ADVISOR

TEACHERS, EMPLOYEES, PUBLIC, STATE POLICE AND JUDICIAL

Vol. XXX — No. 8 SERVING OVER 295,000 MEMBERS February 2005

RSA Investments

By: David G. Bronner

DEFINED BENEFIT PLAN

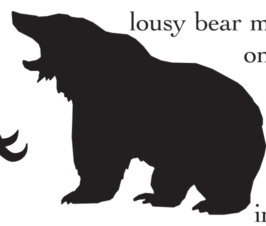
My investment strategy has been that *long-term, solid investment earnings are the key to a sound pension program*. Likewise, whenever the RSA can strengthen Alabama's economy, we will certainly do our best to accomplish this. Yet, as members of the RSA, please understand that the RSA is a defined benefit (DB) plan, which means *investments do not influence your benefits.* Your retirement benefit is based on a formula and is guaranteed by law. On the other hand, if you have a 401K, or a mutual fund, you have a defined contribution (DC) plan where investments do have a major, direct impact on your benefits.

Because the RSA is a DB plan, any investment losses at the RSA will not affect your retirement benefit, but investment earnings are extremely important to holding down the costs to the state (taxpayers). Last month's *Advisor* clearly indicated that Alabama taxpayers only contributed 14.9% of the total revenue in 2004, while 72.2% came from RSA investment earnings. The RSA officially adjusts market values (marks to market) every six months, whereas mutual funds adjust on a daily basis. Investments that either increase or decrease in value are adjusted accordingly.

BAD NEWS TRAVELS

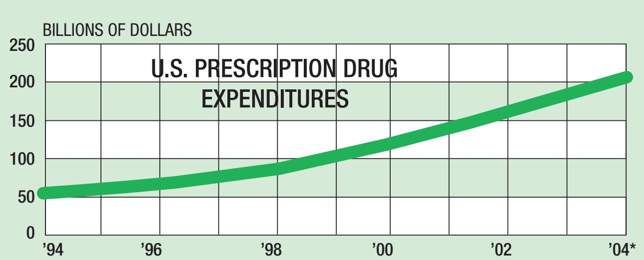
I have often stated, "Bad news travels while good news stays at home." In other words, bad news makes the news, whereas good news is of less interest.

When investing billions of dollars, there will always be winners and losers. The 2001 and 2002 fiscal years were lousy bear markets and everyone lost. The 2003 and 2004 fiscal years were good markets even with the huge losses in Enron, WorldCom (90% of which the RSA got back via the courts), or writing off U.S. Airways. The RSA had a positive net gain in investment earnings of $2.96 billion in 2003 and $2.38 billion in 2004. That is $5.3 billion in just the last two years.



So what is the point? Try not to get all stressed-out on what individual companies are doing. You will not read about the ones that are doing fine. However, when politicians want to decrease the amount contributed by the state (taxpayers) get ready for war and remind them that taxpayers only contributed 14.9% of total revenue.

DRUG NATION



*ESTIMATES FOR 2003 AND 2004

Data: Centers for Medicare & Medicaid Services

Simple Solutions

Editorial

There is an old saying, "Simple minds come up with simple solutions." Sometimes that is very good—a difficult problem solved by a simple solution. Other times, "it is what it is."

Washington, D.C. activists and an Alabama Congressman are rightly concerned about the genocide taking place in Sudan. They are trying to model a campaign against it, like the one against apartheid in South Africa 20 years ago. Any human being should be against genocide, whether it is in Africa, Asia, Kosovo, or any other place in the world, as that crime is way beyond belief. Yet, to say pension funds need to do something about it when the world is unable to stop such crimes, often for decades, is simply unrealistic.

If the activists are sincere about wanting to do something for the Sudan, study the country and identify the top ten companies doing business in Sudan (most will be European/Asian Corporations). Then, ask those companies and Boards of Directors to get directly involved in solving the problem. Clearly, neither a U.S. company selling a mere six-pack of Coke nor a pension fund investor is going to influence what is going on in the Sudan.

Choose and Lose

By Barry Schwartz

"There are three arguments being made in favor of privatizing part of Social Security. First, the Social Security Trust Fund needs money and privatization will, in the long run, increase the amount of money available for retirees. Second, privatization will give people choice, and choice is good. And third, "it's your money," and you ought to be able to do with it as you wish….

Though experts differ on the urgency and the severity of the problem, most everyone agrees that the trust fund will eventually run out of money unless we do something, from 2042 to 2052. Two obvious and painful things we can do are decrease benefits or increase payroll taxes. Privatization, it is argued, solves the problem without the pain. Equity investments return about twice as much, historically, as Treasury bills. So by allowing people to put some of their payroll taxes into equity investments, we will increase the value of that part of their retirement account so we can then decrease the benefits paid out by the standard Social Security program and still leave retirees better off.

There are several problems with this argument, however. For starters, there is no guarantee that equities will return more than Treasury bills. One of the reasons that equities have a higher rate of return than other types of investments is that investors have to be compensated for taking risks. Perhaps equities will outperform Treasury bills in the long term but that doesn't mean that they will be outperforming Treasury bills at the specific moment you retire.

For example, a person who retired in 2000 after a lifetime of investing half in stocks and half in bonds would have had 50 percent more in his account than a person making the same investments who retired in 2003….

What's more, the administrative costs of keeping track of these private accounts, according to President Bush's Commission to Strengthen Social Security, will be 10 to 30 times the cost of administering the current system, eating up almost all of the hypothetical gains that equity investments could provide.

Finally, even if we grant the advantages of putting trust fund money into equities, this is something that the government could do without privatizing anything by doing the investing itself. The government as investor can ride out risks better than any individual investor, and administrative costs would be vastly reduced. Only brokerage houses could suffer—from lost commissions….

This brings us to the second argument in favor of privatizing Social Security: giving people options makes them better off. There is now accumulating evidence that choice isn't always good…

A study by Sheena Iyengar, a psychologist, and Wei Jiang, an economist, has shown that when employers increase the number of funds available to employees for voluntary 401(k) investments, the rate of participation goes down by 2 percent for every 10 funds offered. And this is true even when participating employees get free money—matching money—from employers.

So whereas there is no denying that choice is sometimes good,…The appropriately abysmal early public response to the administration's Medicare prescription drug choice plan provides ample reason to suspect that many people will not regard being able to choose their Social Security investment instruments as a blessing.

This brings me to the final defense of privatization: the payroll taxes you pay are your money, and you ought to be able to do what you like with your money. This, I suspect, is the real justification behind the move to privatize, and it is the worst reason of all. The payroll tax is not "your" money; it's our money. Social Security was created as an insurance scheme, not a pension scheme. It was meant to provide a safety net, to protect the unlucky from immiserization in old age. The benefits we get are not payouts from accounts in which we have accumulated our own private stash. What we get is largely determined by what we earned, but we keep getting it even after we've taken out every penny we put in. And if we happen to die early, someone else reaps the benefits of our contributions.

The Bush administration should be honest with the American people and ask us if we want to do away with Social Security, without pretending that privatization will solve the problem of financing the trust fund without pain…."

Barry Schwartz, a professor of psychology at Swarthmore College, is the author of The Paradox of Choice: Why More is Less.

Re-elected Members of the TRS Board of Control

Dr. Paul Hubbert, Chairman of the TRS Board of Control, administers the Oath of Office to Dr. Susan Brown, Mrs. Sarah Swindle, Mrs. Peggy Lamb, and Mr. Russell Twilley.

Pounds of Garbage Produced Per Person Each Year

United States	**1,637**
Norway	**1,184**
Netherlands	**1,100**
Germany	**823**
Sweden	**662**
France	**572**
Italy	**548**
Portugal	**367**

Source: Recycling Advocate

Retirees Are Paying More

By Robert Pear

"WASHINGTON—Retirees who receive health benefits from their former employers saw premiums shoot up an average of 25 percent this year, a new study says.

The study, issued by the Kaiser Family Foundation and Hewitt Associates, showed a continued erosion of retiree health benefits among large employers.

Companies are requiring retirees to pay a larger share of premiums and other health costs. While continuing to provide coverage for people who have already retired, about 8 percent of large private employers took action in the last year to end all subsidized health benefits for future retirees, and 11 percent said they would do so next year.

"Prospects for retiree health coverage are slowly disappearing for America's workers, and retirees who have it will be paying more," said Drew E. Altman, the president of the Kaiser Family Foundation, which conducted the study with Hewitt, a benefits consulting firm."

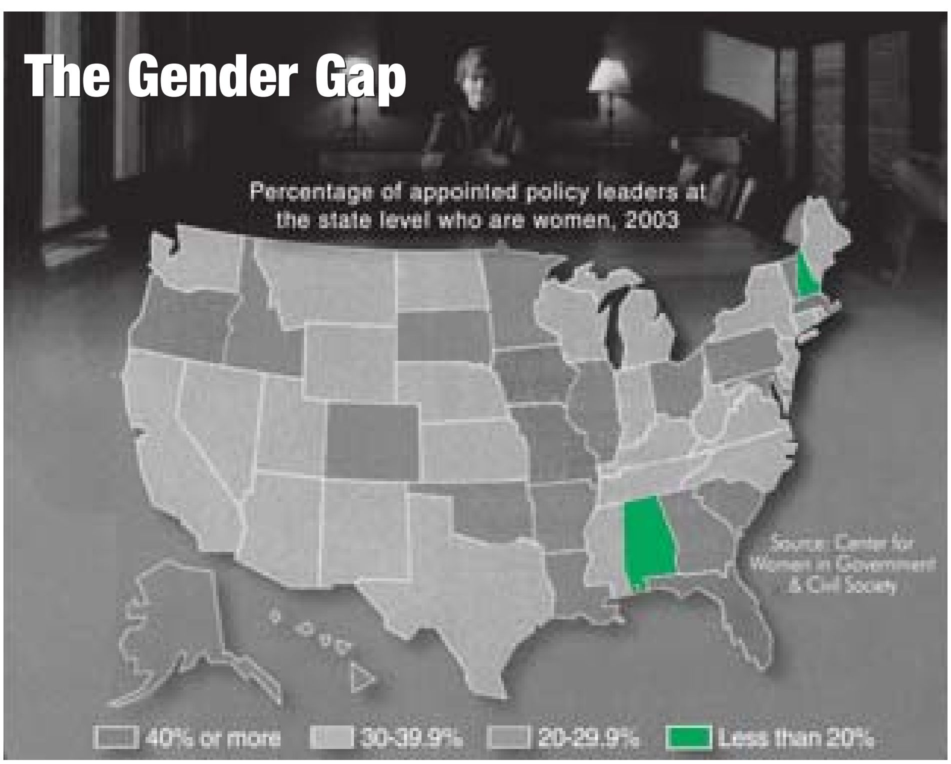
(Editor's Note: PEEHIP member Mr. Stuart tells us, "He helps to hold down PEEHIP costs by utilizing state/county Health Departments whenever possible.")

Health Benefit Changes for the Retired

Some findings from a survey of retiree health benefits at 333 companies with 1,000 or more employees:

	PERCENTAGE MAKING CHANGES IN 2004	PERCENTAGE LIKELY TO MAKE CHANGES IN 2005
Increase retirees' contributions to premiums	**79%**	**85%**
Increase co-payments	**45**	**51**
Increase deductibles	**37**	**43**
Add or improve coverage or benefits	**12**	**11**
Eliminate subsidized benefits for future retirees	**8**	**11**
Changes to manage prescription drug costs		
Increase drug co-payments	**53%**	**49%**
Require prior authorization for some drugs	**37**	**40**
Impose three-level system for co-payments	**24**	**28**
Establish lists of preferred drugs	**14**	**19**
Require mail order for refills of some prescriptions	**11**	**25**

Source: The New York Times, Kaiser/Hewitt 2004 Survey on Retiree Health Benefits



HOW CHEAP IS CHINESE LABOR?

PayGap

Average hourly compensation for factory workers*

U.S. $21.11

CHINA $0.64**

*2002 data. U.S. production workers; China: all manufacturing workers **Est.

Data: Bureau of Labor Statistics; Judith Banister, consultant to the BLS

BANISTER CONCLUDED China has about 38 million city manufacturing workers. The 30 million on whom she found data earn an average $1.06 an hour. Another roughly 71 million suburban and rural manufacturing workers earn an average 45¢ an hour, for a blended 64¢. In the current BLS survey, Mexico's $2.48 hourly compensation is the lowest.

U.S. Debt

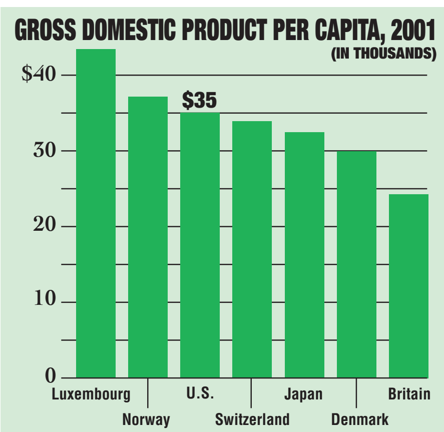
Source: Dow Theory Letters

If debt is not out-of-control, it is getting close. The U.S. is now paying over $320 billion a year in interest to holders of Federal debt. The $37 trillion debt is four times the Gross National Product (GDP) of the U.S., and is now running a $650 billion deficit or near 6 percent of GDP, and anything over 5 percent is considered a danger to a currency.

The U.S. is now sopping up 80 percent of the savings of "All" the nations of the world. We currently spend monthly about $5 billion for the wars in Afghanistan and Iraq, and we face around $5 trillion in future liabilities for Social Security.

Taking our cue from the federal government, U.S. consumers are doing the same. Since the year 2000, household debt has risen over 30 percent. Total household debt is just under $10 trillion. The U.S. consumer savings rate is now 0.2 percent, just about zero!

The world has never seen anything like it. Either we will print the paper in an effort to finance all this debt, which means inflation, or being unable to handle the debt, the dollar will swoon, and the U.S. sinks into a recession. It seems obvious; the best answer is to get debt under control. ■



Source: Statistical Abstract of the United States

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Report — Street Lights that are out — to the Power Company!
Report — Weedy Lots—to the Mayor!