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Systematic vs. residual risk contribution
Asset allocation vs. selection risk contribution
  - What are the sources of volatility?
  - What factors drive performance?
    - Is the fund adequately diversified?
Sharpe ratio (total risk)
Information ratio (active risk)
  - Are risk exposures being rewarded?
  - Historical risk adjusted returns
Performance Attribution
  - What are the sources of active return?
    - Asset allocation versus security selection
    - Which asset classes contributed or detracted from return?
Risk Metrics for UCRP
Asset Allocation

- Total Risk is largely related to the allocation between equity and bonds
- The portfolio had a small overweight to public market equities during Q1 2011
Asset Allocation and Risk

Note: Exposures and Risk charts below are shown using March 1, 2011 target asset weights. Systematic risk is estimated using long term forecasts [from Mercer Investment Consulting, January 2011], not recent realized volatility.

(Lower Left) Asset weights are measured relative to Current Policy. The fund has an overweight in U.S. equity and Private equity and underweight in Core Bonds and TIPS.

(Lower Right)
- The fund’s forecast total systematic risk (blue bars) is 14.75% annualized standard deviation. It is heavily weighted to US and Non-US developed equity (67% of total).
- Forecast active systematic risk is down slightly at 33 bp. The US equity and Private equity overweights accounted for over 100% of this amount (red bars).
Expected Risk and Return

Forecast risk and return (using Mercer’s January 2011 capital markets assumptions) lies near the constrained efficient frontier; long-term forecast return of the current policy allocation of 8.1%* is close to the actuarially required return of 7.5%.

*Asset Class returns and efficient frontiers are shown in the chart as arithmetic (i.e., average) expected returns.

The projected compound annual return over multi-year horizon is 8.1% for the Current Policy weights.

Forecast volatility of the current policy is 14.5%.
The Pension Fund’s liabilities have been growing steadily (upper left) with University employment, while the assets have grown (and fallen) with the equity markets. The ratio of actives to retirees has recently fallen from 3x to 2x (lower left).

The Funded Ratio (= the ratio of assets to liabilities), is an overall metric of the financial health of a pension plan. This ratio has fluctuated considerably over the past (lower right), and has recently fallen below 100% with the bear market of 2007-09.
Forecast Funded Status

- Contributions were suspended in 1990, but annual benefit payments have grown in line with and recently exceeded, Normal Cost over the last decade (upper left).
- The bottom two charts show projected funded ratio with planned contributions (left) and with contributions equal to Normal Cost + amortization of unfunded liability (right), assuming a constant 7.5% investment return beginning FY 2011.

Note that even a maximum level of contributions barely increase the funded ratio over this forecast period.

These projections are approximations only, developed by Treasurer’s Office, not Segal Co.
Risk Measures: Total

Total risk trend quite similar to benchmark; recently Plan volatility has been slightly less than the Budget, but well within ranges. Total volatility has resumed a historically normal range, higher than the mid 2000’s but lower than the 2008-09 crash.

Total Risk budget equals Benchmark risk plus the Active risk budget. The ranges are +/- 20% around the budget.

Risk is measured by standard deviation of monthly total returns; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights. (This and following charts show risk budgets as if they had been in place during entire historical period.)
The spike in Active Risk in Q1 09 resulted from the underweight in equity as the market fell and then rallied. Active risk has currently resumed its low level of the mid 2000’s (about 0.50% annualized standard deviation). It is still well below long term expectations for active return, but is well diversified.

Risk is measured by standard deviation of monthly active returns; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights.

The Active risk budget is 3% annualized Tracking Error (adjusted for market volatility), with ranges of +/- 1 pct. point around Budget.
Risk Attribution

(Virtual Left) Virtually all of Total Risk is attributed to systematic (market) factors (red bars).

(Lower Right) Normally, the majority of Active Risk is attributed to security selection. When asset allocation transitions are implemented, allocation risk increases. During the market turmoil, equity overweight/underweight dominated all other decisions, but for the past 4 quarters residual risk is resuming its normal contribution.

Risk is measured here by variance (standard deviation squared) of monthly returns; each bar shows a 12-month measurement period.

Systematic Risk is associated with benchmark exposures; residual risk is associated with non-benchmark decisions (security selection).
Risk Adjusted Return: Total

Sharpe ratio is “excess” return (total return less risk-free rate) divided by total risk; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights.

Sharpe Ratio (risk adjusted total return) trend has been quite similar to the benchmark for the past 5 years. The 12 month return on risky assets is positive but diminished after the May 2010 market decline.
Information ratio (risk adjusted active return) is the result of both asset weighting decisions and active performance. It is higher when the returns are positive and more consistent (less volatile). The Info. ratio has been positive for the past 4 quarters; from the graph below, active returns for the past 7 quarters have been small but positive.

Information ratio is active return (total return less benchmark) divided by active risk; each point shows a 12 month measurement period. The Significance level is the probability that results are due to skill, with 50% being a neutral measure. All risk calculations done using exponentially declining weights.
Active Return for the Quarter was +0.10% (Fund return of 3.81% vs. policy benchmark of 3.71%).

[BELLOW] Asset allocation decisions (blue bars) added 0.07% (equity overweight and core bond underweight). Security selection decisions (red bars) added 0.03% (primarily Absolute Returns offset by public equity).
Risk Metrics for GEP
Asset Allocation

- Total Risk is largely related to the allocation between equity and bonds.
- The portfolio was close to a neutral position in equities during Q1 2011.
Asset Allocation and Risk

**Note:** Exposures and Risk charts below are shown using March 1, 2011 target asset weights. Systematic risk is estimated using long term forecasts [from Mercer Investment Consulting, January 2011], not recent realized volatility.

**(Lower Left)** Asset weights are measured relative to Current Policy. The fund is overweight in US equity, Private equity, and Cross Asset Class strategies (CAC), and underweight in Emerging Market equity and TIPS.

**(Lower Right)** The fund’s forecast total systematic risk (blue bars) is 14.9% annualized standard deviation. It is evenly balanced among US equity, Non US developed equity, and Absolute Return (74% of total). Forecast active systematic risk is down slightly at 22 bp. The US Equity and Private equity overweights accounted for more than 100% of active risk (red bars).
Forecast risk and return (using Mercer's January 2011 capital markets assumptions) lies near the constrained efficient frontier; forecast return of the current policy mix of 8.4%* is close to the nominal return needed to maintain a constant real payout per student (estimated at 8.5%).

* Asset Class returns and Efficient frontiers are shown in the chart as arithmetic (average) expected returns.

The projected compound annual return over multi year horizon is 8.4% for the Current Policy weights.

Forecast volatility is 14.8%.
Risk Measures: Total

Total risk trend has been quite similar to benchmark; GEP volatility is quite close to its Budget. Total volatility has resumed a historically normal range, higher than the mid 2000’s but lower than the 2008-09 crash.

Total Risk budget equals Benchmark risk plus the Active risk budget. The ranges are +/- 20% around the budget.

Risk is measured by standard deviation of monthly total returns; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights. (Charts show risk budgets as if they had been in place during entire historical period.)
Active risk for the total fund has grown slowly over this period from 0.50% to 1.50% annualized standard deviation, up until the 2008 crash.

Active risk has resumed its low level of the mid 2000’s (about 1.0%), but is still well below long-term expectations for active return, and is well diversified.

The Active risk budget is 3.0% annualized Tracking Error (adj. for market volatility), with ranges of +/- 1 pct. point around Budget.

Risk is measured by standard deviation of monthly active returns; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights.
Risk Attribution

(Virtual Left) Virtually all of Total Risk is attributed to systematic (market) factors (red bars).

(Lower Right) Normally, the majority of Active Risk is attributed to security selection. When asset allocation transitions are implemented, allocation risk tends to dominate. In late 2009, the equity overweight dominated all other active decisions. For the past 12 months, residual risk has resumed its normal contribution level.

Risk is measured here by variance (standard deviation squared) of monthly returns; each bar shows a 12 month measurement period. Systematic risk is associated with benchmark exposures; residual risk is associated with non-benchmark decisions (security selection).

Office of the Treasurer of the Regents
University of California
Sharpe Ratio (risk adjusted total return) trend has been quite similar to the benchmark for the past 5 years. The 12 month return on risky assets is positive but diminished after the May 2010 market decline.

Sharpe ratio is “excess” return (total return less risk-free rate) divided by total risk; each point or bar shows a 12 month measurement period. All risk calculations done using exponentially declining weights.
Information ratio (risk adjusted active return) is the result of both asset weighting decisions and active equity and bond performance. It is higher when the returns are more consistent (less volatile). The information ratio has been positive for the past four quarters; active return has been small but on average, positive in the past 7 quarters.

Information ratio is active return (total return less benchmark) divided by active risk; each point shows a 12 month measurement period. The Significance level is the probability that results are due to skill, with 50% being a neutral measure. All risk calculations done using exponentially declining weights.
Active Return for the Quarter was +0.28% (Fund return of 3.43% vs. policy benchmark of 3.16%).

Asset allocation decisions (blue bars) added 0.03%.

Security selection decisions (red bars) added 0.25% (virtually all from Absolute Returns).

GEP Attribution for 3 mo. ending Mar-31-11

US Equity
Non-US Equity
Emg Mkt Equity
Global Equity
Core Bonds
HY Debt
EM Debt
TIPS
Private Equity
Abs Ret - Div.
Abs Ret - CAC
Real Assets
Real Estate

Adv. Active Weight

Avg. Active Return