

McGladrey & Pullen

Certified Public Accountants

ILLINOIS STATE BOARD OF INVESTMENT (An Internal Investment Pool of the State of Illinois)

Compliance Examination

Year ended June 30, 2008

Performed as Special Assistant
Auditors for the Auditor General,
State of Illinois

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Table of Contents

	Page
Agency Officials	1
Management Assertion Letter	2
Compliance Report:	
Summary	3
Accountants' Report:	
Independent Accountants' Report on State Compliance, on Internal Control over Compliance, and on Supplementary Information for State Compliance Purposes	4
Schedule of Findings:	
Current Findings	7
Prior Findings Not Repeated	8
Supplementary Information for State Compliance Purposes:	
Summary	9
Fiscal Schedules and Analysis:	
Comparative Schedule of Operations	10
Schedule of Investment Portfolio	11
Schedule of Investment Manager Fees	12
Schedule of Soft Dollar Credits (Unaudited)	14
Schedule of Investment Commissions (Unaudited)	15
Schedule of Property and Equipment	18
Reconciliation of the State Treasurer's Cash Balance with that of the Board	18
Analysis of Accounts Receivable	18
Analysis of Operations:	
Board Functions and Planning Program	19
Number of Employees	20
Derivative Securities	20
Securities Lending Program	21
Proceeds from General Obligation Bonds, Pension Funding Series June 2003 (Unaudited)	22
Third-Party Marketing Fees Paid (Unaudited)	22
Service Efforts and Accomplishments (Unaudited)	23
Overall Rates of Return	23
Investment Returns – Benchmark and Actual	23
Net Asset Allocations as of June 30, 2008	25

The annual financial statements of the Illinois State Board of Investment for the year ended June 30, 2008 were issued under a separate cover.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Agency Officials

Executive Director	Mr. William R. Atwood
Deputy Executive Director	Ms. Katherine A. Spinato
Chief Fiscal Officer	Ms. Alise White
General Counsel/Chief Compliance Officer	Ms. Emily A. Reid

Illinois State Board of Investment Office is located at:

180 N. LaSalle Street
Suite 2015
Chicago, Illinois 60601



ILLINOIS STATE BOARD OF INVESTMENT

180 North LaSalle Street, Suite 2015
Chicago, Illinois 60601
(312) 793-5718

February 17, 2009

McGladrey & Pullen
20 North Martingale Rd. Suite 500
Schaumburg, IL. 60173-2420

Ladies and Gentlemen:

We are responsible for the identification of, and compliance with, all aspects of laws, regulations, contracts, or grants that could have a material effect on the operations of the Illinois State Board of Investment (the Board). We are responsible for and we have established and maintained an effective system of internal controls over compliance requirements. We have performed an evaluation of the Board's compliance with the following assertions during the year ended June 30, 2008. Based on this evaluation, we assert that during the year ended June 30, 2008, the Board has materially complied with the assertions below.

- A. The Board has obligated, expended, received and used public funds of the State in accordance with the purpose for which such funds have been appropriated or otherwise authorized by law.
- B. The Board has obligated, expended, received and used public funds of the State in accordance with any limitations, restrictions, conditions or mandatory directions imposed by law upon such obligation, expenditure, receipt or use.
- C. The Board has complied, in all material respects, with applicable laws and regulations, including the State uniform accounting system, in its financial and fiscal operations.
- D. The State revenues and receipts collected by the Board are in accordance with applicable laws and regulations and the accounting and recordkeeping of such revenues and receipts is fair, accurate and in accordance with law.
- E. The money or negotiable securities or similar assets handled by the Board on behalf of the State or held in trust by the Board have been properly and legally administered, and the accounting and recordkeeping relating thereto is proper, accurate and in accordance with law.

Very truly yours,

Illinois State Board of Investment


William R. Atwood
Executive Director


Katherine A. Spinato
Deputy Executive Director


Emily A. Reid
*General Counsel/
Chief Compliance Officer*

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Compliance Report

Summary

Year ended June 30, 2008

The compliance testing performed during this examination was conducted in accordance with *Government Auditing Standards* and in accordance with the Illinois State Auditing Act.

Accountants' Reports

The Independent Accountants' Report on State Compliance, on Internal Control over Compliance, and on Supplementary Information for State Compliance Purposes does not contain scope limitations, disclaimers, or other significant nonstandard language.

Summary of Findings

	Current Report	Prior Report
Number of:		
Findings	-	-
Repeated findings	-	-
Prior recommendations implemented or not repeated	-	-

Details of findings are presented in a separately tabbed report section.

Schedule of Findings		
Item No.	Page	Description
Current Year Findings:		
None.		
Prior Findings Not Repeated (<i>Government Auditing Standards</i>):		
None.		
Prior Findings Not Repeated (State Compliance):		
None.		

Exit Conference

The Board reviewed the entire report and waived a formal exit conference.

McGladrey & Pullen

Certified Public Accountants

Independent Accountants' Report on State Compliance, on Internal Control over Compliance, and on Supplementary Information for State Compliance Purposes

Honorable William G. Holland
Auditor General
State of Illinois

Board of Directors
Illinois State Board of Investment

Compliance

As Special Assistant Auditors for the Auditor General, we have examined the Illinois State Board of Investment's compliance with the requirements listed below, as more fully described in the Audit Guide for Financial Audits and Compliance Attestation Engagements of Illinois State Agencies (Audit Guide) as adopted by the Auditor General, during the year ended June 30, 2008. The management of the Illinois State Board of Investment (the Board) is responsible for compliance with these requirements. Our responsibility is to express an opinion on the Board's compliance based on our examination.

- A. The Board has obligated, expended, received, and used public funds of the State in accordance with the purpose for which such funds have been appropriated or otherwise authorized by law.
- B. The Board has obligated, expended, received, and used public funds of the State in accordance with any limitations, restrictions, conditions, or mandatory directions imposed by law upon such obligation, expenditure, receipt, or use.
- C. The Board has complied, in all material respects, with applicable laws and regulations, including the State uniform accounting system, in its financial and fiscal operations.
- D. The State revenues and receipts collected by the Board are in accordance with applicable laws and regulations and the accounting and recordkeeping of such revenues and receipts is fair, accurate, and in accordance with law.
- E. Money or negotiable securities or similar assets handled by the Board on behalf of the State or held in trust by the Board have been properly and legally administered and the accounting and recordkeeping relating thereto is proper, accurate, and in accordance with law.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants; the standards applicable to attestation engagements contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the Illinois State Auditing Act (Act); and the Audit Guide as adopted by the Auditor General pursuant to the Act; and, accordingly, included examining, on a test basis, evidence about the Board's compliance with those requirements listed in the first paragraph of this report and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on the Board's compliance with specified requirements.

In our opinion, the Illinois State Board of Investment complied, in all material respects, with the requirements listed in the first paragraph of this report during the year ended June 30, 2008.

As required by the Audit Guide, immaterial findings related to instances of noncompliance excluded from this report have been reported in a separate letter to your office.

Internal Control

The management of the Board is responsible for establishing and maintaining effective internal control over compliance with the requirements listed in the first paragraph of this report. In planning and performing our examination, we considered the Board's internal control over compliance with the requirements listed in the first paragraph of this report in order to determine our examination procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the Audit Guide, issued by the Illinois Office of the Auditor General, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Board's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with the requirements listed in the first paragraph of this report on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to comply with the requirements listed in the first paragraph of this report such that there is more than a remote likelihood that noncompliance with a requirement that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies that results in more than a remote likelihood that a material noncompliance with a requirement listed in the first paragraph of this report will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance with the requirements listed in the first paragraph of this report was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

As required by the Audit Guide, immaterial findings excluded from this report have been reported in a separate letter to your office.

Supplementary Information for State Compliance Purposes

As Special Assistant Auditors for the Auditor General, we have audited the basic financial statements of the Board as of and for the year ended June 30, 2008, and have issued our report thereon dated December 12, 2008. The accompanying supplementary information, as listed in the table of contents as Supplementary Information for State Compliance Purposes, is presented for purposes of additional analysis and is not a required part of the basic financial statements of the Board. The 2008 Supplementary Information for State Compliance Purposes, except for that portion marked "unaudited" on which we express no opinion, has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements for the year ended June 30, 2008, taken as a whole.

The basic financial statements of the Board for the year ended June 30, 2007, were audited by other auditors whose report thereon dated January 15, 2008, expressed an unqualified opinion on the basic financial statements. Their 2007 Independent Accountant's Report on State Compliance, on Internal Control over Compliance, and on Supplementary Information for State Compliance Purposes noted, except for that portion marked "unaudited," that the Supplementary Information for State Compliance Purposes is fairly stated in all material respects in relation to the basic financial statements for the year ended June 30, 2007.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Illinois State Board of Investment Board of Directors, and the Board's management and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

Schaumburg, Illinois
February 17, 2009

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule of Findings

Current Findings

Year ended June 30, 2008

None.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule of Findings

Prior Findings Not Repeated

Year ended June 30, 2008

None.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)
Supplementary Information for State Compliance Purposes
Year ended June 30, 2008

Summary

Supplementary Information for State Compliance Purposes presented in this section of the report includes the following:

Fiscal Schedules and Analysis:

- Comparative Schedule of Operations
- Schedule of Investment Portfolio
- Schedule of Investment Manager Fees
- Schedule of Soft Dollar Credits (Unaudited)
- Schedule of Investment Commissions (Unaudited)
- Schedule of Property and Equipment
- Reconciliation of the State Treasurer's Cash Balance with that of the Board
- Analysis of Accounts Receivable

Analysis of Operations:

- Board Functions and Planning Program
- Number of Employees
- Derivative Securities
- Securities Lending Program
- Proceeds from General Obligation Bonds, Pension Funding Series June 2003 (Unaudited)
- Legislative Changes
- Third-Party Marketing Fees Paid (Unaudited)
- Service Efforts and Accomplishments (Unaudited)

The accountants' report that covers the Supplementary Information for State Compliance Purposes presented in the Compliance Report Section states that it has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in the accountants' opinion, except for that portion marked "unaudited," on which they express no opinion, it is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
 Comparative Schedule of Operations
 Years ended June 30, 2008 and 2007

	2008	2007	Increase (decrease)
Investment income:			
Interest	\$ 154,620,159	\$ 172,400,021	\$ (17,779,862)
Dividends	162,205,372	147,112,290	15,093,082
Securities lending	16,624,470	4,493,459	12,131,011
Realized gain on investments	594,579,054	848,635,310	(254,056,256)
Unrealized gain/(loss) on investments	<u>(1,623,821,419)</u>	<u>745,633,561</u>	<u>(2,369,454,980)</u>
Total investment income/(loss)	<u>(695,792,364)</u>	<u>1,918,274,641</u>	<u>(2,614,067,005)</u>
Expenses:			
Salaries and benefits	1,422,254	1,277,024	145,230
Operating	567,688	448,056	119,632
External support	<u>39,860,694</u>	<u>38,838,254</u>	<u>1,022,440</u>
Total expenses	<u>41,850,636</u>	<u>40,563,334</u>	<u>1,287,302</u>
Net investment income/(loss)	<u>\$ (737,643,000)</u>	<u>\$ 1,877,711,307</u>	<u>\$ (2,615,354,307)</u>

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
Schedules of Investment Portfolio
June 30, 2008 and 2007

Fair value	2008		2007	
	Amount	Percentage of portfolio	Amount	Percentage of portfolio
Equities:				
Common stocks:				
U.S. equities:				
Consumer discretionary	\$ 365,831,551	3.20%	\$ 750,423,267	5.86%
Consumer staples	237,580,894	2.08	272,238,283	2.13
Energy	526,199,724	4.60	558,750,267	4.36
Financials	559,349,879	4.89	1,290,227,457	10.07
Healthcare	430,812,010	3.77	612,033,064	4.78
Industrials	570,949,815	5.00	817,691,924	6.39
Information Technology	639,744,095	5.60	860,066,637	6.72
Materials	224,164,675	1.96	250,548,688	1.96
Telecommunication Services	115,795,367	1.01	184,928,286	1.44
Utilities	121,182,167	1.06	144,204,447	1.13
Other	450,075,756	3.94	318,296,707	2.49
Non-U.S. equities	1,984,917,495	17.37	1,365,647,941	10.65
Preferred stock	4,491,500	0.04	1,865,020	0.01
Total equities	<u>6,231,094,928</u>	<u>54.52</u>	<u>7,426,921,988</u>	<u>57.99</u>
Fixed income securities:				
Government and agency obligations:				
U.S. Treasury	236,044,092	2.07	317,358,768	2.48
Federal agencies and other governments	616,292,422	5.39	867,031,944	6.77
Options	(290,813)	0.00	(114,828)	0.00
Municipal	-	0.00	-	0.00
Foreign obligations	113,005,430	0.99	72,189,687	0.56
Corporate obligations:				
Finance	159,397,789	1.39	256,092,972	2.00
Industrials	593,294,641	5.19	531,051,552	4.15
Commercial mortgage backed securities	11,815,522	0.10	57,603,793	0.45
Collateralized mortgage obligations	124,232,849	1.09	112,780,484	0.88
Asset backed	29,407,855	0.26	87,801,215	0.69
Miscellaneous	125,838,571	1.10	154,338,401	1.21
Private placement	14,177,105	0.12	5,622,489	0.04
Commingled	-	0.00	23,679,106	0.18
Convertible bonds				
Total fixed income securities	<u>2,023,215,463</u>	<u>17.70</u>	<u>2,485,435,583</u>	<u>19.41</u>
Real estate investments	1,332,081,349	11.65	1,189,614,911	9.29
Private equity	524,628,589	4.59	563,366,021	4.40
Infrastructure Funds	209,975,518	1.84	108,436,449	0.85
Hedge funds	598,985,402	5.24	496,404,578	3.88
Money market investments	307,481,504	2.69	535,699,912	4.18
Bank Loans	202,137,983	1.77	-	0.00
Forward foreign currency contracts	(72,622)	0.00	(108,696)	0.00
Total investments	<u>\$ 11,429,528,114</u>	<u>100.00%</u>	<u>\$ 12,805,770,746</u>	<u>100.00%</u>

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
 Schedule of Investment Manager Fees
 Years ended June 30, 2008 and 2007

	2008	2007
Alinda	\$ 927,612	\$ 940,946
Amalgamated Bank NY	1,282,500	650,307
Ariel	-	152,973
Ativo	49,244	54,684
Atlanta Life	323,461	213,181
Blackrock	29,227	848,243
Boston Company	161,178	1,295,327
Brandywine	825,874	866,896
Buford, Dixon	133,147	121,264
Channing	238,406	237,508
Chicago Equity Partners	338,726	260,090
Decatur	46,818	41,938
Earnest Partners	37,650	991,882
Entrust	1,128,570	-
Fiduciary Management Associates	100,627	-
Fort Washington	608,868	584,037
Globeflex Capital	569,363	606,039
Goldman Sachs	1,778,284	1,536,224
Grosvenor Capital Management	1,085,838	1,017,417
Harris Investment Management	-	97,396
Harris Investment Management-High Yield	-	479,776
High Pointe	7,520	209,932
Howland	130,614	118,088
IronBridge Capital Management	1,302,394	991,000
Ivy	1,449,361	1,267,457
JP Morgan Asset Management	1,557,903	2,876,435
LM Capital	332,534	266,692
Loomis Sayles	1,163,454	194,779
LSV Asset Management	2,036,244	2,161,689
Lynmar	527,473	285,785
Martingale Asset Management	1,110,441	1,279,997
Macquarie	3,000,000	2,700,624
McDonnell Investment Management	477,558	-
Mesirow	1,121,843	1,021,165
New Amsterdam	34,133	896,395
NWQ	1,258,203	1,375,431

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
 Schedule of Investment Manager Fees (Continued)
 Years ended June 30, 2008 and 2007

	2008	2007
Opus Capital Management	\$ 428,428	\$ 288,492
Profit	517,602	288,074
Rhumblin	125,400	116,464
Rockcreek	1,356,393	1,268,194
Segall Bryant and Hamill	1,089,988	698,820
SSgA (Cash Overlay)	223,101	257,438
SSgA Intermediate Gov./Credit Index	30,634	64,894
SSgA MSCI ACWI Index	120,102	-
SSgA MSCI EAFE Index	74,352	-
SSgA MSCI EAFE Small Cap	23,114	-
SSgA Small Cap Global	1,726,950	1,609,981
Templeton	1,460,946	1,331,765
Trust Company of the West (TCW)	332,725	-
Trust Fund Advisors	264,146	543,348
Union Labor Life Investment Co. (ULLICO)	1,172,250	729,960
Various (allocated equally to all Investment Managers)	27,500	-
Vontobel Asset Management	260,505	-
Walter Scott	139,870	1,058,674
Western Asset Management	1,074,129	856,759
William Blair	2,385,767	1,542,910
	<u>\$ 38,008,970</u>	<u>\$ 37,297,370</u>

Investment manager fees are related to fees paid to various investment managers. Fees are negotiated primarily on market values. A graduated rate is used for most managers based upon various increments per million dollars of market value.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
Schedule of Soft Dollar Credits (Unaudited)
Years ended June 30, 2008 and 2007

	2008	2007
Soft dollar credits outstanding, at beginning of fiscal year	\$ 319,951	\$ 291,422
Soft dollar credits earned	19,685	44,089
Investment expenses paid with soft dollar credits	<u>(16,017)</u>	<u>(15,560)</u>
Soft dollar credits outstanding, at end of fiscal year	<u>\$ 323,619</u>	<u>\$ 319,951</u>

Soft dollar credits are issued to the Board by certain brokers based on the level of activity of investment managers using that particular broker. The Board can use these credits to pay for various investment expenses.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)
 Fiscal Schedules and Analysis
 Schedule of Investment Commissions (Unaudited)
 Years ended June 30, 2008 and 2007

	2008	2007
Investment brokerage firms:		
Abel Noser	\$ -	\$ 9,100
Amhold & S Bleichroeder	8,266	-
Archipelago	-	16,845
Banc of America Securities Inc.	108,533	16,732
Bank of New York	-	18,932
BB&T Capital	-	6,981
Bear Stearns Securities Corp.	53,069	53,590
Berean Capital Inc.	-	40,229
Bernstein Sanford & Co	13,854	-
Blair, William & Co.	11,758	9,317
Bloomberg Tradebook	16,571	19,421
BMO Capital Markets	13,059	-
BNY ESI & Co.	-	8,306
BOE Securities	5,582	-
Bridge Training	11,714	-
Cabrera Asset Management	107,363	116,514
Canaccord Adams Inc.	-	5,686
Cantor Fitzgerald & Co.	49,362	49,855
Cheevers & Company	26,193	68,870
Citigroup Smith Barney Inc.	45,196	26,252
Credit Suisse First Boston Corp.	133,521	35,419
DeMatteo Monness	5,861	-
Deutsche Banc Securities Inc.	224,293	45,382
ESP	26,765	-
First Boston	11,770	-
First Honolulu	81,176	44,450
Fox Pitt Kelton	6,572	-
Friedman Billings and Ramsey & Co. Inc.	15,062	13,792
Future Trade	9,994	-
Gardner Rich & Co.	187,476	145,018
Goldman Sachs & Company	16,009	33,299
Guzman & Co.	20,980	23,206
Hoenig & Co.	-	7,324
Howard, Weill Labouisse, Fried	5,520	-

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT

(An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis

Schedule of Investment Commissions (Unaudited) (Continued)

Years ended June 30, 2008 and 2007

	2008	2007
Investment brokerage firms (Continued):		
Instinet	\$ 7,073	\$ 8,826
International Strategy & Investment	-	11,782
Investment Technology Group	32,511	46,573
J.P. Morgan Securities, Inc.	315,908	36,508
Jackson Securities	17,162	24,010
Janney Montgomery Scott, Inc.	-	13,260
Jefferies & Company	51,075	38,536
Johnson Rice & Co.	-	10,461
Jones & Associates	-	5,413
Jones Trading	10,008	5,085
Keefe Bruynette and Woods Inc.	7,149	11,247
KeyBanc Capital Markets	8,005	-
Knight Equity Markets LP	19,670	-
Knight Securities	54,359	-
Lehman Brothers Inc.	82,091	85,646
Liquidnet Inc.	217,262	202,404
Loop Capital Markets	198,816	132,511
Loopus	11,645	-
Lynch Jones & Ryan	32,288	37,326
M. Ramsey King Securities	-	23,484
Magna Securities	47,825	23,876
Melvin Securities Corp	56,704	52,666
Merrill Lynch Pierce Fenner & Smith	140,272	56,389
Midwest Research Securities	10,647	10,076
Morgan Stanley & Co.	128,821	224,008
MR Beal	76,532	51,283
Muriel Siebert	11,274	22,350
Natexis Bleichroeder	-	10,925
Nomura Securities	-	5,861
Nutmeg Securities	36,679	42,224
NYFIX	6,898	15,815
Oppenheimer	10,931	-
Pacific American	19,719	18,454
Pacific Crest Securities	9,415	-
Pipeline Trading Systems	8,256	11,250

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis
Schedule of Investment Commissions (Unaudited) (Continued)
Years ended June 30, 2008 and 2007

	2008	2007
Investment brokerage firms (Continued):		
Prudential Securities	\$ -	\$ 12,982
Pulse Trading	88,922	-
Ramirez	26,199	5,970
Ramsey King	36,694	-
Raymond James & Assoc.	13,142	12,174
Redi Book	-	15,048
Reynolds Securities LLC	13,248	-
Robert W. Baird & Co.	22,749	32,304
Robinson Humphery	-	21,049
Roth Capital	-	6,309
Salomon Smith Barney	12,969	36,374
Sanford C. Bernstein	14,209	18,864
SBK Brooks	-	7,533
SG Cowen and Company	8,896	-
Sidoti	-	8,297
Stephen Inc.	-	14,081
Stiffel, Nicolaus & Company Inc.	5,038	9,773
Thompson Davis	-	7,789
U.S. Bancorp Piper Jaffray Inc.	7,572	7,046
UBS Securities	-	9,038
UBS Warburg Dillon Read	58,896	9,598
Wachovia Securities	5,599	-
Wedbush Morgan Securities, Inc.	-	8,116
Weeden & Co.	11,363	22,239
Williams Capital Group	64,864	109,452
Various (Under \$5,000)	145,037	187,836
	<u>\$ 3,379,911</u>	<u>\$ 2,614,641</u>

Commissions relate to fees paid to investment brokerage firms for the purchase and sale of investments.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis

Year ended June 30, 2008

Schedule of Property and Equipment

A schedule of changes in property and equipment is as follows:

	Beginning balance	Additions	Deletions	Ending balance
Cost	\$ 100,536	\$ 15,662	\$ (8,260)	\$ 107,938
Less accumulated depreciation	(51,253)	(7,375)	3,487	(55,141)
Net property and equipment	<u>\$ 49,283</u>	<u>\$ 8,287</u>	<u>\$ (4,773)</u>	<u>\$ 52,797</u>

Note: Amounts reported in the Schedule of Property and Equipment have been reconciled to property reports submitted to the Office of the Comptroller.

Reconciliation of the State Treasurer's Cash Balance with that of the Board

Balance per State Treasurer at June 30, 2008	\$ 185,604
Vouchers in transit	<u>(76,819)</u>
Balance per Board at June 30, 2008	<u>\$ 108,785</u>

Analysis of Accounts Receivable

The Board's receivable balance at June 30, 2008 amounted to \$187,106,001, which consisted of \$40,460,171 of dividends, interest, foreign taxes, and accounts receivable on investments held and receivables of \$146,645,830 for investments sold prior to June 30 but settled after year-end. Because the collection of this interest is relatively assured and the sale of investments is merely an issue of timing, the Board does not maintain a reserve for uncollectible receivables or age the receivable detail.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

Board Functions and Planning Program

The Illinois State Board of Investment (the Board) was created on October 10, 1969, by Article 22A of the Illinois Pension Code to manage and invest the assets and reserves of any pension fund or retirement system that transfers this responsibility to the Board. In accordance with Article 22A, the Trustees of the State Employees' Retirement System, the General Assembly Retirement System, and the Judges' Retirement System transferred all of their investment assets to the Board as of June 30, 1970. Since that date, all additional funds available for investment for those three systems have been transferred to the Board.

In 1978, in accordance with Article 24, the Board shall be responsible for developing and establishing the State Employees' Deferred Compensation Plan (the Plan). Initial enrollment began in 1979, at which time the Department of Personnel (now Department of Central Management Services) was named as the Administrator of the Plan. With respect to developing and establishing the plan, the Board reviews investment offering options for the Plan and supervises the Department of Central Management Services' administration of the Plan.

Beginning July 1, 1978, the Board merged the Illinois Board Fund, Illinois Equity Fund, and Illinois Segregated Fund into the Illinois State Board of Investment Commingled Fund (the Commingled Fund). The purpose of this consolidation was to enhance control over investment policy through increased flexibility in the allocation of cash reserves between fixed income and equity investments. The Board's investment policy and strategy can be more uniformly applied to each member system irrespective of cash flow. In addition, it simplified the Board's accounting and reporting systems. The result is that the Commingled Fund now represents all of the assets under the Board's supervision.

Beginning in 1982, the Board expanded the asset base of the Commingled Fund to include both real estate and venture capital.

In 1992, the Board completed its investment strategy to have all equity security investments managed externally.

During fiscal year 2004, the Board engaged Marquette Associates as its investment consultant. The Board conducted an asset allocation study and, in December 2003, adopted a written Asset Allocation Study. The Asset Allocation Study summarizes the Board's investment policies and measures of performance, formally documents objectives of the Board, and details a strategic plan for the Board. Criteria for the review and evaluation of investment managers are included in the Asset Allocation Study. Additionally, a methodology and format is outlined to highlight the results of the objectives and goals established within the Asset Allocation Study. The Asset Allocation Study reaffirms the broadly diversified investment strategy that has been pursued by the Board with the belief that, over a period of time, this approach will maximize investment return within a prudent level of risk. In March 2008, the Asset Allocation Study was updated to incorporate asset classes and revise asset allocation percentages.

Members of the Board of Directors as of June 30, 2008 include:

Guy W. Alongi	Treasurer Alexi Giannoulis
James Buchanan	Justice Thomas E. Hoffman
Allison S. Davis	Gordon John Mazzotti
Michael Goetz	Representative Kurt M. Granberg
Ronald E. Powell	

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

The Board has established both long-term and short-term goals with the intention of maximizing earnings for Member Retirement Systems' investments. These goals are reviewed in accordance with the Strategic Investment Policy.

Number of Employees

The Board had 10 full-time employees and June 30, 2008 and 9 full-time employees at June 30, 2007.

Derivative Securities

Some of the Board's managers invest in derivative securities. A derivative security is an investment whose payoff depends upon the value of other assets such as bond and stock prices, a market index, or commodity prices. The Board's investments in derivatives are not leveraged. Obligations to purchase (long a financial future or a call option) are held in cash or cash equivalents. In the case of obligations to sell (short a financial future or a put option), the reference security is held in the portfolio. Derivative transactions involve, to varying degrees, credit risk and market risk. Credit risk is the possibility that a loss may occur because a party to a transaction fails to perform according to terms. Market risk is the possibility that a change in interest or currency rates will cause the value of a financial instrument to decrease or become more costly to settle. The market risk associated with derivatives, the prices of which are constantly fluctuating, is regulated by imposing strict limits as to the types, amounts, and degree of risk that investment managers may undertake. The Board of Trustees and senior management approve these limits, and the risk positions of the investment managers are reviewed on a regular basis to monitor compliance with the limits.

During the year, derivative investments included forward foreign currency contracts, collateralized mortgage obligations (CMOs), futures, and options. The remaining derivative securities are used to improve the yields or to hedge changes in interest rates.

Forward foreign currency contracts are used to hedge against the currency risk in the Board's foreign stock and fixed income portfolios. Forward foreign currency contracts are agreements to buy or sell specific amounts of a foreign currency at a specified delivery or maturity date for an agreed upon price. As the market values of the forward contracts vary, the Board records an unrealized gain or loss. Forward foreign currency contracts represent an off-balance-sheet obligation, as there are no balance sheet assets or liabilities associated with those contracts. The market values of forward foreign currency contracts outstanding at June 30, 2008 and 2007 were as follows:

	<u>Cost</u>	<u>Fair value</u>	<u>Gain/loss</u>
June 30, 2008:			
Forward currency purchases	\$ 6,018,928	\$ 6,025,470	\$ 6,542
Forward currency sales	5,890,350	5,969,514	(79,164)
Total gain/(loss)			<u>\$ (72,622)</u>
June 30, 2007:			
Forward currency purchases	\$ 1,559,632	\$ 1,550,171	\$ (9,461)
Forward currency sales	7,691,150	7,790,385	(99,235)
Total gain/(loss)			<u>\$ (108,696)</u>

The Board also invests in mortgage-backed securities to maximize yields and to hedge against a rise in interest rates. These securities are based on cash flows from principal and interest payments on underlying mortgages. The value, liquidity and

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

related income of these securities are sensitive to prepayments by mortgagees, changes in economic conditions, including real estate values, delinquencies or defaults, or both, and may be adversely affected by shifts in the market's perception of the issuers and insurers and changes in interest rates. As of June 30, 2008 and 2007, the fair value of the Board's CMO holdings totaled \$165,456,226 and \$170,384,277, respectively.

The Board's investment managers utilize financial futures to replicate an underlying security they desire to hold (sell) in the portfolio. In certain instances, it may be beneficial to own a futures contract rather than the underlying security (arbitrage). Financial futures contracts are also used to improve the yield or adjust the duration of the portfolio. Financial futures contracts are agreements to buy or sell a specified amount at a specified delivery or maturity date for an agreed upon price. The market values of the future contracts vary from the original contract price; a gain or loss is recognized and paid to or received from the clearinghouse. Financial futures represent an off-balance-sheet obligation, as there are no balance sheet assets or liabilities associated with those contracts. The cash or securities to meet these obligations are held in the investment portfolio.

The Board's investment managers utilize options in an effort to add value to the portfolio (collect premiums) or protect (hedge) a position in the portfolio. Options are agreements that give one party the right, but not the obligation, to buy or sell a specific amount of an asset for a specific price (called the strike price) on or before a specified expiration date. As the writer of financial options, the Board receives a premium at the outset of the agreement and bears the risk of an unfavorable change in the price of the instrument underlying the option. As the purchaser, the Board pays a premium at the outset of the agreement and the counterparty bears the risk of an unfavorable change in the price of the financial instrument underlying the option.

The following table shows the futures and options positions held by the Board as of June 30, 2008 and 2007:

	2008		2007	
	Number of contracts	Contract principal*	Number of contracts	Contract principal*
Domestic:				
Equity futures purchased	1,892	\$ 122,985,600	2,169	\$ 168,891,330
Fixed income futures purchased	3	599,694	609	77,268,953
Fixed income futures sold	790	167,444,230	1,333	248,776,093
Fixed income written put options	347	34,700,000	78	33,000,000
Fixed income written call options	283	28,300,000	209	74,900,000
Fixed income purchased call options	-	-	241	241,000,000

*Contract principal amounts shown represent the market value of the underlying assets the contracts control. Contract principal is shown to present the volume of the transactions but does not reflect the extent to which positions may offset one another. These amounts do not represent the much smaller amounts potentially subject to risk. Contract principal values also do not represent actual balance sheet values.

Securities Lending Program

The Board participates in a securities lending program with State Street Bank and Trust who acts as securities lending agent. Securities are loaned to brokers and, in return, the Board has rights to a portion of a collateral pool. All of the securities are eligible for the securities lending program. Collateral consists solely of cash, letters of credit, commercial paper and

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

government securities having a market value equal to or exceeding 102% of the value of the loaned securities (105% for non-U.S. securities). In the event of borrower default, State Street provides the Board with counterparty default indemnification. The Board had no credit risk as a result of its securities lending program as the collateral held exceeded the market value of the securities loaned. As of June 30, 2008 and 2007, there were outstanding loaned investment securities having market values of \$1,851,952,625 and \$2,129,513,426, respectively, against which collateral was received with a value of \$1,912,742,552 and \$2,189,767,674, respectively. Collateral received at June 30, 2008 and 2007 consisted of \$1,703,959,890 and \$2,084,820,497, respectively, in cash and \$208,782,662 and \$104,947,177, respectively, in securities for which the Board does not have the ability to pledge or sell.

Proceeds from General Obligation Bonds, Pension Funding Series June 2003 (Unaudited)

Public Act 93-0002 (the Act) became effective on April 7, 2003 and authorized the State of Illinois to issue \$10 billion of General Obligation Bonds for the purpose of making contributions to designated retirement systems. The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System are "designated retirement systems" for the purpose of this law.

On June 12, 2003, the State of Illinois issued \$10 billion of General Obligation Bonds, Pension Funding Series June 2003. The net bond proceeds were allocated among the five state-funded retirement systems to reduce their actuarial reserve deficiencies as provided in the Act.

The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System received an allocation of bond proceeds equal to \$1,544,924,744 on July 1, 2003. The monies were deposited into the Master Trust Account with the Illinois State Board of Investment, on July 2, 2003. The Board initially approved investing the pension bond proceeds in separate index funds. These index funds were subsequently liquidated and combined with the Board's other investments and invested in accordance with the asset allocation policy of the Board during the year ended June 30, 2004. The Board estimates the return of the pension bond proceeds earned an annual rate of return of (6.2)% during the year ended June 30, 2008, which is the same as the overall return for the Board's investment portfolio.

Third-Party Marketing Fees Paid (Unaudited)

The Board disclosed that investment managers hired marketing groups to assist with promoting their investment product to the Board. Marketing fees paid by investment managers were as follows:

Investment Manager	Third Party Marketer	Type of Fund	Year ended June 30,	
			2008	2007
Alinda Infrastructure Fund	C.P. Eaton & Associates	Infrastructure	\$ -	\$ 399,614
Blackstone Capital Ptrs. V	Park Hill Group	Private Equity	50,000	175,000
Castil Ventures	Connors & Co.	Private Equity	75,000	75,000
Court Square Capital Partners II	UBS P.E. Funds Group	Private Equity	168,000	229,625
Ironbridge Capital	Frontier Partners-Fronterage Asset Mgmt.	Equity	248,520	198,337
Ivy Asset Management	The Marwood Group	Hedge Fund	319,068	301,939
Resolute II	Credit Suisse LLC	Private Equity	62,617	-
William Blair	Orlando Jones	Equity	105,212	176,395
			<u>\$ 1,028,417</u>	<u>\$ 1,555,910</u>

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

Service Efforts and Accomplishments (Unaudited)

For purposes of evaluating service efforts and accomplishments, three different measures have been included. One measure presents a historical perspective of overall annual and compound rates of return; another compares benchmark rates of return with actual rates of return by fund; and the last presents asset allocations by fund type.

Overall Rates of Return

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Annual total return	(6.2)%	17.1%	11.0%	10.1%	16.4%
Compound annual rate of return since July 1, 1982	11.2	11.5	10.7	10.7	10.8

Investment Returns – Benchmark and Actual

The Board operates under a long-range investment plan with the objective to maximize the total rate of return. The objectives set forth are as follows:

- At least equal to the assumed actuarial interest rate, currently 8.5% per year
- At least equal to the return of a composite benchmark of market indices in the same proportions as the Board's asset allocation policy targets

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

The Board earned a total rate of return of (6.2)% for the year ended June 30, 2008, which did not meet the investment objectives.

	2008	2007	2006	2005	2004	(Annualized)	
						3 years	5 years
Total fund	(6.2)%	17.1%	11.0%	10.1%	16.4%	6.8%	19.3%
<i>Composite bench mark*</i>	(4.6)	16.4	11.5	10.9	16.3	7.3	9.8
<i>Consumer price index</i>	5.0	2.7	4.2	2.5	3.3	4.0	3.6
U.S. equities	(11.6)	19.9	10.7	9.3	21.7	5.5	9.2
<i>Russell 3000 Index</i>	(12.5)	20.1	9.6	8.1	20.5	4.7	8.4
International equities	(10.3)	28.8	28.9	14.8	29.8	14.2	17.2
<i>MSCI-EAFE Index</i>	(10.2)	27.5	27.1	14.1	32.9	13.3	17.2
Fixed income	5.3	6.9	0.8	6.9	0.7	4.3	4.1
<i>Lehman U.S. Universal Bond Index</i>	6.2	6.6	(0.3)	7.4	1.0	4.2	4.2
Real estate	2.6	15.3	19.5	14.8	9.1	12.2	12.1
<i>NCRIF Real Estate Index</i>	9.2	17.2	18.7	15.6	9.7	15.0	14.7
Private equity	(4.9)	31.7	21.3	29.6	16.9	15.0	17.2

* Composite benchmark:

Effective 04/2008: 30% Russell 3000; 20% MSCI-EAFE; 25% Lehman Universal; 10% NCRIF; 5% Venture Economic all Private Equity Index; 10% HFR Equity Hedged Index.

Effective 12/2003: 45% Wilshire 5000; 10% MSCI-EAFE; 25% Lehman Universal; 10% NCRIF; 5% Venture Economic all Private Equity Index; 5% HFR Equity Hedged Index.

Effective 04/2002: 46% Russell 3000; 15% MS-AC Free ex U.S.; 23% Lehman Universal; 8% NCRIF; 8% Russell 2000 +3.0%.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Analysis of Operations

Year ended June 30, 2008

Net Asset Allocations as of June 30, 2008

The investment policy of the Board establishes asset allocation targets and ranges for each asset class, selected to accomplish the long-range investment plan. The actual asset mix is roughly in line with the policy target, with modest over-allocations to U.S. equity and unallocated cash with offsetting under-allocations to international equity, alternative investments, and real estate.

	<u>Fair value</u>	<u>Actual asset mix</u>	<u>Policy target</u>
	(\$ million)		
U.S. equity	\$ 4,246,177,433	37%	30%
U.S. equity hedge funds	598,985,402	5%	10
International equity	1,984,917,495	17%	20
Fixed income ¹	2,023,215,463	18%	18
Bank Loans	202,137,983	2%	2
Real estate	1,332,081,349	12%	10
Private Equity ²	524,628,589	5%	5
Infrastructure ²	209,975,518	2%	5
Cash ³	192,933,929	2%	-
Total	<u>\$ 11,315,053,161</u>	<u>100%</u>	<u>100%</u>

¹ Maturities of one year or longer, including convertible bonds.

² Interests in limited partnerships and other entities which have limited liquidity.

³ Includes money market instruments and other assets, less liabilities.