October 3, 2008

The University of California Investments Remain Sound in Market Turmoil

The University's pension and endowment portfolios are well-diversified and recent stock market volatility is mitigated by investments in other asset classes. The University continues to focus on investing for the long term while finding opportunity within this changing market environment.

UC Pension and Endowment

The portfolio holdings within the University of California Retirement Plan (UCRP/pension) and the General Endowment Pool (GEP) are well-diversified among U.S. and foreign public equities, private equity, fixed income, real estate, and absolute return opportunities as shown in the current asset allocation policy below:

	Pension Policy %	Endowment Policy %
U.S. Equity	34.5	19.0
Non-U.S. Equity-Developed	22.0	18.0
Non-U.S. Equity-Emerging	4.0	5.0
Global Equity	2.0	2.0
Core Fixed Income	12.0	8.0
High Yield Bond	3.0	3.0
Non-U.S. Fixed Income	3.0	2.5
Emerging Market Debt	3.0	3.0
TIPS	6.0	4.0
Private Equity	4.0	7.0
Real Estate	3.0	5.0
Absolute Return	3.5	23.5
	100.0	100.0

It is important to note that the benefits paid by the UCRP are not directly impacted by gains or losses in its investments. The Regents, as Plan fiduciaries, have the responsibility to pay benefits accrued benefits as defined by the UC Retirement Plan (generally based on a participant's age, service credit and salary) regardless of investment returns. The investment objective of the plan is to earn a return over the long-term that will meet this responsibility. During some periods, the investment pool earns more, some times less, and which is to be expected in fluctuating markets. The current actuarial goal is 7.5% annual return.

UC Short Term Investment Portfolio (STIP)

The STIP portfolio is the cash investment pool in which the pension, endowment, and campus fund groups participate. It includes cash for payroll, operation expenses, and construction funds and is managed as a highly liquid portfolio. The STIP's primary investment objective is the safety of principal and Treasurer's Office Staff will continue to invest the University's short-term cash in high-quality, liquid securities.

None of the debt issuers behind the STIP investments has declared bankruptcy or missed a coupon payment. STIP has come through September's unprecedented turbulence intact and well positioned to take advantage of attractive valuations in high-quality assets.

UC Core Funds

The UC Core Funds are available for employees to invest in within the UC Retirement Savings Program's 403(b), 457(b) and DC Plans. The Treasurer's Office, which oversees the UC Core Funds, continues to monitor these funds and notes the following:

The UC **ICC Fund** does not own insurance company contracts with AIG. The Office continues to feel that the Fund is currently protected, as only financially strong institutions are selected and are actively monitored.

Like many other institutional investors in the U.S. and abroad, the UC **Savings Fund** has investments in Fannie Mae senior debentures. These bonds have traditionally offered the advantages of an AAA rating, very good liquidity, and a material yield advantage over comparable maturity U.S. Treasuries. Despite the turmoil in the financial markets, the senior debentures in the Savings Fund have maintained their value, and the Office of the Treasurer is highly confident they will continue to do so.

Because of ongoing stress in the housing and mortgage markets, the U.S. Treasury and the Federal Housing Finance Agency (FHFA) announced on September 7, 2008, a four-part plan to support the debt and primary mission of the Government-Sponsored Enterprises (GSEs). The main feature of this plan is that the FHFA would take over as conservator of Fannie Mae and Freddie Mac. The purpose of this move is to:

- Preserve the companies' assets
- Place them in a sound and solvent condition
- Insure that their business is conducted without interruption

In effect, as stated by the FHFA, this is a strong backing for their senior, subordinated, and mortgage-backed securities debt.

The Treasurer's Office continues to believe that holding GSE debt—and the UC Savings Fund's policies and strategies—are appropriate, given the Fund's objectives.

The UC **Bond Fund** is a diversified pool of fixed-income securities, including U.S. government, mortgage-backed, and corporate bond securities. Although the fund had modest exposures to Lehman Brothers and AIG debt, the benefits of diversification mitigated the impact on the overall fund. In the worst period for credit markets in history, the value of the Bond Fund has declined just over 1% since the fiscal year end, broadly in line with its benchmark—the Lehman Aggregate Bond Index.

The Treasurer's Office continues to monitor the markets closely and our short term performance will likely mirror broad market movements in the various asset classes. Although we believe markets may remain volatile for the near to intermediate future, we continue to focus on investment for the long term and finding opportunity within this challenging environment.

The policies of all Funds managed by the Treasurer have been reviewed and approved by the Regents Committee on Investments.