University of California Berkeley Foundation

ENDOWMENT RETURNS AND INVESTMENT POLICY

by **John-Austin Saviano**, Chief Investment Officer,
Berkeley Endowment Management Company

We closed another fiscal year with continued volatility in the markets — and Berkeley's endowment held its own through this tumult. As of June 30, 2012, the endowment's 10-year track record stands at an annualized 7.0% return vs. 6.1% for the portfolio's benchmark and 6.3% returns for global equity markets (the MSCI All Countries World Index). For the year, the portfolio recorded a -1.6% return vs. -3.1% for its benchmark and -6.0% for global equity markets.

In these challenging times for Berkeley's finances, the Berkeley Endowment Management Company (BEMCO) plays a key role in the campus's overall efforts to maintain the highest standards in all aspects of financial stewardship. As BEMCO enters its fourth year, we are making significant progress — making the most of existing endowment resources, building capabilities to encourage further giving, and leveraging the University's preeminent reputation and loyal alumni to engage the investment management community.

Background

The Foundation launched BEMCO in the fall of 2009 as an extension of its mission to steward endowment gifts given in support of the University. Our goal has been to create a professional investment management function that matches Berkeley's academic prowess.

The buildout of our operations and governance structure is now complete, and we are now staffed by a five-person investment team and overseen by a six-person board of directors. Building on the years of dedicated service from the Foundation's previous volunteer investment committee, we are reshaping the portfolio to make the most of our day-to-day professional management resources.

Goals and Approach

Endowment investing is a generations-long endeavor, and our measures of success are geared toward that time-frame. We seek to deliver results over rolling 10-year periods that keep up with the endowment's inflation-adjusted rate of spending (7.4% over the past 10 years) as well as keep up with a similar globally oriented portfolio of equities.

We build our portfolio with a goal of earning the required returns, but with lower levels of volatility than the markets and preserving sufficient liquidity. Diversification is key, and we use a flexible framework that focuses more on how an asset is expected to behave rather than its particular name. (For instance, we do not assume that all bonds are low-risk and all stocks are high-risk.)

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Our approach has been to partner with high-quality specialist investors in different segments of the financial markets, and build a portfolio of these top firms. This approach enables us to gain access to a breadth and level of investment talent that would be impossible to replicate in-house. We select these partners not just by their historical results, but also by our qualitative assessment of their team and organization based on a set of values that reflect the highest standards for stewardship.

Berkeley must compete with other investors for these highly sought-after opportunities — and, as noted below, we are making good progress.

Markets

Three years after the lowest point of the 2008–2009 financial crisis, the world economy and markets are still navigating uncertain terrain. Concerns in the banking and mortgage sector have moderated and been replaced with concerns over sovereign solvency in Europe, the 2012 presidential election and "fiscal cliff" in the U.S., and sustainability of growth in China and other emerging economies.

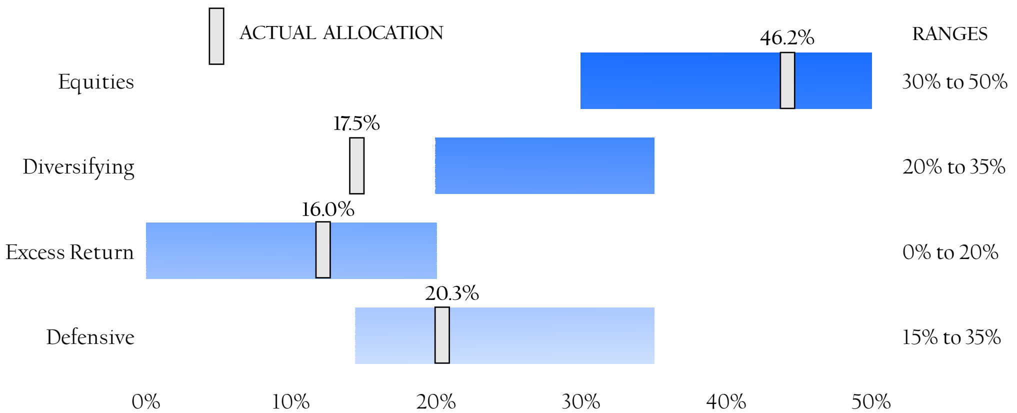
Central banks have unleashed a flood of liquidity into the markets, resulting in the lowest rates in sovereign bonds in generations. These breathtaking levels of monetary intervention are an attempt to ignite growth and to prevent destructive deflationary pressures from spiraling into a depression. The effectiveness of these measures is anything but certain, and the world's collective uncertainty is reflected in falling trading volumes, falling equity mutual fund ownership, rising corporate cash levels, and stubbornly low consumer confidence.

From Inception Through 2012

Against the backdrop of these market conditions and only three years into our startup, the BEMCO team remains focused on the task at hand: ensuring that we have a reasonably diversified portfolio that works with the most creative minds in the investment business.

To that end, we have been working to increase the portion of our portfolio whose success is not as directly tied to the ebbs and flows of the equity markets. In our portfolio framework, we characterize these as "Diversifying" strategies, and they include

Asset Allocation at June 30, 2012 vs. Policy Ranges



Note: Values may not sum to 100% due to rounding.

less directional hedge fund and certain real assets strategies. Since BEMCO's inception, we have moved these from 9.5% of the portfolio to 17.5% as of June 30, and we continue to add to them.

Within our other major categories — Equities, Excess Return and Defensive — we continue to improve our implementation. We have been able to engage with higher-quality managers and in many cases simplify the portfolio, making the most of our resources and research.

The table on the previous page shows our year-end asset allocation and reflects our ongoing work in reshaping the portfolio. As noted, we continue to build out our Diversifying exposures (currently below target) as we improve our roster of partners throughout the portfolio.

10-Year and 2012 Results

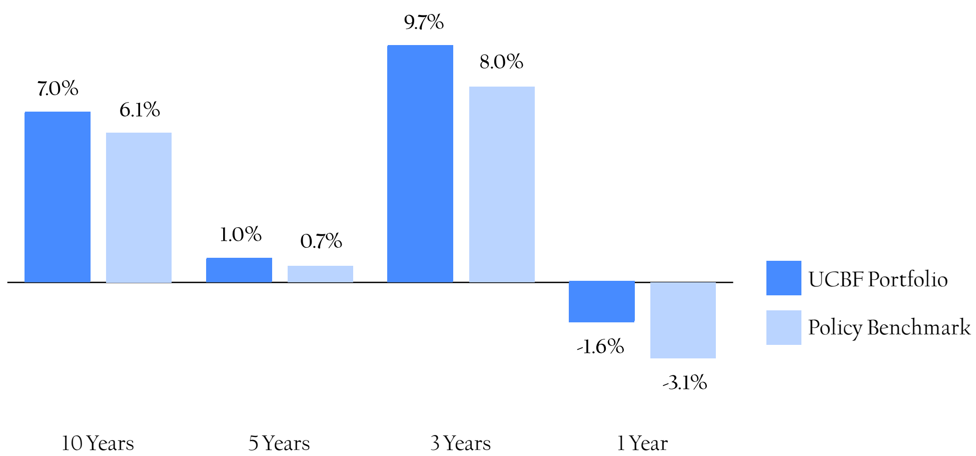
Endowment investing is a long-term enterprise, and our first measure is always our 10-year results vs. our mandate to support the Foundation's spending and, secondarily, keep up with other investable alternatives. The 10-year track record falls short of our primary goal (spending plus inflation was 7.4% annualized for the past 10 years) even while it outpaced our benchmark.

The Year Ahead

We know macro factors will continue to play a big part in the year ahead, but we are tempered by the humility of not knowing when or how they will play out. While the moves of electorates, central banks, and parliamentary bodies are all but impossible to predict, our work is clear. We continue to add sophistication to the management of Berkeley's endowment assets, forge new relationships, and keep our focus on supporting a sustainable payout to the University.

For additional details on BEMCO's staff and investment policy, visit www.berkeleyendowment.org.

Annualized Investment Results as of June 30, 2012



Berkeley Endowment managed by the UC Berkeley Foundation

	6/30/12	6/30/11	6/30/10	6/30/09	6/30/08
Market Value ($ thousands)	$1,126,822	$1,091,985	$895,456	$785,758	$920,926
Annual Return on Investment	-1.6%	18.9%	11.7%	-20.6%	-0.3%

UC Berkeley Foundation Payout

	2011–12	2010–11	2009–10	2008–09	2007–08
Annual Payout Policy Rate	4.27%	4.75%	4.75%	4.76%	5.00%
	Aug–12	Aug–11	Aug–10	Aug–09	Aug–08
Payout ($ thousands)	$36,492	$37,676	$36,570	$35,915	32,565

The UC Berkeley Foundation payout is based on a 12-quarter moving average rate. The payout figures above reflect actual distributions. While the majority of payout is distributed in August of each year, distributions do occur throughout the year, and those incremental distributions are included. The August 2011 figure reflects, for example, the total of distributions made in the 2011-12 fiscal year.