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SOCIALLY SCREENED INVESTING: COMBINING COMPETITIVE RETURN POTENTIAL WITH INVESTORS' VALUES

From global climate change to civil strife in the Sudan, a host of issues continue to fuel investor interest in socially responsible investing (SRI). In its latest report on SRI trends, the Social Investment Forum (www.socialinvest.org) identified \$2.29 trillion in total assets under management in the United States that use one or more of the three core socially responsible investing strategies: screening, shareholder advocacy and community investing¹. Screening—the practice of including or excluding securities based, at least in part, on social and environmental criteria—continues to be the most widely used SRI approach.

Socially screened mutual funds, variable annuities and other pooled accounts make up the fastest-growing segment of the SRI space. At the end of 2005, assets in these types of accounts totaled \$179 billion (see Figure 2). Of this amount, the CREF Social Choice Account represented \$7.8 billion (more than 4% of the total), making it the largest socially screened investment fund for individual investors. As of 12/31/06, the account's assets had grown to \$8.7 billion. In addition to the CREF Social Choice Account, which includes both equity and fixed-income segments, TIAA-CREF offers socially screened equity-only portfolios through mutual funds and other vehicles available to individual and institutional investors.



¹ http://www.socialinvest.org/areas/research/trends/sri_trends_report_2005.pdf.

FIGURE 1
NUMBER OF SOCIALLY SCREENED PORTFOLIOS
2001–2005

	2001	2003	2005
Mutual Funds	154	178	151
Variable Annuities	13	11	22
Other Pooled Products	14	11	28
TOTAL	181	200	201

Source: Social Investment Forum Foundation

FIGURE 2
ASSETS OF SOCIALLY SCREENED PORTFOLIOS
2001–2005

(In billions)	2001	2003	2005
Mutual Funds	\$111	\$127	\$148
Variable Annuities	\$7	\$2	\$11
Other Pooled Products	\$18	\$22	\$19
TOTAL	\$136	\$151	\$179

Source: Social Investment Forum Foundation

WHY INTEREST IN SOCIAL SCREENING CONTINUES TO GROW

Among the most important factors driving the growth in SRI is investor realization that competitive long-term returns are possible while incorporating social screening in the investment process. In addition, the scope of SRI has evolved over the years to reflect a broader array of issues. During the 1980s and 1990s, investment-related advocacy often focused on a single issue (such as apartheid in South Africa) or product (tobacco). Because of this relatively narrow approach, many investment firms viewed SRI, including social screening, as an isolated, possibly fleeting niche opportunity.

However, following the fall of apartheid, interest in SRI grew steadily. Socially conscious investors began to focus on the role of corporations in relation to broader, global issues. Public concern about the potentially negative impacts of globalization (including the Exxon Valdez oil spill and accusations of child and sweatshop labor at Nike and Wal-Mart) further drove demand for “non-financial” indicators of corporate citizenship. More recently, corporate governance scandals at companies like Enron and Worldcom also accelerated interest in SRI products.

Currently, socially screened pools of assets tend to be defined by the application of some combination of environmental, social and governance (“ESG”) factors. Examples of ESG issues include the near consensus emerging about the link between human activity and climate change (environmental); concern over investments related to the crisis in Sudan’s Darfur region (social); and perceptions of disproportionate executive pay (governance).

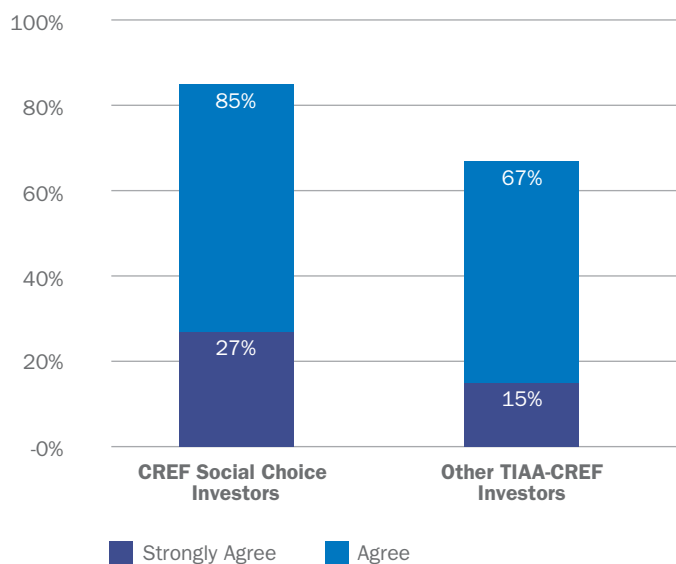
TIAA-CREF PARTICIPANTS EXPRESS STRONG INTEREST IN SRI

TIAA-CREF launched the CREF Social Choice Account in 1990, reflecting strong participant interest in a socially screened investment option. As the account’s assets have grown over the years, so too has our commitment to enhancing the account and to exploring additional ways to meet growing participant interest in SRI. One of these ways was to create socially screened equity mutual funds, including the TIAA-CREF Institutional Social Choice Equity Fund, launched in 1999.

In July 2006, TIAA-CREF released the results of a participant survey on SRI-related issues. The survey found that while financial return is a primary driver of participants’ investment decisions, the majority want their social values reflected in their investments. The survey also indicated that while 15% of participants use the CREF Social Choice Account, support for the underlying concepts and principles of SRI is even more widespread, as shown in Figure 3. (You can access the survey results on the TIAA-CREF website by visiting http://www.tiaa-cref.org/about/press/pdf/sri_memo.pdf.)

FIGURE 3
SURVEY RESULTS: STRONG INTEREST IN SRI

“When making investment decisions, what is most important to me is ensuring that my investment decisions reflect my personal values about social and environmental impacts.”



Source: “How SRI is Viewed by SCA and Non-SCA Participants,” Greenberg Quinlen Rosner Research, 2005–2006.

TIAA-CREF’S APPROACH TO OPTIMIZING SOCIAL SCREENS

There are a number of approaches to social screening. Some investment firms use in-house ESG analysis to build a “buy” list from a universe of acceptable companies; others attempt to build ESG analysis into a traditional active stock selection and portfolio construction process; still others rely on an indexing approach based on a social index (i.e., a socially screened variation of a widely used benchmark such as the S&P 500 Index).

TIAA-CREF’s process combines the social screening that underlies social indexes with a systematic approach to help minimize tracking error versus the Russell 3000 Index, a mainstream broad-market benchmark. (“Tracking error” means the degree to which the portfolio’s performance differs from that of the benchmark.) We use the same methodology across all of our socially screened equity

portfolios, including the equity portion of the CREF Social Choice Account and our institutional and retail Social Choice Equity Funds.

To construct our screened portfolios, we first perform an ESG analysis by using the Broad Market Social Index (BMSI), published by KLD Research & Analytics, Inc., as our “buy list.” (KLD Research & Analytics, Inc. is an independent investment research firm providing management tools to professionals integrating environmental, social and governance factors into their investment decisions.)

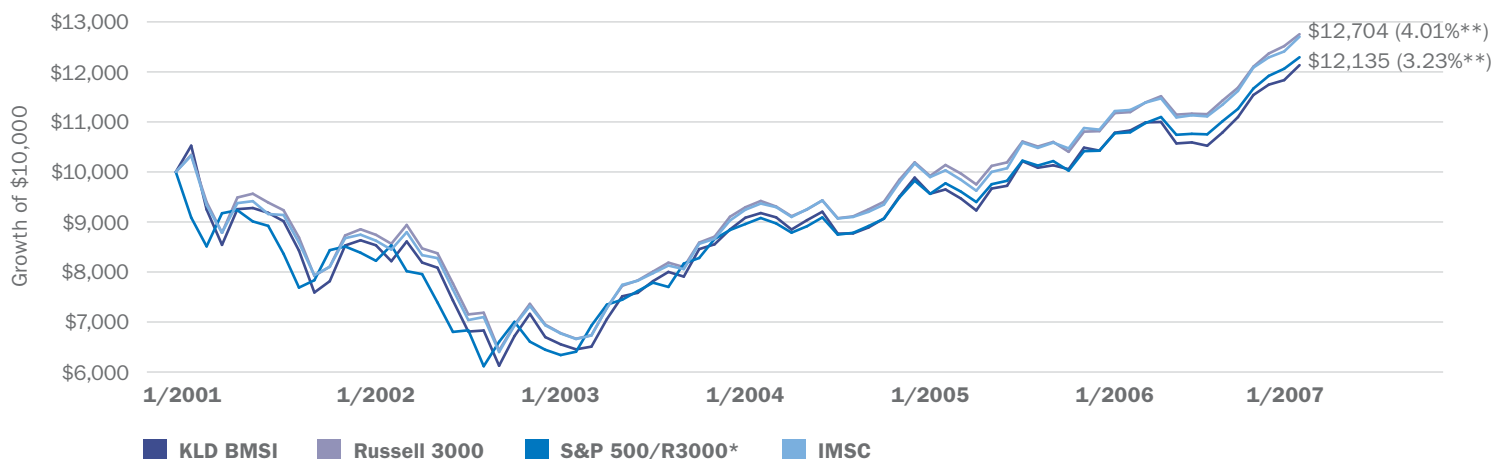
We then use a proprietary optimization technique to match the risk characteristics of the Russell 3000 benchmark. The intention is to neutralize, as much as possible, the inherent biases of a screened universe of companies.

This process is both comprehensive and flexible, enabling to respond to topical issues and concerns. Moreover, we believe our approach serves the interests of our participants by offering a combination of social screening, transparency and the potential for competitive investment returns.

Although past performance is no guarantee of future results, investment returns using our optimization approach have been competitive, as shown in figure 4. This graph charts the growth of a hypothetical \$10,000 investment in the TIAA-CREF Institutional Social Choice Equity Fund – Institutional Class (IMSC) from January 1, 2001, through January 31, 2007. For the purpose of comparison, the graph also shows the change in values of the KLD Broad Market Social Index (BMSI); the fund’s current benchmark, the Russell 3000 Index; and a blend of the Russell 3000 and S&P 500 indexes.

FIGURE 4

GROWTH OF \$10,000 SINCE JANUARY 1, 2001



* Blended benchmark. (The fund's benchmark changed from the S&P 500 to the Russell 3000 on 7/1/02.)

** Returns shown in parentheses are annualized.

Note: To represent the equity performance of our SRI methodology, Figure 4 shows performance of the TIAA-CREF Institutional Social Choice Equity Fund rather than that of the CREF Social Choice Account, since the CREF Social Choice Account is a balanced portfolio that uses a composite equity/fixed income benchmark.

TIAA-CREF INSTITUTIONAL SOCIAL CHOICE EQUITY FUND
(INSTITUTIONAL CLASS)

AVERAGE ANNUAL TOTAL RETURNS AS OF 12/31/2006***

1 Year	5 Years	Since Inception (7/1/1999)
14.40%	7.24%	2.84%

***Performance shown was impacted by a misallocation of income and net capital gains among the fund's share classes. If this misallocation had not occurred, the 1-year, 5-year and since-inception average annual total returns would have been 13.52%, 7.06% and 2.72% respectively. Teachers Advisors, Inc. made a cash infusion into the fund in August 2006 to address the impact of this misallocation. For additional information, please contact our Telephone Counseling Center at 800 927-3059.

The performance data quoted represents past performance and is no guarantee of future results. Your returns and the principal value of your investment will fluctuate so that your shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance quoted above. For performance current to the most recent month-end, visit the TIAA-CREF Website at www.tiaa-cref.org, or call 877 518-9161.

The fund is subject to market risk, company risk and moderate index risk. In addition, because its social criteria exclude securities of certain issuers for non-financial reasons, this Fund may forgo some market opportunities available to Funds that don't use these criteria.

LOOKING AHEAD: TIAA-CREF'S COMMITMENT TO SOCIALLY RESPONSIBLE INVESTING

Through the CREF Social Choice Account and other pooled funds, TIAA-CREF has demonstrated its ability and commitment to serve participants' growing interest in socially responsible investment options. We will continue to explore new opportunities in the SRI arena, led by our Social and Community Investing Department, which was created in May 2006. This department is dedicated to increasing TIAA-CREF Asset Management's focus on several aspects of socially responsible investing. For more information, please visit http://www.tiaa-cref.org/about/press/about_us/releases/pressrelease177.html

TIAA-CREF is a national financial services organization and the leading provider of retirement services in the academic, research, medical and cultural fields with over \$400 billion in combined assets under management (12/31/06). Further information can be found at www.tiaa-cref.org.

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Brett Hammond, Leo Kamp and Douglas Fore are available to comment on economic data. If you wish to speak with them, please contact Chad Peterson, Media Relations, 212-916-4808 or email cpeterson@tiaa-cref.org.

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