SECOND QUARTER 2011 | PAT QUINN, GOVERNOR

Insight

A QUARTERLY PERIODICAL DEDICATED TO HELPING YOU PREPARE FOR TOMORROW

YOUR SAVINGS AND YOUR INCOME IN RETIREMENT

The amount of money you set aside now will make a big difference in your income after you retire. So will the way you withdraw from your savings when the time comes.

How Much Savings Will I Need?

This is the essential question every investor needs to answer. Unless you plan to scale back your lifestyle significantly in retirement, you should have enough to replace 75% of your preretirement income:

50% from your savings and 25% from other sources, which may include Social Security benefits, a pension, or part-time job. And you will need to draw on your nest egg in such a way that it lasts throughout your retirement, even if you live to age 95 or longer.

How Do I Make My Money Last?

After a lifetime of setting money aside, withdrawing from your savings can be confusing. One rule of thumb is to take no more than 4% of your retirement assets in the first year you stop working (age 65), then increase that dollar amount by 3% each subsequent year to keep pace with inflation. This can give you a good chance of having your money last until you're age 95. But keep in mind that 4% of your balance won't give you the income you need if your savings aren't ample enough.

Why Does My Savings Rate Matter?

Your retirement savings rate is the percentage of your gross paycheck—including your employer's matching contribution, if available—that you set aside for retirement. To see why it is so important, consider the three situations below:

Three investors, each 30 years old and earning $50,000, retire 35 years later with a salary of $140,000. To replace 50% of their final salary, they'll need $70,000 in retirement income from investments. Based on the 4% rule, they'll need $1,750,000 to generate that income in the first year of retirement.[1]

INVESTOR 1

Savings Rate 5%

Investor 1 retires with **$552,000**[2], which will provide $22,000, or 16% of preretirement income.

INVESTOR 2

Savings Rate 10%

Investor 2 saves **$1,103,000** by age 65, enough to generate $44,000, or 31% of preretirement income.

INVESTOR 3

Savings Rate 15%

Though it requires discipline, Investor 3 saves **$1,655,000**. That's enough to provide $66,000, or 47% of preretirement income.

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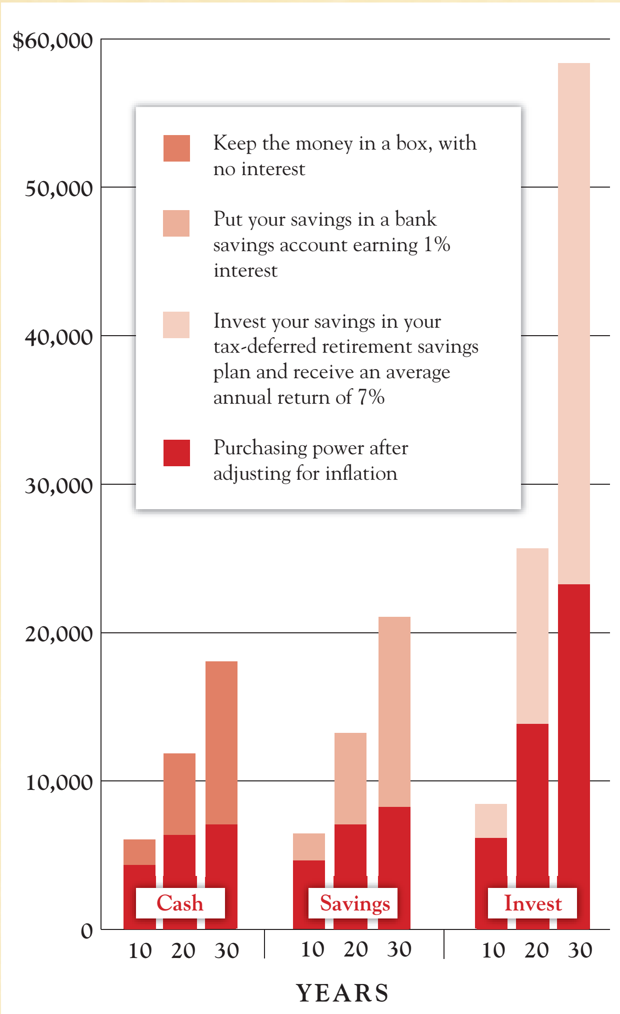
YOUR SAVINGS: THE INFLATION FACTOR

Saving enough for retirement means staying ahead of inflation. Here's a look at how three different approaches to saving $50 a month fare against an average annual 3% rise in the cost of goods and services.



Tax-deferred savings amount assumes only your contributions, not any employer contributions. This chart is for illustrative purposes only and not meant to represent the performance of any specific investment option.

To learn more about investing basics, visit our Investing 101 page at **troweprice.com/investing101**.

In What Order Do I Draw Down My Accounts?

Drawing from your accounts in a strategic way can maximize your investments' potential growth and help you reduce your tax bill. To accomplish both, consider withdrawing from any taxable accounts you have before you take savings from tax-advantaged accounts.[3] Leaving assets in tax-deferred and tax-free accounts untouched for as long as possible will help to maintain the tax-advantaged treatment of those assets and potentially help you financially during the latter years of your retirement.

[1] Salary increase assumes a 3% annual raise. Note that 4% of $1,750,000 is $70,000.

[2] Final balances assume an annual return of 7%. The examples are for illustrative purposes only and not meant to represent the performance of any specific investment option.

[3] Once you reach age 70½, you will have to take required minimum distributions (RMDs) from your tax-deferred accounts (other than Roth IRAs), although you may delay taking your first distribution until April 1 of the following year. (All subsequent distributions must be taken by December 31 of each year.)

GETTING ON COURSE FOR COLLEGE

Jen and Michael have a two-year-old daughter and another child on the way. They're eager to put aside money for college, but they've heard that having savings could hurt their chances of getting financial aid.

After doing some research, Jen and Michael find that their savings have little effect on needs-based federal aid, which is based primarily on a child's income and assets as well as the parents' income. And they learn that most aid is in the form of loans, which will need to be paid back. The most important fact: Federal aid formulas expect only 5.6% of parents' nonretirement assets to be used for education.[1] If Jen and Michael save $5,000 for college, the aid amount offered would be reduced by only $280—and they'll have money they wouldn't have had without saving. So the couple begin saving as much as they can for college.

Start Early, Stay Steady

First Jen and Michael make sure to contribute a full 15% of their income to their retirement savings Plan. Then the couple cut expenses to save for college, aiming to put aside $80,000 in 15 years. Starting right now, and assuming a 7% annual return, they only need to contribute a little over $250 per month. But if they wait five years, they'll have to nearly double their contributions to $462.

TELEPHONE NUMBERS

Deferred Compensation

Plan Rules/Options Information
800-442-1300/ 217-782-7006
TDD/TTY: 800-526-0844
Internet: http://www.state.il.us/cms/employee/defcom

Recordkeeper

T. Rowe Price Retirement Plan Services, Inc.
Account Value Information and Investment Changes:
888-457-5770 or TDD/TTY: 800-521-0325
Internet Access: 800-541-3022
Internet: http://rps.troweprice.com

Grading the 529

Jen and Michael fund a 529 college savings Plan—a tax-advantaged, state-sponsored account. If the money is used for qualified educational expenses, any earnings in the Plans are not subject to federal tax or, in most cases, state tax. If one of the couple's children doesn't need the money when the time comes, they can switch the Plan to benefit another member of the family.

Students can apply for and receive financial aid directly from their college or university, or from the federal government. Colleges and universities use a specific formula to calculate the Expected Family Contribution called the institutional methodology, which may differ from the federal formula. Because this can vary by institution, the student or parent should contact the particular college or university's financial aid office for specific details.

Please note that the Plan's disclosure document includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

[1]Federal Student Aid, www.studentaid.ed.gov.

UNEXPECTED EVENTS AND YOUR INVESTMENTS

Events in one country can affect financial markets around the globe—and this can have a major impact on consumers and their investments. What should you do to help insulate your portfolio from market swings?

A number of events this year have caused volatility in the financial markets. Political instability in the Middle East drove up oil prices significantly and unsettled stock markets around the world. Then a powerful earthquake and tsunami struck Japan, causing more volatility. The performance of the Standard & Poor's 500 Stock Index in the first quarter of this year tells the story: At one point, the benchmark was up 7%, only to lose those gains and a little more. Then the market recovered to end the quarter up 5.2%.

Market swings—whether they're declines or rises in asset prices—are a natural and inevitable part of investing. Be sure to spread your holdings among a wide variety of funds to keep your portfolio from being dependent on any one industry or sector. Do the same with your bond holdings by investing in domestic and international funds.* And be sure your asset allocation—the mix of stocks, bonds, and money market/stable investments—is appropriate for your time horizon, the years remaining until you begin drawing on your investments, and the amount of time you will need the money. Having both an asset allocation with enough stock funds and the proper diversification can help reduce your portfolio's volatility without sacrificing the return potential.

An investor who remains focused on the long term during market swings typically fares better than one who buys and sells investments when major events occur. And investing regularly through all the ups and downs means you will inevitably purchase assets when prices are low—and potentially benefit during any recoveries in the market.

**Diversification cannot assure a profit or protect against a loss in declining markets.*

You are invited to the 2011 Columbia Acorn Funds Shareholder Information Meeting

The Columbia Acorn Funds will be hosting their annual shareholder information meeting on September 21, 2011, in Chicago. The meeting will be held at Drinker Biddle & Reath LLP, which is located at 191 North Wacker Drive, Suite 3700. This is a new location for this annual event. The building is located at the corner of North Wacker Drive and Lake Street and it is recommended that attendees keep the Wacker Drive construction project in mind when planning their route to the meeting. The building is easily accessed via its Wacker Drive entrance but road repairs have closed other blocks of Wacker Drive.

The meeting will start at 12 p.m. central time and will feature presentations by Columbia Acorn Fund's lead portfolio manager Chuck McQuaid and other members of the investment team. Those attending will also have an opportunity to ask questions following the presentations. A buffet lunch will be provided prior to the meeting at 11:30 a.m.

If you are interested in attending this year's meeting, please RSVP by calling the Columbia Acorn Funds at (800) 922-6769 by Friday, September 16, 2011. Information on the meeting will also be available in July on the company's website, www.columbiamanagement.com.

YOU ARE INVITED TO THE 2011 COLUMBIA ACORN FUNDS SHAREHOLDER INFORMATION MEETING

Where: Drinker Biddle & Reath LLP
191 North Wacker Drive, Suite 3700
Chicago, Illinois

When: Wednesday, September 21, 2011 12 p.m. CST

Buffet lunch served at 11:30 a.m.

RSVP: (800) 922-6769 by September 16, 2011

WHAT DOES BEING ON THE "WATCH LIST" MEAN?

It is important that you understand what it means to be on the watch list and, perhaps more importantly, what it does not mean. Being on the watch list, as the name would imply, simply means we believe there is good reason to watch this fund more closely. Being on the watch list does not mean you should immediately sell your fund shares. It is not unusual for a fund to appear on the list from time to time. It does not mean the fund is necessarily a bad investment. If we believe the fund no longer represents a suitable investment option, we will remove the fund from the Plan.

Why are funds placed on the watch list?

Funds can be placed on the watch list for several reasons. Why a fund is on the watch list is more important than the mere fact that it is on the watch list. The most typical reasons are as follows:

1. **Performance—**The most common reason a fund is placed on the watch list is poor performance relative to its appropriate market benchmark and/or peer group. When signs of relative underperformance appear, we place a fund on the watch list.
2. **Risk—**Less obvious to many participants is the risk that a fund manager incurs. If a fund becomes too volatile, we will place it on the watch list.
3. **Risk-Adjusted Returns—**What returns has the fund manager been able to deliver relative to the risk the fund has incurred? If the manager is unable to deliver adequate returns for the risk taken, we will place the fund on the watch list.
4. **Portfolio Construction/Style Drift—**Is the fund manager investing the money in the way he or she said? If you invest part of your assets in an aggressive fund that is supposed to be investing in the stocks of small, growth-oriented companies, then you want the manager to do just that. We monitor the manager's portfolio and if the security holdings do not reflect what has been communicated, we place the fund on the watch list.
5. **Operations—**There are many operational reasons for placing a fund on the watch list. For example, the manager of the fund could leave. Remember, when you purchase shares of a mutual fund, what you are really doing is hiring a professional portfolio manager to invest your money. If that manager leaves, you should watch the fund closely. There could also be firm-level issues. These can include issues such as regulatory violations, turnover in senior management, or a merger or acquisition. Any of these operational issues will automatically place a fund on the watch list.

WATCH LIST—THE STATE OF ILLINOIS DEFERRED COMPENSATION PLAN

Current Watch List Summary

The following funds are on the watch list as of 6/30/2011:

The State of Illinois Deferred Compensation Plan Current Watch List

Ariel Fund: The fund's performance over the past two calendar years of 2009 and 2010 was very strong. In 2009 the fund ranked in the 5th percentile of their comparative peer group and ranked in the 25th percentile in 2010. The fund's holdings in the media and consumer luxury goods names propelled returns higher. However, due to lagging performance in the periods prior to 2009, the five year annualized return continues to underperform the benchmark and currently ranks in the third quartile of its peer group. In the first quarter of this year, the significant overweighting to consumer names as well as a lack of exposure to energy stocks detracted from results. The energy sector posted the greatest returns of any other sector in the first quarter. Over the first five months in 2011, the fund is lagging its peer group and the benchmark. This fund will remain on the watch list due to longer term underperformance. Participants also have access to the Northern Small-Cap Value Fund which invests in a small-cap value equity style.

Invesco International Growth Fund: The fund was recently placed on watch list status due to a notable change in the lead portfolio management team. On Friday, June 10, 2011, Invesco announced the departure of long-term co-lead portfolio manager, Barrett Sides. Mr. Sides has worked alongside his counterpart co-lead portfolio manager, Clas Olson, since 1994. Mr. Olson will assume full lead portfolio manager responsibilities and will maintain this structure going forward. Over the years, Invesco has added investment professionals to the team which now has 9 portfolio managers and 4 analysts. Invesco also plans to add an additional analyst to the research team over the course of the next year. However, due to the departure of one of the co-lead portfolio managers, the fund will be closely monitored over the next year. An alternative fund for participants to choose is the Janus Overseas Fund as it also invests inlarge-cap international stocks.

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