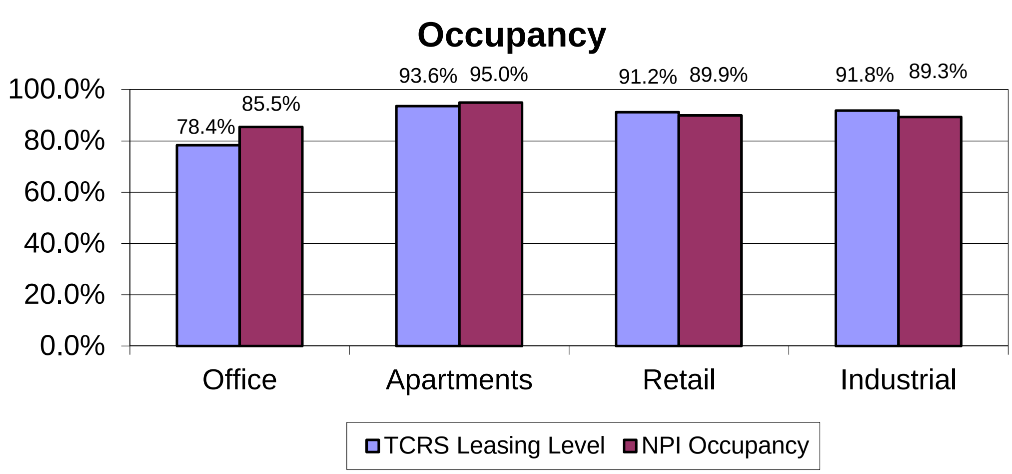
Page is intended to be blank



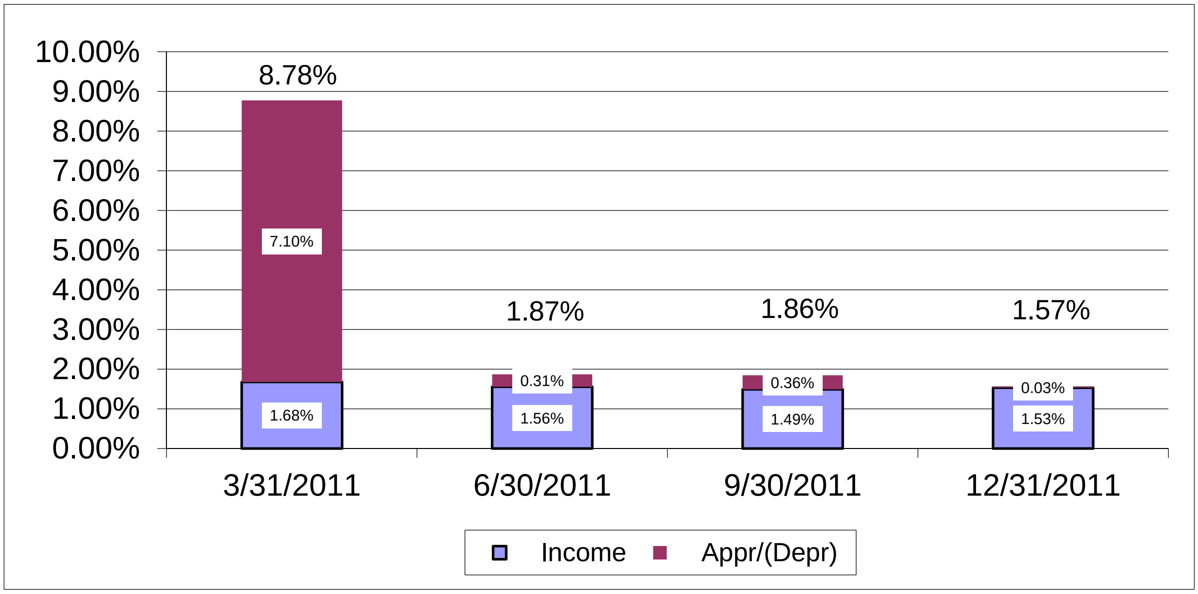




*One acquisition totaling $22.45 million occurred in the most recent quarter.

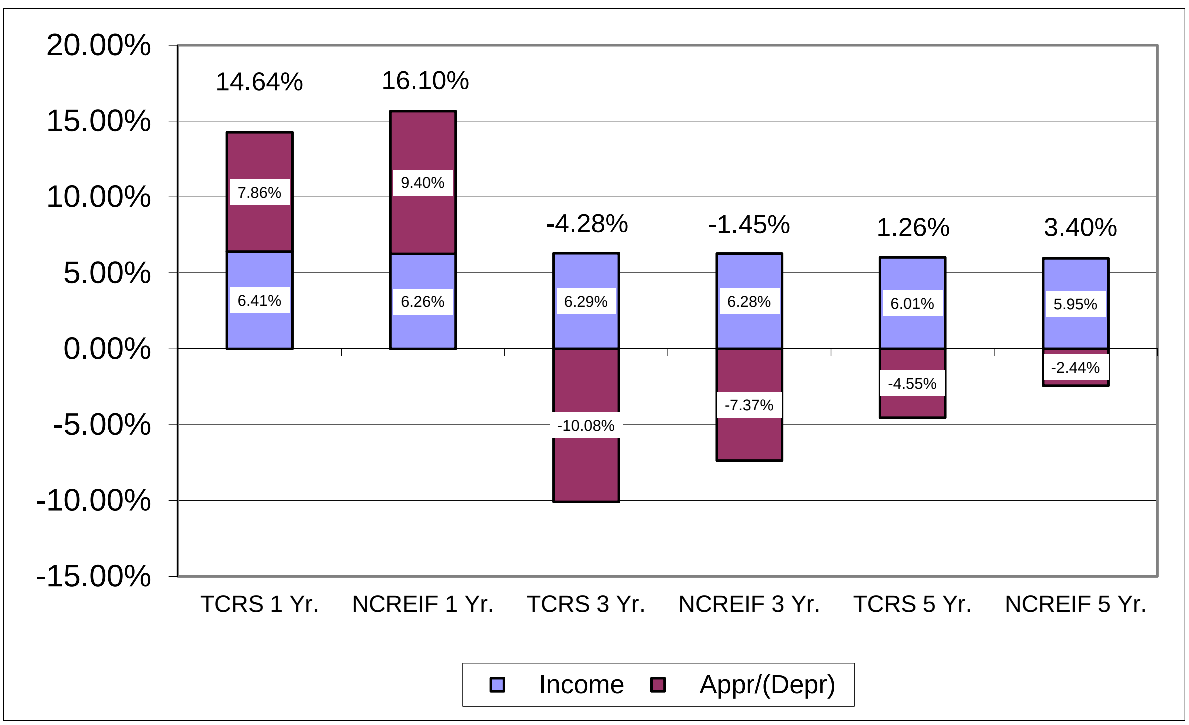


The NPI is the National Property Index of the National Council of Real Estate Investment Fiduciaries (the index used for US core properties).



All returns shown above are reported one quarter in arrears.

Budgeted Annual Income Return for calendar year 2011 (excluding REITs). 5.99%



All returns shown above are reported one quarter in arrears.

Tennessee Consolidated Retirement System
Private Equity Program
Fiscal Q2 2012 Update
Lamar Villere, CFA

Performance

We have finalized our fiscal Q1:2012 results (9/30/11), and are pleased to report that the program continues to show positive returns. As of that date, the portfolio value had reached $108.8 million, with 19.2% in buyout funds, 48.7% of that in credit funds, and 32.1% in venture funds. This breakdown is inconsistent with long term expectations for two primary reasons. First, TCRS seeks to partner with the top firms in each category, many of whom are not currently fundraising. Second, Hellman & Friedman VII, TCRS's largest commitment to date, only began calling capital in August 2011 despite the fund closing in 2009.

The table below breaks out the $108.8 million of TCRS private equity net asset value by sub-asset class. Essentially, the Net Asset Value percentage is a photograph of the program as of 9/30/11, while the Economic Exposure is an indication of where the program is heading. Note that the target exposure to secondaries is 0%-10%, and that secondaries are typically dominated by buyouts. As the table indicates, the portfolio is significantly below target in terms of buyout allocation; this is a primary focus over the coming year.

As of 9/30/11	**Target**	**Net Asset Value**	**Economic Exposure***
Buyout	45.0%	19.2%	29.0%
Credit	25.0%	48.7%	42.9%
Venture	20.0%	32.1%	28.1%
Secondaries	10.0%	0.0%	0.0%
TCRS PE Overall	**100.0%**	**100.0%**	**100.0%**

**Economic exposure is defined by net asset value + unfunded commitments.*

The table on the following page provides a brief overview of performance thus far. Please note that this performance is not particularly meaningful, nor will it be meaningful for several years. It is Staff's and Cambridge's expectation that performance will likely be weak in the early years of the program as the j-curve effect negatively impacts the portfolio performance.

Overall performance in the portfolio was weak in the quarter across all three segments. Within venture capital and buyouts, the weakness was primarily due to significant capital calls and management fees leading to a j-curve impact. Within credit, the primary driver of the negative performance was the overall weakness in credit markets.

Generally, though, we are pleased to see that the portfolio is outperforming its benchmark of S&P 500 plus 3% across the trailing quarter, year, and since inception.

IRR as of 9/30/11	**Quarter**	**Trailing 1 Year**	**Since Inception**
Buyout	-7.1%	21.3%	-5.6%
Credit	-8.1%	-5.0%	-0.2%
Venture	-0.6%	-2.7%	18.3%
TCRS PE Overall	**-5.5%**	**5.1%**	**6.3%**
S&P 500 + 3%	*-13.0%*	*-5.4%*	*-0.8%*

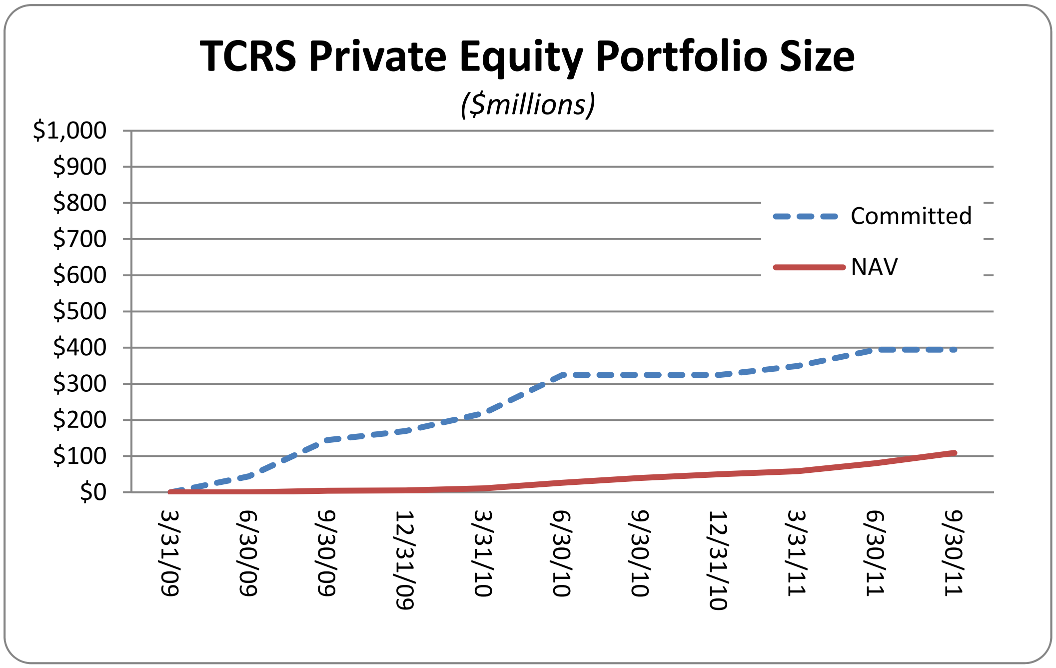
Looking Ahead to Fiscal Q2 2012 Results

Based on the handful of reporting figures that have arrived thus far, Staff anticipates a stronger quarter, led by a recovery in the credit markets.

Commitments

In December, TCRS committed $25 million to General Catalyst VI, a venture capital fund. Also in December, TCRS committed $50 million to Denham VI, a fund focused on energy and commodities.

The following chart shows the growth of the private equity program since inception in terms of cumulative commitments and net asset value. As the chart illustrates, there is a significant lag between dollars committed and their impact on net asset value. Note that based on overall TCRS 12/31/11 balance of approximately $33 billion, the target size of the private equity portfolio is roughly $1 billion of NAV (3%).



Fund Pipeline

TCRS closed on three venture capital commitments in January, but is not yet able to disclose the identity of those firms. Looking ahead, TCRS staff will spend much of calendar 2012 focused on increasing the portfolio's allocation to buyouts, as well as refining the long term strategy for credit investing.

TCRS Equity Derivative Report

Domestic Stock Index Futures
Roy Wellington, CFA

Domestic Stock Index Futures Transaction Log

Date	B/S	Contracts			Broker	Price	Total	Reason
Begin	B	5,950	Russell 2000	Dec 2011	Citigroup	641.5000	381,692,500	
Trades								
12/9/2011	S	5,950	Russell 2000	Dec 2011	Citigroup	747.0000	(444,465,000)	2a
12/9/2011	B	5,950	Russell 2000	Mar 2012	Citigroup	743.2000	442,204,000	2b
Contracts Outstanding on September 30, 2011								
End	B	5,950	Russell 2000	Mar 2012	Citigroup	738.8000	439,586,000	
					Total 2Q FY2012	$	62,445,250	

1 Move equity allocation towards allocation target.
2a Swap to next contract.
2b Swap from earlier contract.

Strategy: TCRS is replicating a small company stock portfolio using Russell 2000 index futures. The Russell 2000 future plus cash should produce a return equal to the Russell 2000 Index. TCRS utilizes index futures to its advantage to make timely investments and to gain small cap exposure as desired. Our exposure to small cap remains below the policy target.

TCRS also believes that it can add value to the underlying equity index return by investing cash allocated to the strategy in better (in terms of duration and credit) returning instruments than those implied by futures prices. Another source of extra return comes from rolling the futures contract from one calendar quarter to the next. If these sources of extra return dry up then TCRS can opt to own the underlying equity securities.

TCRS designated certain assets that in combination with the futures represents an equity allocation. The drop in equity market values in the third quarter prompted a reduction in the amount of Short Duration Fixed Income assets designated for the equity futures program. These other assets were:

Collateral:	US Treasury Notes	$ 56,977,642
Short Duration Fixed Income:		298,334,000
TCRS Cash:		84,274,358

Review: TCRS maintained its exposure to small cap stocks by utilizing the Russell 2000 Index future. The market value of small cap stocks represented by our futures exposure fell in line with the drop in the Russell 2000 Index. Forthe second quarter the drop in the Russell 2000 Index has exceeded the fall in the Small Cap policy benchmark, the S&P 600.

Affiliations: TCRS has used Citigroup exclusively in the quarter to trade index futures. We also have a clearing agreement with JPMorgan.

Domestic Fixed Income Derivatives Report

Andrew C. Palmer, CFA

Domestic Fixed Income Derivatives Transaction Log

ACCT	SOLD	BOUGHT	NET	EXPIRATION	CONTRACT	TYPE	STRIKE	
Begin								
			250		SEP (U) 2012	EURODOLLAR	PUT	96
			2220		FUT DEC 11 U.S T-BONDS		FUTURE	
			5024		FUT DEC 11 CBT UL T-BONDS		FUTURE	
			1795		FUT DEC 11 10 YR T-NOTES		FUTURE	

TRADE SUMMARY BY ACCOUNT

ACCT	SOLD	BOUGHT	NET	EXPIRATION	CONTRACT
5+ Gov-t (1381)					
	(500)	-	(500)		US 10YR NOTE FUT Dec11
	-	-	-		US 5YR NOTE (CBT) Dec11
	(500)	-	(500)		US LONG BOND(CBT) Dec11
	(1,000)	-	(1,000)		US ULTRA BOND(CBT Dec11
	-	-	-		US ULTRA BOND(CBT Mar12
	-	500	500		US LONG BOND(CBT) Mar12
	-	500	500		US 10YR NOTE (CBT)Mar12
1-5 Gov't (1368)					
	(1,345)	50	(1,295)		US 10YR NOTE FUT Dec11
	-	-	-		US 5YR NOTE (CBT) Dec11
	(1,920)	200	(1,720)		US LONG BOND(CBT) Dec11
	(2,874)	100	(2,774)		US ULTRA BOND(CBT Dec11
	-	2,524	2,524		US ULTRA BOND(CBT Mar12
	-	1,920	1,920		US LONG BOND(CBT) Mar12
	-	1,245	1,245		US 10YR NOTE (CBT)Mar12
Overlay (1371)					
	-	-	-		US 10YR NOTE FUT Dec11
	-	-	-		US 5YR NOTE (CBT) Dec11
	-	-	-		US LONG BOND(CBT) Dec11
	(1,250)	-	(1,250)		US ULTRA BOND(CBT Dec11
	-	1,250	1,250		US ULTRA BOND(CBT Mar12
	-	-	-		US LONG BOND(CBT) Mar12
	-	-	-		US 10YR NOTE (CBT)Mar12
Corporate (1365)					
	(56)	56	-		US 10YR NOTE FUT Dec11
	(130)	130	-		US 5YR NOTE (CBT) Dec11
	-	-	-		US LONG BOND(CBT) Dec11
	-	-	-		US ULTRA BOND(CBT Dec11
	-	-	-		US ULTRA BOND(CBT Mar12
	-	-	-		US LONG BOND(CBT) Mar12
	-	-	-		US 10YR NOTE (CBT)Mar12

ACCT	SOLD	BOUGHT	NET	EXPIRATION	CONTRACT	TYPE	STRIKE	
End								
			250		SEP (U) 2012	EURODOLLAR	PUT	96
			3774		US ULTRA BOND(CBT Mar12		FUTURE	
			2420		US LONG BOND(CBT) Mar12		FUTURE	
			1745		US 10YR NOTE (CBT)Mar12		FUTURE	

Domestic Fixed Income Derivatives Report

Andrew C. Palmer, CFA

Domestic Fixed Income Derivatives Transaction Log

SUMMARY OF LAST QUARTER'S ACTIVITY:

CONTRACTS IN USE:

- 5-year Futures
- 10-year Futures
- Long Bond Futures
- Ultra-Long Futures
- Eurodollar Put

STRATEGIES:

- Used Ultra-Long, Long Bond and Ten-Year Futures to manage interest rate exposures in the 1-5 Gov't portfolio, the 5+ Gov't Portfolio and the Corporate portfolio and as part of the transition to the LPF Index.
- Rolled Ten-Year, Thirty-Year and Ultra Futures contracts in 5+ Gov't portfolio to replicate the duration profile of the index without using physical Treasury notes.
- Used Ultra-Long Bond Futures to offset the duration impact of a strategic overweight to the MBS portfolio.

EFFICACY:

- Futures positions performed as expected. The replication strategy produced returns similar to the LPF Government Index and the duration adjustment transactions produced the expected impact on interest rate sensitivity. The Eurodollar put option trade was held and still provides protection against a tightening of monetary policy and a widening in Eurodollar spreads.

PROPOSED STRATEGIES FOR CURRENT QUARTER:

- Use Ultra-Long, Long Bond and Ten Year Futures to manage interest rate exposures in the 1-5 Gov't portfolio, the 5+ Government Portfolio and the Corporate portfolio.
- Use Ultra-Long Bond Futures to offset the duration impact of a strategic overweight to the MBS portfolio.
- Use Ultra-Long, Long Bond and Ten-Year Futures along with cash equivalents to replicate the duration profile of the LPF Government Index without using physical Treasury notes.
- Employ Ultra-Long, Long Bond , Ten-Year and Five-Year Futures in the Corporate portfolio to offset the duration impact of timing differences in individual corporate bond trades.
- Buying out-of-the-money calls or puts on long and intermediate Treasuries to hedge big movements in rates.

Currency Forwards Activity

Jesse Picunko, CFA

2011 4th Quarter Activity

NO ACTIVITY

TCRS MORTGAGE PORTFOLIO

END OF QUARTER MORTGAGE TBA POSITIONS

Jesse Picunko, CFA

	PRICE	PAR ($milion)	MARKET ($million)	SETTLE	FIRM
FNMA 15yr 3.0	103.266	20	20.65	JAN	MZ
FNMA 15yr 3.0	103.266	65	67.12	JAN	WFC
FNMA 30yr 4.0	105.031	20	21.01	JAN	BAML
FNMA 30yr 4.0	105.031	50	52.52	JAN	BARC
FNMA 30yr 4.0	105.031	20	21.01	JAN	RBS
FNMA 30yr 4.0	105.031	20	21.01	JAN	DB
FHLMC 30yr 4.5	105.961	30	31.79	JAN	C
GNMA 30yr 3.5	104.438	45	47.00	JAN	CS
GNMA 30yr 4.5	108.984	50	54.49	JAN	NOM
FNMA 30yr 5	108.039	-50	-54.02	JAN	DB
FNMA 30yr 4.5	106.602	25	26.65	JAN	NOM
FNMA 30yr 5.0	108.039	-19	-20.53	JAN	NOM
FNMA 30yr 4.5	106.406	25	26.60	JAN	DB
FNMA 30yr 5.5	108.891	25	27.22	JAN	DB
	Total	**326**	**343**		

By Firm	Market Value ($million)
BAML	21.0
C	31.8
DB	21.0
NOM	60.6
CS	47.0
WFC	67.1
RBS	21.0
BARC	52.5
MZ	20.7
Total	343

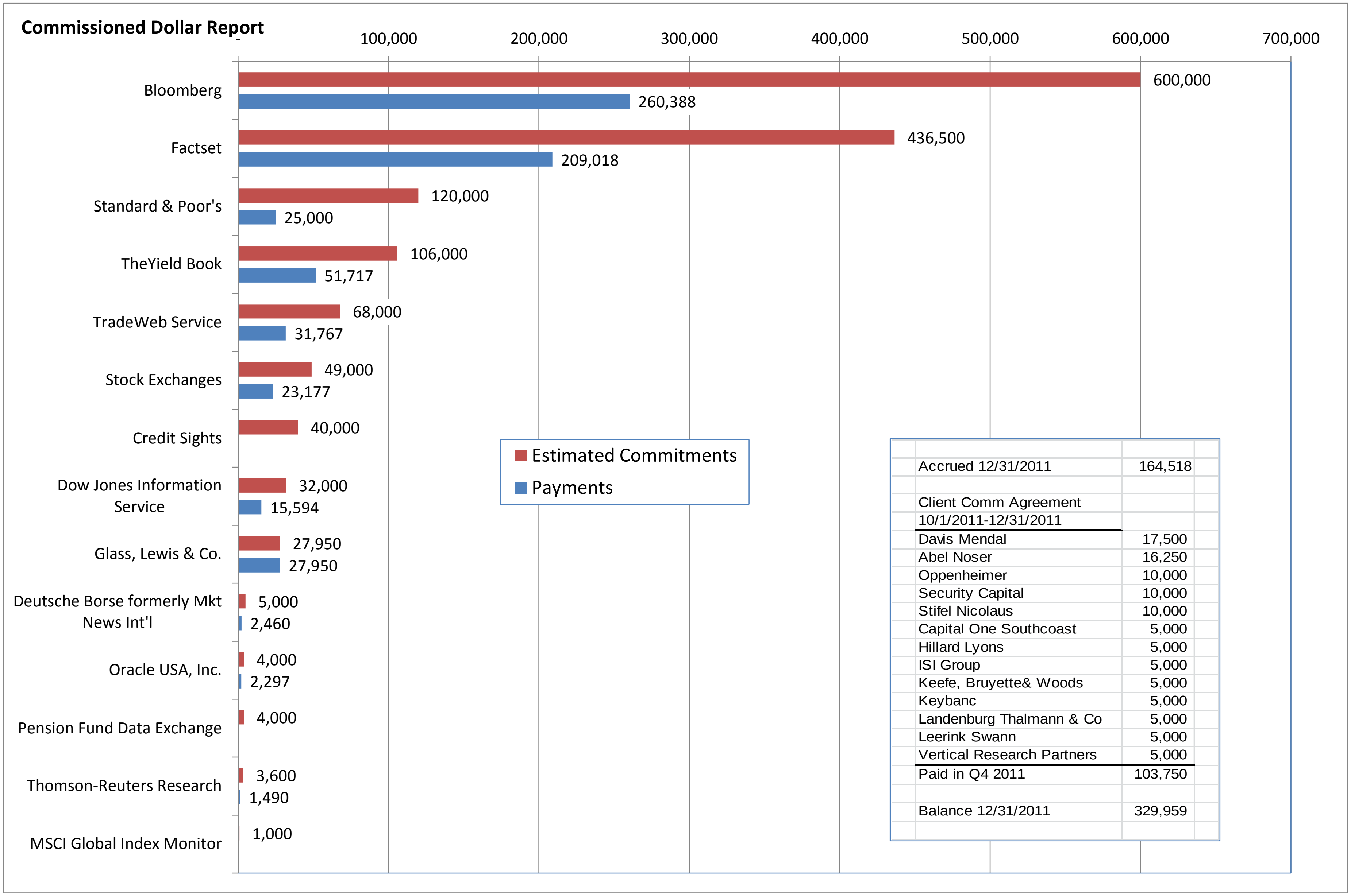
OPERATIONS UPDATE
Tim McClure, CTP

TCRS continues to move forward with changes to the Operations area. As TCRS looks for ways to add value to the Fund, this is an area that offers some opportunity for efficiencies and technology upgrades.

Trade Order Management System (OMS) – Paul Robertson continues to work toward implementing the pre-trade compliance module to the OMS. The system continues to add value and stream line the entire trading process. Staff appears to be comfortable with the system and there seems to be very few issues.

Trading – Internal Audit has concluded their review of the CSA process, and although the written report has yet to be produced, management has been given a verbal response that the CSA process seems to be sound and sufficiently transparent. Brad and Dianne have utilized the information available on Abel Noser (discussed later) and Bloomberg and continue to search for ways to reduce the costs associated with trading.

Trading Cost Analysis –The latest full quarter of time stamped data (October thru December 2011) has been reviewed. Non-basket trades had a cost of 18.95 basis points versus the Abel Noser universe costs of 20.44 basis points. Basket trades had a cost of 20.05 basis points versus the Abel Noser universe costs of 13.89 basis points. Domestic equity trades for the quarter totaled $7.48 billion.



Accrued 12/31/2011	164,518
Client Comm Agreement	
10/1/2011-12/31/2011	
Davis Mendal	17,500
Abel Noser	16,250
Oppenheimer	10,000
Security Capital	10,000
Stifel Nicolaus	10,000
Capital One Southcoast	5,000
Hillard Lyons	5,000
ISI Group	5,000
Keefe, Bruyette& Woods	5,000
Keybanc	5,000
Landenburg Thalmann & Co	5,000
Leerink Swann	5,000
Vertical Research Partners	5,000
Paid in Q4 2011	103,750
Balance 12/31/2011	329,959