

The University of Houston System Endowment Fund



FISCAL YEAR 2008

JULY 31, 2008

Market Overview

In addition to the IndyMac Bank closure, the financial market crisis hit another previously overlooked sector: Government Sponsored Entities (GSEs) in July. The stability of Fannie Mae and Freddie Mac, the two giant mortgage companies that provide liquidity to the U.S. mortgage market by buying mortgages from local lenders and selling the repackaged assets back to the market, was questioned when analysts looked into the companies' assets and predicted growing losses as a result of rising mortgage defaults. As a consequence, volatility spiked again in July with losses extended in the first two weeks of the month, before staging a tentative rebound in the latter half.

Small Cap vs. Large Cap & Growth vs. Value

Small caps showed resilience in July, particularly small cap value which rallied over 5%. Except for the 3 year period, small cap stocks have outperformed large cap stocks for all periods measured.

Global Market Overview

Global equity markets continued their pullback in July. International equities, as measured by the MSCI EAFE Index, returned -3.2% for July. Similar to the U.S. equity markets, the MSCI EAFE value outperformed growth by 57 basis points for the month of July. Over longer time horizons, growth has outperformed value by a significant margin for the past quarter, 1 year and 3 year period.

Valuation

The market value at the end of July was \$536 million, including \$55 million of non-endowed funds invested in the endowment.

Performance

As indicated in table 1 below, the endowment's performance lagged the dynamic portfolio benchmark for the month, quarter, calendar-year-to-date and 1-year ending July 31, 2008. International equities, hedged equities and inflation hedges were the major contributors to the underperformance of the endowment for the periods measured. On the positive side, the endowment's asset allocation has protected some capital in this difficult market as the major equity markets are down much farther than the endowment.

Table 1	One Month	Three Months	Calendar YTD	One Year
UHS Endowment	-2.29%	-5.69%	-8.07%	-4.30%
Dynamic Portfolio Benchmark	-0.76%	-4.13%	-5.38%	-2.80%
DJIA	+0.43%	-10.65%	-13.00%	-11.71%
S&P 500 Index	-0.84%	-8.02%	-12.66%	-11.09%
Russell 1000 Index	-1.16%	-7.71%	-12.23%	-10.62%
Russell 2000 Index	+3.70%	+0.11%	-6.02%	-6.71%
NAREIT Equity	+3.47%	-7.07%	-0.26%	-3.08%
MSCI EAFE Index	-3.21%	-10.26%	-13.82%	-12.19%
Lehman Agg. Index	-0.08%	-0.89%	+1.04%	+6.15%
CPI-U	+0.53%	+2.39%	+4.73%	+5.60%

Asset Allocation

The portfolio's asset allocation is in compliance with the investment policy as indicated in table 2.

Table 2	Asset Allocation 07/31/08	Asset Allocation 07/31/08	FY 2008 Target Allocation	Long-term Target Allocation	Policy Range
Asset Class	\$000s	%	%	%	%
Equities					
US Equity	134,990	25.2	29.0	25.0	20 - 50
International	130,495	24.3	25.0	25.0	10 - 30
Total Equities	265,485	49.5	54.0	50.0	30 - 80
Fixed Income	83,629	15.6	15.0	15.0	15 - 30
Absolute Return	30,769	5.7	7.5	7.5	5 - 10
Hedged Equities	63,232	11.8	12.5	7.5	5 - 10
Inflation Hedge	75,354	14.0	10.0	10.0	5 - 15
Alternatives	4,299	0.8	1.0	10.0	0 - 10
Cash	13,728	2.6	0.0	0.0	
Total	536,496	100%	100%	100%	

Unfunded commitments to partnership investments were \$36.9 million at the end of July.