Treasurer's Annual Report

One hundred and thirty-fifth fiscal year
University of California • 2002-2003

The University of California

The University of California, founded in 1868, is a system of 10 campuses with a mission of teaching, research and public service. With over 197,000 graduate and undergraduate students, UC is the world's premier public university. UC has three law schools, five medical schools and the nation's largest continuing education program. The University also manages three national laboratories that are engaged in energy and environmental research. Its Natural Reserve System manages approximately 130,000 acres of natural habitats for research, teaching and outreach activities.

Campuses and National Laboratories

The Regents of the University of California

The University of California is governed by The Regents, a 26-member board, as established under Article IX, Section 9 of the California Constitution. The Treasurer of The Regents is responsible for managing the investments and cash for the University of California System. The Treasurer's Office carries out these activities under the policies established by the Investment Committee of The Regents of the University of California.

Treasurer's Annual Report Fiscal 2002-2003

Established in 1933, The Office of the Treasurer of The Regents has had a long and successful history of managing the University's pension and endowment funds. These investments provide substantial benefits to current and retired employees and support the University's mission of education, research and public service. The Treasurer's Office currently manages a portfolio of retirement and endowment funds totaling $53 billion.

FISCAL YEAR 2003 IN REVIEW

Financial markets grappled with several major themes during the fiscal year, including global political tensions, the lingering remnants of the technology bubble, and the threat of deflation. These uncertainties led to new multi-year lows in the broad equity indices and U.S. Treasury yields before economic activity rebounded after the military action in Iraq proved relatively swift.

Equity markets recovered over 25% from the lows, but produced only a small positive return of 0.74% for the entire period. While corporate profits rose 17% over last year, corporations continued to emphasize productivity gains and corporate balance sheet repair over job creation.

At the same time, intense global competitive pressures and general economic slack led to further disinflation in consumer prices. Against this backdrop, the Federal Reserve stated its intention to keep interest rates low for an extended time, and 10-year U.S. Treasuries ended the fiscal year at 3.5% vs 4.8% at 6/30/02. This produced a strong total return of 10.4% for the Lehman Aggregate Bond Index for the fiscal year.

Private Equity markets normally track public equities with a lag, so they did not participate in the late rally, but investment in this sector has begun to pick up after three years of reduced activity.

In addition to low interest rates and substantial savings from mortgage refinancings, consumers have benefited from aggressive fiscal stimulus, which appears to be paying off in robust Gross Domestic Product growth for the second half of calendar year 2003. While Treasury yields have risen since the end of the fiscal year in acknowledgment, some risks to a sustained rebound in world economic activity and equity valuations remain: sluggish employment gains, the rising U.S. budget deficit, high consumer debt levels, and the still tenuous situation in the Middle East.

MESSAGE FROM THE TREASURER

We are pleased to report that the University of California Retirement Plan (UCRP), the General Endowment Pool (GEP), High Income Pool (HIP) and the Short Term Investment Pool (STIP) all produced positive returns for the fiscal year: respectively UCRP 5.6%, GEP 5.4%, HIP 17.3%, and STIP 3.9%. All Regents' assets combined grew by $2.2 billion or $2,200 million over the previous fiscal year.

The UCRP grew by $949 million over the fiscal year, net of all payments to beneficiaries and expenses. As of January 1, 2003, the UCRP was over-funded by 129% on an actuarial basis. From January 1 to June 30, 2003 the UCRP portfolio gained 9.8%. The University is in an enviable position considering that many U.S. public and corporate plans are severely *under-funded*.

All of the UC-managed 403(b) and defined contribution plan funds' returns exceeded or matched the returns of their benchmarks: Equity Fund -1.2%, Bond Fund 12.5%, Multi-Asset Fund 4.5%, Savings Fund 4.7%, Insurance Company Contract Fund 6.3% and the Money Market Fund 1.5%.

During periods of volatile markets it is important that appropriate asset allocation planning be both appreciated and maintained. The Regents and our Office continually work toward improving returns while maintaining appropriate risk. To that end, several important changes occurred in the past fiscal year affecting your investment portfolios:

The historical returns for the internally managed U.S. equity portfolio, for both short and long term periods between July 1992 and June 2002, were less than the appropriate U.S. equity benchmark index (i.e. S&P 500 Index or Russell 3000 Index). After extensive consultation with outside investment professionals on The Regents Investment Advisory Board and The Regents Committee on Investments, I recommended the following enhancements to our U.S. equity allocation:

1. Transfer the internal management of the U.S. equity investments to multiple external managers.
2. Move from a single concentrated actively managed large capitalization strategy to a range of diversified equity strategies.

These recommendations were approved by The Regents at their November 14, 2002 meeting and were undertaken in order to improve equity investment performance, reduce overall portfolio risk exposures, and to better conform UC's practices to the national industry norm of institutional external equity management. It is both an extension of, and consistent with, the University's overall asset allocation investment strategy approved by The Regents in March 2000.

This diversification affects the U.S. and Non-U.S. Equity allocations within the GEP, the UCRP and the UC-managed Equity Fund. To initiate the transition to external equity management, the University transferred all of its internally managed U.S. equity investments into a Russell 3000 Tobacco-Free Index Fund managed by State Street Global Advisors, a leading institutional investment manager and UC's current passive index manager. This resulted in the closure of our internal equity portfolio management division. This transfer of $15 billion, from a concentrated portfolio of 156 stocks to a broadly diversified index fund, was completed between November 18 and 30, 2002.

We are in the process of building our External Management group whose role will be to determine the optimal range of equity strategies and implement the Request For Proposal (RFP) process being employed to hire qualified active external managers within each of these strategies. As external managers are hired, holdings will be transferred out of the domestic and international index funds. The objective is to retain investment managers who we expect will add value by outperforming their respective benchmark indices net of all management fees on a risk-adjusted basis. A Managing Director of Externally-Managed Investments was hired in June, and the initial RFP for U.S. Small Capitalization investment managers has been posted on our website at this writing.

In January 2003 we established the UC Private Equity Vintage Year funds for our UC Foundation investors. This first portfolio was created to give the UC Foundations an opportunity to invest alongside The Regents' UCRP and GEP funds in many of the Private Equity – and particularly Venture Capital – funds in which my predecessor Treasurers had the foresight to invest beginning in 1979. The objective is to create a Vintage Year fund each calendar year for the UC Foundations.

At the May 2002 Regents' meeting, a 5% allocation to an Absolute Return strategy was added to the GEP. Absolute Return strategies include market neutral, long/short equities, merger arbitrage and other investment methods that attempt to reduce risk while preserving capital. After staffing this area with an experienced professional we made our first investment on April 1, 2003.

At their May 2003 meeting, The Regents approved the addition of a 5% allocation of Real Estate to both the GEP and the UCRP. The Real Estate portfolio will provide diversification benefits to the overall portfolio by offering returns that have low correlation to other asset classes.

We continue to integrate Investment Risk Management into all aspects of our portfolio management process. We are providing The Regents quarterly risk reports that place returns into the context of their risk framework.

This year's Annual Report includes a new Q&A section (see pages 10-11) providing answers to common questions posed by our clients: The Regents, faculty, staff, students, and retirees of the University of California. In addition, we have provided links to materials that offer greater insight into topics covered in both the Q&A and this letter.

I am extremely pleased to serve as Treasurer of The Regents and it is particularly a pleasure to report on the mutually successful efforts of The Regents and the Office of the Treasurer following the tumultuous capital markets of the past several years.

Best Regards,

David H. Russ
Treasurer of The Regents
and Vice President for Investments
University of California
October 2003

SENIOR MANAGEMENT

DAVID H. RUSS, MA – Treasurer and Vice President for Investments

Mr. Russ is responsible for overseeing the University of California investment portfolio. Mr. Russ brings over 18 years of investment management experience to the Treasurer's Office. Prior to joining the Treasurer's Office in 2001, Mr. Russ served as Managing Director-Public Markets for the University of Texas Investment Management Company. Mr. Russ also served as the Director of Investment Management and Portfolio Manager for Pacific Telesis Group (now SBC Communications) and as Senior Portfolio Manager for the Stanford Management Company. Mr. Russ received his Master of Administration in Finance and Accounting from the University of California, Davis, and his BA degree in Genetics from the University of California, Berkeley.

MELVIN L. STANTON, MBA – The Assistant Treasurer

Mr. Stanton, along with the Treasurer, is responsible for the overall management of the Treasurer's Office. Prior to joining the Treasurer's Office in 1989, Mr. Stanton had more than 13 years experience as a financial executive in portfolio management and securities trading, including Director of Sales for Midland Montagu Securities, Inc., San Francisco; First Vice President and Manager with Crocker National Bank, San Francisco; and Vice President and Regional Sales Manager with Bankers Trust Company, Los Angeles. Mr. Stanton received his MBA and BS degrees from California State University, Northridge.

RANDOLPH E. WEDDING, MBA – Managing Director – Fixed Income Investments

Mr. Wedding is responsible for the strategic focus and management of the long- and short-term fixed-income portfolios. Prior to joining the Treasurer's Office in 1998, Mr. Wedding was Manager of Currency Options and Derivatives Trading for Bank of America, NT&SA, New York; Managing Director, Commodities and Derivative Sales for Bear Stearns & Co., New York; and Principal, Manager of Fixed-Income Derivative Sales for Morgan Stanley & Co., New York. Mr. Wedding began his career with Wells Fargo Bank, responsible for the Bank's Fixed Income Portfolio. Mr. Wedding earned his MBA in Finance from the University of California, Berkeley and BA in Mathematics from the University of California, San Diego.

MARIE N. BERGGREN, MS – Managing Director – Alternative Investments

Ms. Berggren is responsible for the private equity portfolio, venture capital and buy-out investments. Prior to joining the Treasurer's Office in 2002, Ms. Berggren was Executive Vice President/Department Head of Venture Capital Investments for Bank One Corporation. While employed at Bank One and its predecessor organization, First Chicago Corporation, she was the Senior Vice President and Department Head of the Corporation's Mergers and Acquisitions activity. Prior to that she was the Managing Director of Public Equities and Director of Research for First Chicago Investment Advisors (the predecessor to Brinson Partners). Ms. Berggren earned her MS in Management from Stanford University Graduate School of Business and a BA in Economics from the College of New Rochelle.

JESSE L. PHILLIPS, CFA, MBA, MA – Managing Director – Investment Risk Management

Mr. Phillips is responsible for integrating risk monitoring, measurement, and management into all aspects of the investment process. Prior to joining the Treasurer's Office in 2002, Mr. Phillips worked at Northrop Gruman for 11 years, first as Corporate M&A Analyst and then as Manager, Risk Analysis and Research in the Treasury department. Mr. Phillips also worked as Corporate Planning Analyst with Florida Power & Light Company and as Senior Financial Analyst with Storer Communications, Inc., both in Miami Florida. Mr. Phillips earned his BA degree in Mathematics/Economics and MA in Applied Mathematics from the University of California, Los Angeles and his MBA in Finance from the University of Miami. Mr. Phillips is a CPA (Florida) and holds the CFA designation.

ROBERT B. BLAGDEN, MBA – Managing Director – Externally-Managed Investments

Mr. Blagden is responsible for overseeing all externally managed funds and activities with overall responsibility for executing an investment strategy that generates optimal total return relative to risk taken. Prior to joining the Treasurer's Office, Mr. Blagden served as Director of Investments overseeing endowment assets of the Ludwig Institute for Cancer Research. Previous to this position, Mr. Blagden served as Managing Director, Public Equity for the Stanford Management Company, joining them in 1991. Mr. Blagden received his MBA, Finance degree from Stanford University Graduate School of Business and his BA in Statistical Psychology from Dartmouth College.

INVESTMENT MANAGEMENT OVERVIEW

The investment funds managed by the Treasurer of The Regents consist of the University's retirement, defined contribution and endowment funds, as well as the system's cash assets. At June 30, 2003, the Treasurer's Office managed $53 billion in total assets as outlined below.

TOTAL FUNDS UNDER MANAGEMENT[1]
June 30, 2003
($ in billions)

University of California Retirement Plan (UCRP)	$35.2
Defined Contribution Plan and 403(b) Plan Funds	6.9
Endowment Funds	4.7
Short Term Investment Pool (STIP)[2]	6.4
Total Funds	$53.2

The Treasurer's investment management staff includes 17 investment professionals with an average of 15 years of investment experience.

INVESTMENT OBJECTIVES & PHILOSOPHY

The investment objective for all funds under management is to maximize long-term total real returns (adjusted for inflation) while assuming appropriate levels of risk. Because the purpose of each fund is unique, The Regents has established the following specific objectives for each fund, along with the overall goal of exceeding the policy benchmark return and the rate of inflation:

Retirement Funds: for the University of California Retirement Plan, produce a real return to meet obligations to beneficiaries and to meet or exceed the actuarial rate of return; for the University-Managed Defined Contribution Funds, meet stated investment objectives for each fund.

Endowed Funds: produce a real return sufficient to meet the needs of the endowed projects and generate growth of principal and a growing payout stream to ensure that future funding for endowment-supported activities can be maintained in perpetuity.

ASSET ALLOCATION

Asset allocation is the primary determinant of long-term investment returns. UC funds are diversified among global equities and fixed-income securities, within a Regental target allocation (see pages 13, 27 and 30.) Historically, portfolio asset allocation has favored equity investments over fixed-income securities due to the expectation that equities will provide higher total returns over the long term. This emphasis on equity investing has resulted in substantial growth in both the endowment and retirement funds managed on behalf of The Regents.

The Portfolio Management Committee meets weekly to review asset allocation and other portfolio issues. Asset allocation rebalancing is required when an asset class moves out of the allowable range. The Committee decides on the timing and extent of the rebalancing, within The Regents' policy, based on market conditions.

PUBLIC EQUITY INVESTING

Historically, The Regents' Public Equity investment strategy utilized both active and passive management. In the process of implementing the November 2002 Regents-approved changes to the U.S. equity strategy, the internally managed U.S. common stock was transferred into a Russell 3000 Tobacco Free Index fund. As of fiscal year end, the Treasurer's Office is in the process of building an internal team of experienced investment professionals who will select multiple U.S. strategies, select the external managers to implement these strategies, and monitor those external managers on an ongoing basis. As strategies are selected, the Office will transfer some of the holdings out of the index fund. The Non-U.S. Equity strategy intends to implement a similar process and currently utilizes a MSCI EAFE Tobacco Free Index fund and Emerging Markets funds.

REAL ESTATE INVESTING

In May, 2003 The Regents approved a 5% allocation to real estate for UCRP and GEP. Adding real estate investments to these portfolios is expected to provide long-term risk-adjusted total returns between those of U.S. equities and bonds; diversification benefits given real estate's low correlation with other asset classes; protection against unanticipated inflation; and a high proportion of the total return coming from current income.

The real estate investment program will utilize a combined public (40%) and private (60%) strategy. The dual strategy reduces risk within the real estate allocation, offers opportunities for increased liquidity and broader diversification, and will enable the Treasurer to actively tilt overall real estate exposure toward public or private investments depending on relative valuations.

1 Market values exclude accrued income.

2 The Short Term Investment Pool excludes the cash invested for, and reported as part of the UCRP, Defined Contribution and Endowment Funds.

The public strategy will employ the use of external managers who specialize in publicly-traded real estate securities, such as real estate investment trusts (REITs). The private strategy will be accomplished through investing in limited liability investment vehicles, such as limited partnerships sponsored by experienced real estate investment firms with demonstrated expertise and superior performance. The Real Estate investment team, along with a real estate consultant, will review and recommend managers of publicly-traded investments and sponsors of private investments and screen investment opportunities. Upon completion of due diligence and subsequent investment selection, the team will negotiate investment agreements and monitor performance.

ABSOLUTE RETURN INVESTING

The Absolute Return (AR) investments offer risk-return attributes that are not readily available through traditional equity and fixed income investments because they are designed to protect capital and provide positive returns irrespective of overall equity and fixed income market performance. The AR strategies are able to achieve this by selling instruments short, in addition to positions owned long, to hedge out much of the market risk. AR investments should have low correlation with other asset classes and increase the overall portfolio diversification and reduce risk. AR includes long/short equity, merger arbitrage, event-driven and other strategies. An AR portfolio might be net long, net short or neutral relative to the underlying investment market.

Strategy and manager selection are the important drivers of the Absolute Return allocation. The Treasurer's Office is focusing on a subset of available strategies to achieve the diversification benefits and preservation of capital. The Office has also been able to invest with established and accomplished managers, including some that are no longer open to new investors. The office will continue to build the allocation toward the target working with a consultant that specializes in AR strategies.

Another critical element of the AR program is ongoing monitoring of the investments. Investments typically offer quarterly liquidity, which permits rebalancing toward strategies with a favorable outlook or redeeming from managers that are no longer suitable investments. The Treasurer's Office has regular contact with the investment managers to review adherence to the expected investment style, personnel turnover, performance and other issues to ensure the appropriate investments and allocations for the program.

FIXED INCOME INVESTING

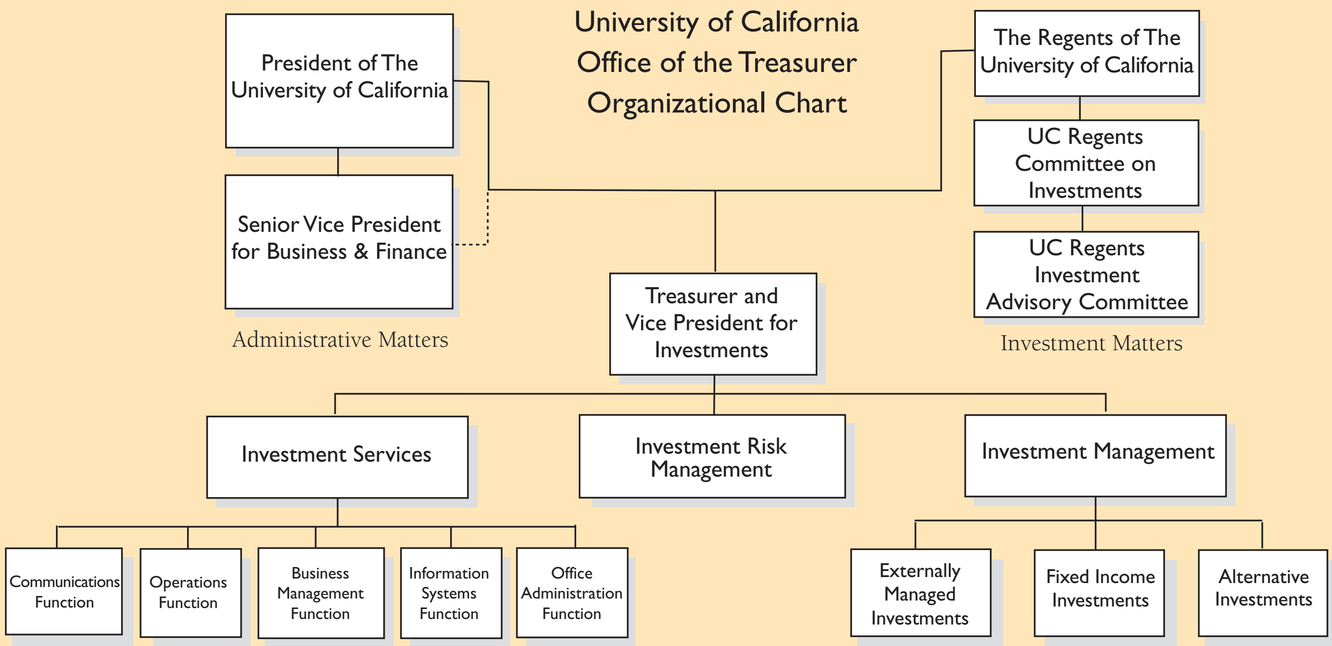
Within the primary goal of maximizing total return over a long-term horizon, the Treasurer's Office Fixed Income team takes an active approach to managing the portfolios, focusing on safety of principal, credit quality, liquidity and efficient use of risk. They start with a "top-down" approach to evaluate the global macroeconomic environment, including analysis of business cycles, monetary and fiscal policies, and political backdrops, in order to assign appropriate sector weights among the three core sectors of Government, Credit and Collateralized bonds. This is coupled with a "bottom-up" approach to individual security selection. Each portfolio manager utilizes a variety of proprietary and industry-developed analytical tools best suited for the particular sector, emphasizing rigorous analysis of such factors as yield curve exposures, portfolio convexity and duration, credit fundamentals, relative value and position weights. Attractive out-of-benchmark investments are also identified in this process and used to enhance returns.

The managers closely monitor current and prospective investments on a daily basis. New opportunities are identified, and existing positions are adjusted as appropriate. The team, along with representatives from Risk Management and Quantitative Analysis, meet monthly to review performance, portfolio exposures and current economic assumptions. Potential new products and strategies are also presented at these sessions before seeking Board approval. This combination of rigorous fundamental and quantitative analysis within an active risk management framework has produced a history of successful returns for The Regents' fixed income funds.

PRIVATE EQUITY INVESTING

The Regents include private equity investments such as venture capital and buyouts in their overall asset allocation to increase portfolio diversification and reduce risk due to its low correlation with other asset classes. Adding to its attraction, return expectations for private equity are generally at least 300 basis points greater than those of the public equity markets.

Manager selection is key to this asset class, and the Treasurer's Office's team has a strong competitive advantage and many years of successful experience. The University is seen as a sophisticated, long-term investor in the private equity arena, achieving well above average returns over the past 20-plus years. The office has long standing relationships with many top-tier private equity groups and continues to build new relationships with premier firms not ac-



cessible to most institutions. The objective is to build a well-diversified portfolio of top tier U.S. partnerships. The Treasurer's Office Alternative Investments team reviews and recommends private equity investments along with a private equity consultant.

Post-investment monitoring, including investment documentations, interim valuations, and regular meetings with general partners, bolster the integrity of the investment program.

RISK MANAGEMENT

In modern investment theory and practice, risk is understood as the uncertainty of outcomes and quantified as the volatility of asset values (returns). Thus risk is an essential aspect of investing, and thought of as a necessary input into the investment process. Risk management is not about eliminating or necessarily reducing risk, but balancing risk and expected return.

The primary objective of the Risk Management function is to ensure that the Treasurer's Office investment and operational activities do not expose the University to potential or unexpected losses beyond the Regents' risk tolerance levels. This involves, first, to identify risks and bound possible losses; second, to implement policies, guidelines and controls on the investment process to maintain the probability of loss within acceptable limits; and third, to integrate risk monitoring, measurement, and analysis into all aspects of the investment process.

At the portfolio level, various aspects of risk, both quantitative and qualitative, are monitored to ensure that risk levels are proportionate to return expectations and that risk is taken intentionally, and diversified optimally. At the plan level, risk management focuses on the adequacy of assets to pay promised benefits or support spending policies. In addition to measuring risk exposures, scenario analysis, stress testing key assumptions, and optimization of risk and expected return are key components of the risk management process. A key element of modern – and traditional – risk management is diversification across asset classes, strategies, and securities.

Risk exposures are continually monitored, compared to targets, and altered when appropriate. Pension plan risk factors include asset volatility, inflation, and interest rates. Equity risk factors include economic activity, market risk preferences, style factors (e.g., relative value, capitalization size), and industry membership. Fixed Income risk factors include interest rate volatility, term structure, credit quality, mortgage prepayments, currency, and liquidity. Private equity and real estate risk factors include (local) economic activity, industry fundamentals, and business risk. Absolute Return risk factors include the equity and fixed income factors defined above, and the degree to which they are offsetting, hedged, or diversified.

Q&A

This section provides answers to common questions posed by our clients: The Regents, faculty, staff, students, and retirees of the University of California. In addition, we have provided links to materials that offer greater insight into topics covered throughout this report.

WHAT IS ASSET ALLOCATION?

Asset allocation is the process of dividing the investments in a portfolio among different asset classes such as equities, fixed income securities and cash to optimize the risk/reward trade-off based on an individual's or institution's specific situation and goals. Resulting strategies can range from very aggressive to very conservative.

WHAT IS THE OVERALL STRATEGY OF THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN (UCRP)?

The UCRP utilizes a moderate growth strategy which attempts to limit volatility. The Regents adopted the following asset allocation policy in May 2002:

Asset Class	Policy	Minimum	Maximum
U.S. Equity	53%	48%	58%
Non-U.S. Equity	7%	5%	9%
Private Equity	5%	3%	7%
Fixed-Income	30%	25%	35%
TIPS	5%	3%	7%

NOTE: A Real Estate allocation of 5% was adopted by The Regents in May 2003 and will be included in 2003-2004 fiscal year reports.

HOW IS A NEW ASSET CLASS IMPLEMENTED?

New asset classes are implemented upon approval by The Regents; however, the Treasurer's Office may choose to wait or may proceed slowly if market conditions warrant. Asset allocations are fulfilled in a manner benefiting long-range performance of the portfolios.

WHAT IS THE UCRP POLICY IF AN ASSET CLASS MOVES OUTSIDE OF THE ALLOWABLE RANGE?

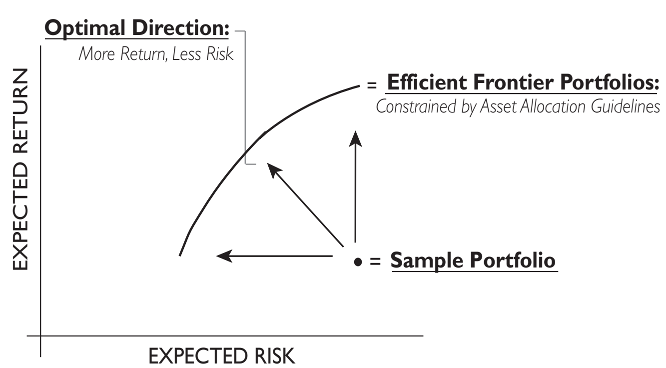
Staying balanced helps avoid unintended risk. Strict adherence to the designated plan forces managers to avoid the temptations of market timing and chasing returns, both of which can position the overall portfolio to underperform when market conditions change.

The Treasurer's Office monitors asset allocation compliance within the allowable ranges on a daily basis. In those circumstances where the asset allocation is outside the allowable ranges, as per The Regents' directive, the Treasurer takes the investment actions necessary to rebalance assets to the policy allocations in a timely and cost effective manner. Under normal circumstances, rebalancing is completed within one month.

The past fiscal year, due to continued market volatility, provided several opportunities for rebalancing.

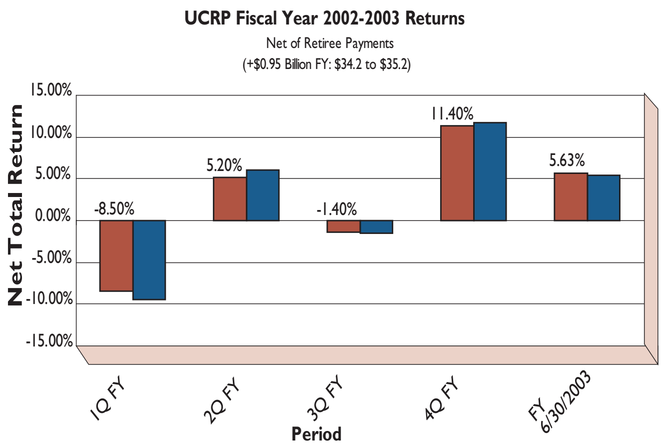
WHAT IS THE 'EFFICIENT FRONTIER'?

The 'efficient frontier' is the line on a risk-reward graph comprised of 'efficient' portfolios. Efficient portfolios are those that provide the greatest expected return for a given level of risk or, conversely, have the least risk for a given level of return. Given the constraints mandated by our asset allocation guidelines, the Treasurer's Office structures and modifies each fund so it moves closer to the efficient frontier.



HOW DID FISCAL YEAR MARKET CONDITIONS IMPACT THE UCRP?

The UCRP returned 5.63% versus 5.36% for the Policy Benchmark, outperforming by 27 basis points. The quarter-to-quarter and total year returns are shown below (rust) along with the policy benchmark performance (blue).



HOW ARE THE EXPENSES OF THE UC-MANAGED FUNDS KEPT SO LOW?

As of fiscal year end the Office of the Treasurer of The Regents' total portfolios were valued at over $53 billion. We retain a relatively small, but experienced investment staff and our large asset size allows us to utilize economies of scale and negotiate cost effective contracts for any outside services. We also work closely with UC Human Resources and Benefits to keep administrative costs associated with UC-Managed Funds utilized within the 403(b) and Defined Contribution plan accounts low.

WHAT IS THE PROCESS FOR SELECTING EXTERNAL MANAGERS?

In hiring external managers for any asset class, the objective is to retain managers who we expect will add value by outperforming their respective benchmark indices net of all management fees on a risk-adjusted basis. Currently, the Office's External Management group is implementing a Request For Proposal (RFP) process to hire qualified active external managers. The initial RFP for U.S. Small Capitalization Equity has been posted on our website as of this writing. Future RFPs for U.S. Large Capitalization Equity, International Equity and Specialty Fixed Income will be posted, analyzed and selected managers funded during the subsequent year.

INTERNET LINKS OF INTEREST

UC-Managed Funds

Quarterly Reports:

www.ucop.edu/treasurer

UC Equity Strategy Transition

UC Factsheet:

www.ucop.edu/news/factsheets/2002/multimanagequity.pdf

Transition Report by State Street Global Advisors:

www.universityofcalifornia.edu/regents/regmeet/jan03/601xa.pdf

External Managers RFP Process:

www.ucop.edu/treasurer/rfp/welcome.html

Regents Committee on Investments

Schedule and Agendas:

www.universityofcalifornia.edu/regents/meeting.html

Investment Risk Management Process

Investment Risk Report 4/22/03:

www.universityofcalifornia.edu/regents/regmeet/april03/603.pdf

Investment Risk Report 8/26/03:

www.universityofcalifornia.edu/regents/regmeet/sept03/601c.pdf

UC News

UC Newsroom:

http://www.universityofcalifornia.edu/news/welcome.html

UC Human Resources and Benefits News:

http://atyourservice.ucop.edu/

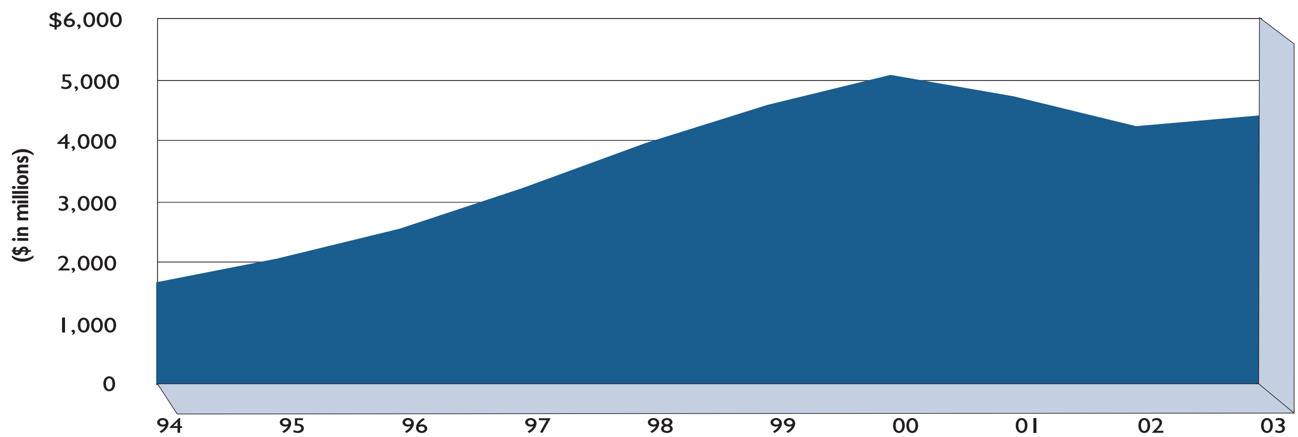
UC Office of the Treasurer News:

http://www.ucop.edu/treasurer/updates/welcome.html

GENERAL ENDOWMENT POOL (GEP)
Summary of Investments[1]
($ in thousands)

	June 30, 2003			June 30, 2002	
GENERAL ENDOWMENT POOL	Cost	Market Value	% of Pool	Market Value	% of Pool
EQUITIES					
U.S. Equity	$ 2,538,884	$ 2,469,137	56.5 %	$ 2,223,564	53.0 %
Non-U.S. Equity	427,772	316,436	7.2 %	286,930	6.8 %
Private Equity	154,865	99,705	2.3 %	142,749	3.4 %
TOTAL EQUITIES	$ 3,121,521	$ 2,885,278	66.0 %	$ 2,653,243	63.2 %
FIXED-INCOME SECURITIES	$ 1,236,223	$ 1,348,258	30.9 %	$ 1,523,429	36.3 %
ABSOLUTE RETURN	$ 105,096	$ 106,288	2.4 %	$ N/A	N/A
STIP PARTICIPATION	$ 29,087	$ 29,087	0.7 %	$ 22,394	0.5 %
TOTAL GENERAL ENDOWMENT POOL	$ 4,491,927	$ 4,368,911	100.0 %	$ 4,199,066	100.0 %
OTHER ENDOWMENT FUNDS	$ 212,076	$ 387,133		$ 364,239	
TOTAL GEP AND OTHER ENDOWMENT FUNDS	$ 4,704,003	$ 4,756,044		$ 4,563,305	

GEP Market Values
(Fiscal Periods Ending June 30)



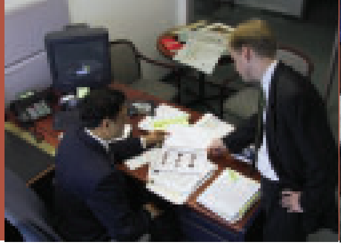
Established in 1933, and unitized in 1958, the General Endowment Pool (GEP) is The Regents' primary investment vehicle for endowed gift funds. GEP is comprised of over 5,000 individual endowments that support the University's mission. GEP is a balanced portfolio of equities and fixed-income securities in which all endowment funds participate, unless payout needs require otherwise.

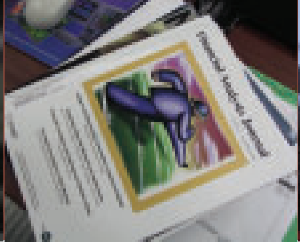
The June 30, 2003 market value of GEP was $4.4 billion, or $15.90 per share, versus $4.2 billion, or $15.56 per share, at the end of fiscal 2002. Total GEP net investment income for the year was $123.8 million, or $0.46 per share, versus $143.9 million, or $0.54 per share, for fiscal 2002.

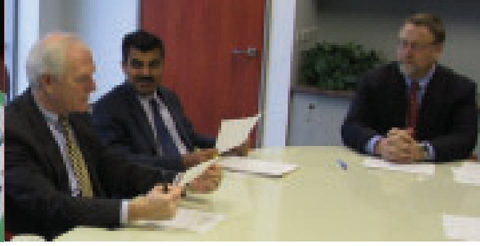
SPENDING POLICY

The Regents believes that a total return investment philosophy aimed at achieving real (after inflation) asset growth will be able to generate growing annual payouts to support donors' designated programs. In October 1998, The Regents adopted a long-term spending rate of 4.75% of a 60-month (5-year) moving average of GEP's market value. The Regents will review the payout rate each year in the context of GEP's investment returns, inflation and the University's programmatic needs, in conjunction with prudent preservation of principal and prudent increases in the payout amount.

[1] For fiscal 2002 and fiscal 2003, the cash portion of the various portfolios excludes the unrealized market appreciation or depreciation of STIP investments, accounts receivable and accounts payable, and the investments in the security lending collateral pool. Therefore, the balances differ from the University's Annual Financial Report.







INVESTMENT OBJECTIVE

The overall investment objective for all funds under management is to maximize real, long-term total returns (income plus capital appreciation adjusted for inflation), while assuming appropriate levels of risk.

For GEP, the primary goal is to generate growth of principal and a growing payout stream to ensure that future funding for endowment-supported activities can be maintained.

INVESTMENT STRATEGY

In order to continue to achieve these investment objectives, The Regents adopted the following asset allocation policy in May 2002:

Asset Class[1]	Policy	Minimum	Maximum
U.S. Equity	45%	40%	50%
Non-U.S. Equity	10%	8%	12%
Private Equity	10%	5%	12%
Fixed-Income	30%	25%	35%
Absolute Return	5%	0%	6%

The asset allocation benchmarks and portfolio guidelines are designed to manage risk and ensure portfolio diversification. The benchmarks for the individual asset classes are: Russell 3000 Tobacco Free for U.S. Equity; Morgan Stanley Capital International All Country World Index ex-U.S. for Non-U.S. Equity; Russell 3000 Tobacco Free +3% (lagged 3 months) for Private Equity; Citigroup Large Pension Fund (LPF) for Fixed Income; and 91-Day Treasury Bill + 4.5% for Absolute Return. The total fund benchmark is a policy-weighted average of the individual asset class benchmarks.

In November 2002, The Regents approved two core changes to the U.S. equity strategy: move from internal management to multiple external managers and diversify from a single actively managed large capitalization strategy to a range of equity strategies. The internally managed U.S. common stock was transferred into a Russell 3000 Tobacco Free Index fund managed by State Street Global Advisors, which is intended to mirror the returns of the broad U.S. stock market. During 2003-2004, UC will begin to hire active external managers to complete the diversification and will transfer some of these holdings out of the index fund.

In the Non-U.S. Equity category, 85% is invested in a MSCI EAFE Tobacco Free Index fund managed by State Street Global Advisors, designed to mirror the returns of the broad developed foreign stock markets. The remaining 15% is invested in emerging markets commingled institutional funds, to gain exposure to the developing foreign markets.

For Private Equity, the Treasurer's Office seeks opportunities through recognized top-tier venture capital partnerships and select buyout funds.

For Absolute Return, investments include long/short equity, arbitrage, event-driven and other strategies.

For Fixed-Income investments, the Treasurer's Office analyzes relative value among the core benchmark sectors of Governments, Corporates, and Mortgage-backed securities and overweights those sectors and securities offering attractive real returns, while maintaining a risk level commensurate with the benchmark index.

RETURNS

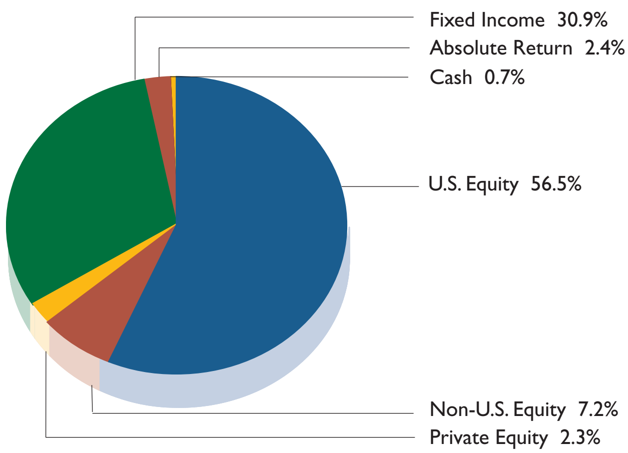
Throughout the years, GEP has exceeded its fund objectives. As illustrated in Table I on page 14, GEP has consistently performed well vs. its policy benchmarks. GEP's total return of 5.4% for the fiscal year primarily reflects strong absolute and relative fixed income returns as yields fell to multi-year lows, along with flat U.S. equity markets after two years of negative returns. For the past 10 years, GEP's compound annual total return was a strong 10.2% vs. 9.8% for its benchmark. During that time, payout distributions grew at an average annual rate of 8.2%—well above annualized inflation of 2.4%.

Chart I on page 14 illustrates the cumulative total returns for GEP for the past 10 years relative to the policy benchmark and inflation. Table II on page 16 provides a detailed illustration of the performance of an endowed gift to GEP for the past 20 years.

ASSET MIX

The following represents GEP's assets at June 30, 2003.

GEP Asset Mix
June 30, 2003

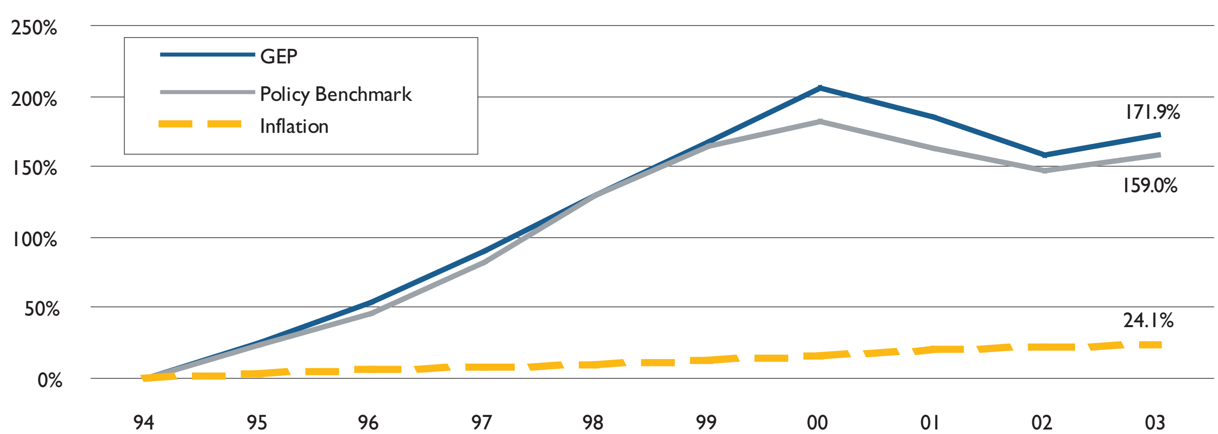


[1] A 5% Real Estate allocation, adopted 5/14/03, will be included in 2003-2004 fiscal year report.

Table I
GEP Annualized Total Returns[1] versus Benchmarks and Inflation
June 30, 2003

	1-Year	5-Year	10-Year	10-Year Cumulative
Total Fund				
GEP	5.4%	3.5%	10.2%	171.9%
Policy Benchmark[2]	5.0	2.2	9.8	159.0
Inflation[3]	2.1	2.4	2.4	24.1
U.S. Equity				
GEP	0.4%	(1.2)%	8.7%	129.2%
Policy Benchmark[4]	0.7	(1.2)	10.3	165.7
Non-U.S. Equity				
GEP	(4.3)%	(3.5)%	0.5%	5.0%
Policy Benchmark[5]	(4.2)	(1.1)	(0.4)	(3.4)
Private Equity				
GEP	(18.4)%	20.7%	26.4%	936.6%
Policy Benchmark[6]	(22.3)	(3.2)	11.8	206.2
Absolute Return				
GEP	2.7%	N/A	N/A	N/A
Policy Benchmark[7]	1.4	N/A	N/A	N/A
Fixed Income Securities				
GEP	15.9%	7.7%	9.6%	149.5%
Policy Benchmark[8]	15.1	7.8	8.3	122.2

Chart I
GEP Cumulative Total Returns: Fiscal 1994-2003
Fiscal Periods Ending June 30



[1] GEP's total returns are based on unit values calculated by UCOP Endowment and Investment Accounting and are net of (after) investment management and administrative expenses of 0.07% of average annual market value, which are automatically deducted from income. The asset class returns reflect investment returns. The performance of The Regents' total return investment portfolio is calculated by State Street Bank, according to the standard recommended by the Bank Administration Institute (BAI), which uses a time-weighted methodology that essentially neutralizes the effect of contributions and withdrawals so as to measure only the return on assets. These calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income. Performance is calculations are reconciled by the Treasurer's Office.

[2] 58% *less* the actual Private Equity weight from the prior month end times the Russell 3000 Tobacco Free (TF) Index, 35% Citigroup LPF Index, 7% MSCI AC World ex US Index, the *actual* Private Equity weight of the prior month end times the Russell 3000 TF Index + 3% (lagged by 3 months); Historical: 65% S&P 500 Index and 35% LB LT G/C Index. Annual index returns assume monthly rebalancing.

[3] Inflation as measured by the Consumer Price Index.

[4] Russell 3000 TF Index; Historical: S&P 500 Index.

[5] MSCI AC World ex US Index; Historical: MSCI EMF Index.

[6] Russell 3000 TF Index + 3% (lagged by 3 months); Historical: S&P 500 Index +5%.

[7] 91-Day TBills + 4.5%.

[8] Citigroup Large Pension Fund Index; Historical: LB LT G/C Index.

EQUITY INVESTMENTS

The equity portion of GEP consists primarily of domestic and foreign common stocks, with a modest exposure to private equity. Total equities represented 66.0% of GEP at year-end, with a market value of $2.9 billion.

U.S. Equity represented 56.5% of the fund at year-end, with a market value of $2.5 billion. In a flat year for the U.S. stock markets, GEP's U.S. Equity returns grew by 0.4%, underperforming the benchmark return of 0.7%. GEP's U.S. Equity return of 8.7% for the 10-year period underperformed the benchmark return of 10.3%.

The following are the 10 largest equity holdings and sector breakdown of the U.S. Equity portfolio as of year end reflective of the underlying index:

Largest Equity Index Holdings	
General Electric	2.3%
Pfizer Inc.	2.2%
Exxon Mobil	1.9%
Microsoft	1.9%
Citigroup Inc.	1.8%
Johnson & Johnson	1.2%
Wal-Mart Stores Inc.	1.2%
Intel Corp.	1.1%
Merck & Co. Inc.	1.1%
IBM	1.1%
	15.8%

Major Index Sector Allocations	% of Total
Financials	23%
Non-Cyc. Consumer Goods	21%
Cyclical Services	15%
Information Technology	15%
General Industrials	8%
Resources	6%
Non-Cyclical Services	4%
Basic Industries	3%
Utilities	3%
Cyclical Consumer Goods	2%
	100%

Non-U.S. Equity represented 7.2% of GEP at year-end, with a market value of $316 million. GEP's Non-U.S. Equities declined 4.3% in the fiscal year, similar to the benchmark return decline of 4.2%. The longer-term returns for this asset class represent the emerging markets funds only, so comparisons are not yet meaningful.

Private Equity represented 2.3% of GEP at year-end with a market value of $100 million. GEP returns for this asset class in the fiscal year were down 18.4%, outperforming the benchmark returns which declined 22.3%. Over the past 5 and 10 years, however, GEP's private equity returns of 20.7% and 26.4% have been an important contributor to total fund return. Longer-term, this category should provide attractive returns, although likely more modest than those of the previous decade.

Absolute Return represented 2.4% of GEP at year-end with the strategy having been in place only one quarter.

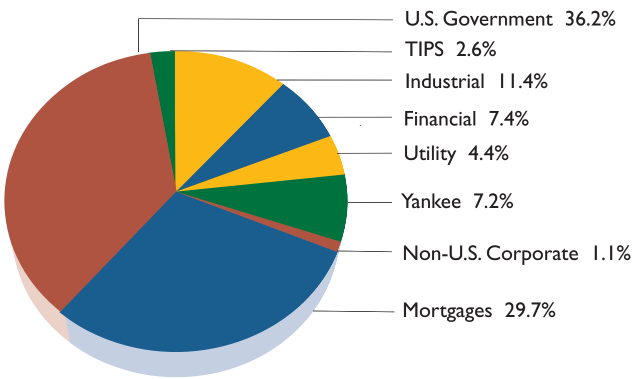
FIXED-INCOME INVESTMENTS

At year-end, Fixed-Income investments constituted 30.9% of the portfolio, with a market value of $1.3 billion.

GEP's fixed-income investments returned a strong 15.9% during the year, outperforming the benchmark return of 15.1%. GEP's fixed income return of 9.6% for the 10-year period exceeded the benchmark returns of 8.3%.

The weighted average maturity of the bond portfolio at year-end was approximately 14 years, the average duration 7.1 years, and the average credit quality was AA, with more than 85% of fixed-income securities rated A or higher. The following pie charts illustrate the sector mix and quality breakdown of the GEP bond portfolio.

GEP Fixed-Income Sector Mix
June 30, 2003



GEP Fixed-Income Quality Mix
June 30, 2003
(BBB and higher = investment grade) Average Quality = AA

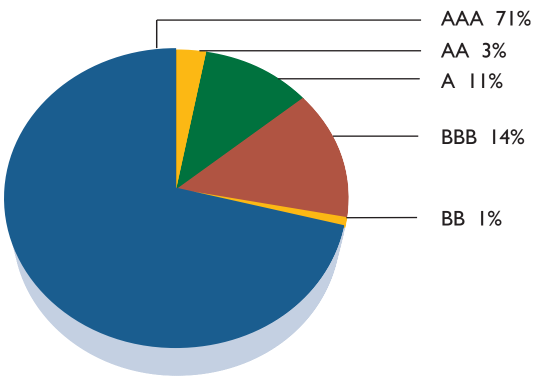


Table II
Example of GEP Investment Performance Fiscal 1984-2003

Endowed Scholarship Fund Growth Example

A Donor made a $100,000 cash gift to the University at the end of fiscal 1983. The Gift entered GEP on the first day of fiscal 1984. The gift purchased 30,647 shares, or units, in the pool based on a unit price of $3.263. GEP and the gift have performed as follows.

	Per Share Performance			Endowment Gift Performance				
Fiscal Year Ending 6/30	Market Value	Payout	% Change Payout	Market Value	Payout	Yield on Beg. Book	Total Return (1)	Inflation
Enter Pool 7/1/83	$3.263			$100,000				
1984	3.263	$0.1769	-2.4%	$90,162	$5,521	6.0%	-4.63%	4.2%
1985	3.801	0.1925	8.8%	$116,488	$5,899	6.5%	36.70%	3.7%
1986	4.986	0.1941	0.8%	$152,804	$5,949	6.6%	37.37%	1.7%
1987	5.937	0.1965	1.2%	$181,949	$6,022	6.7%	23.60%	3.7%
1988	5.346	0.2259	15.0%	$163,837	$6,923	7.7%	-6.13%	3.9%
1989	5.968	0.2522	11.6%	$182,899	$7,729	8.6%	16.84%	5.2%
1990	6.521	0.2933	16.3%	$199,847	$8,989	10.0%	14.43%	4.7%
1991	6.824	0.3157	7.6%	$209,129	$9,675	10.7%	9.86%	4.7%
1992	7.576	0.3203	1.5%	$232,179	$9,816	10.9%	15.91%	3.1%
1993	8.410	0.3489 (2)	8.9%	$257,738	$10,693	11.9%	15.91%	3.0%
1994	7.883	0.3299	-5.4%	$241,584	$10,110	11.2%	-2.51%	2.5%
1995	9.518	0.3435	4.1%	$291,698	$10,527	11.7%	25.64%	3.0%
1996	11.215	0.3507	2.2%	$343,694	$10,748	11.9%	21.80%	2.8%
1997	13.461	0.4090	16.5%	$412,534	$12,534	13.9%	24.20%	2.3%
1998	15.698	0.4795	17.2%	$481,091	$14,695	16.3%	20.47%	1.7%
1999	17.731	0.5406 (3)	12.7%	$542,943	$16,566	18.4%	16.67%	2.0%
2000	19.722	0.6254 (3)	15.7%	$601,939	$19,166	21.3%	14.70%	3.7%
2001	17.759	0.7145 (3)	14.2%	$539,367	$21,897	24.3%	-6.92%	3.3%
2002	15.557	0.7572 (3)	6.0%	$465,919	$23,206	25.7%	-9.50%	1.1%
2003	15.895	0.7675 (3)	1.4%	$466,755	$23,521	26.1%	5.40%	2.1%

<u>Compound Annual Total Return for 20 years (Fiscal 1984-2003)</u>

(Capital Appreciation plus Income) 12.7%

<u>Compound Annualized Growth Rate for 20 years (Fiscal 1984-2003)</u>

Payout Per Share 8.0%

Inflation (Consumer Price Index) 3.0%

[1] GEP's total returns are based on unit values calculated by UCOP Endowment and Investment Accounting and are net of (after) investment management and administrative expenses of 0.07% of average annual market value, which are automatically deducted from income. The performance of The Regents' total return investment portfolio is calculated by State Street Bank, according to the standard recommended by the Bank Administration Institute (BAI), which uses a time-weighted methodology that essentially neutralizes the effect of contributions and withdrawals so as to measure only the returns on assets. These calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income. Performance calculations are reconciled by the Treasurer's Office.

[2] Payout per share in fiscal 1993 is approximately $0.0133 higher than normal as a result of an accounting policy change to distribute equity accruals. Without the change, payout per share would have been $0.3356, or $14,882 for the $100,000 gift.

[3] The payout for fiscal years 1999 and 2000 was 4.35%, the payout for fiscal years 2001 and 2002 was 4.45% and the payout for fiscal year 2003 was 4.50% of a 60-month moving average of GEP's market value.

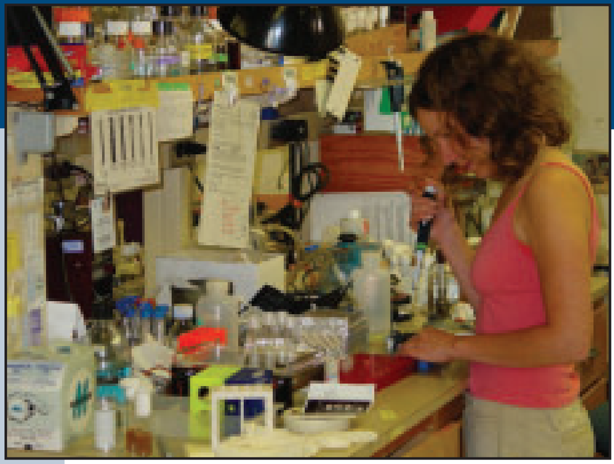
FLETCHER JONES FELLOWS

In order to keep pace with California's growing need for a highly skilled workforce, the University of California anticipates increasing its graduate level enrollment by nearly 50 percent through the end of this decade, requiring a comparable increase in funding. The generosity of donors such as the Fletcher Jones Foundation help to fund scholarships that greatly assist the University in its goal of attracting and retaining gifted graduate students.

The Fletcher Jones Foundation specializes in grants to private colleges and universities, particularly those in California. Born in 1931 in Fort Worth, Texas, Fletcher Jones had his first experience with computers in a job with an aircraft company. A pioneer in the field of computer operations and their applications for business, in 1959 he co-founded Computer Sciences Corporation (CSC) with partner Roy Nutt. By 1963, CSC was the nation's largest software company and today has over 40,000 employees and 600 offices worldwide. In 1970, he established The Fletcher Jones Foundation of Los Angeles with $30 million of his personal fortune. Just two years later, at the age of 41, he died in an airplane crash.

In fiscal year 1997-98, the Foundation donated $1 million to the University of California to fund graduate level education. Held within the General Endowment Pool, this account now valued at $3.9 million funded 10 Fletcher Jones Fellowships throughout the University of California System during fiscal year 2002-2003.

Campus	Fellow	Field
Berkeley	Timothy Fuson	Music
Davis	Kristin A. MacDonald	Comparative Pathology
Irvine	Matthew J. Schwartz	Creative Writing
Los Angeles	Mirana Szeto	Comparative Literature
Riverside	Robin Marie Tinghitella	Biology
San Diego	Leslie Chavez	Physics
San Diego	Amira Rezec	Psychology
San Francisco	Gretchen Ehrenkaufer	Developmental Biology
Santa Barbara	John Lardas	Religious Studies
Santa Cruz	Mary Christine Rose	English Literature



Gretchen Ehrenkaufer works intensely in her lab to uncover the manner in which "Hedgehog" protein is transferred in Drosophila (fruit fly) cells.

FELLOWSHIP RECIPIENT PROFILE

Gretchen Ehrenkaufer, a 2002-03 Fletcher Jones Fellow, began her studies in UCSF's Developmental Biology Program in September 1996, and is due to complete her Ph.D. by the end of the year. Her research examines the mechanism of "Hedgehog" signaling between Drosophila (fruit fly) cells. Hedgehog is a key signaling protein that plays essential roles in the development of both vertebrates and invertebrates, and scientists do not yet understand how the protein moves from the cells that produce it to signal the cells that it targets.

Gretchen's faculty mentor, Dr. Thomas Kornberg, proudly acknowledges, "Gretchen's work represents a courageous effort to devise methods to monitor Hedgehog action and function, and through a series of clever and technically difficult experiments, her work has now revealed an unexpected and revolutionary requirement for direct cell-to-cell contact. This work will be published soon and will constitute an absolutely first-rate thesis."

We wish to acknowledge the help of the following in preparing this information: The University of California Office of the President's departments of Institutional Advancement and Student Financial Support and UCSF's Biochemistry and Biophysics department.

ASSET DESIGNATION BY CAMPUS AND PURPOSE

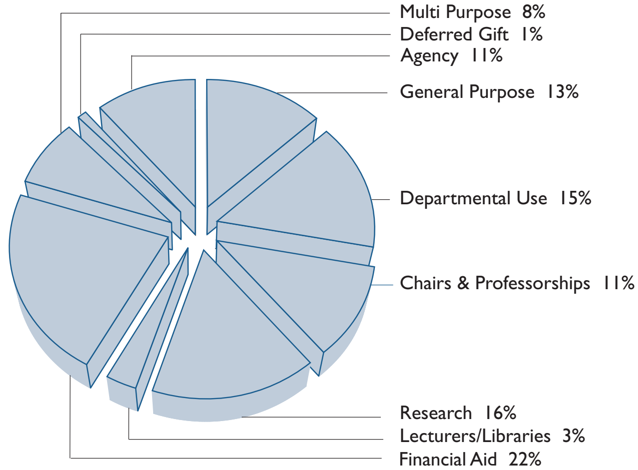
A donor has two avenues for making a gift to or establishing an endowment at the University: either directly to The Regents for a specific campus and/or purpose, or directly to a campus through its Foundation. The campus foundation trustees have discretion in their choice of investment managers and may use the Treasurer's Office or external investment managers.

The Regents' endowment pools include assets that were gifted directly to The Regents, as well as foundation assets where the Treasurer was retained as the investment manager. Chart III (below) illustrates the breakdown of GEP's assets among the campuses. Not surprisingly, a higher proportion of the assets is dedicated to the older campuses, which have a more established alumni and donor base.

Fundraising efforts provide critically needed monies to support the goals of the University. As illustrated above in Chart II, more than half of GEP's assets support departmental use (15%), financial aid (22%) and research (16%).

More detailed information on fundraising results may be found in the University's *Annual Report on Private Support* published by the Office of University and External Relations.

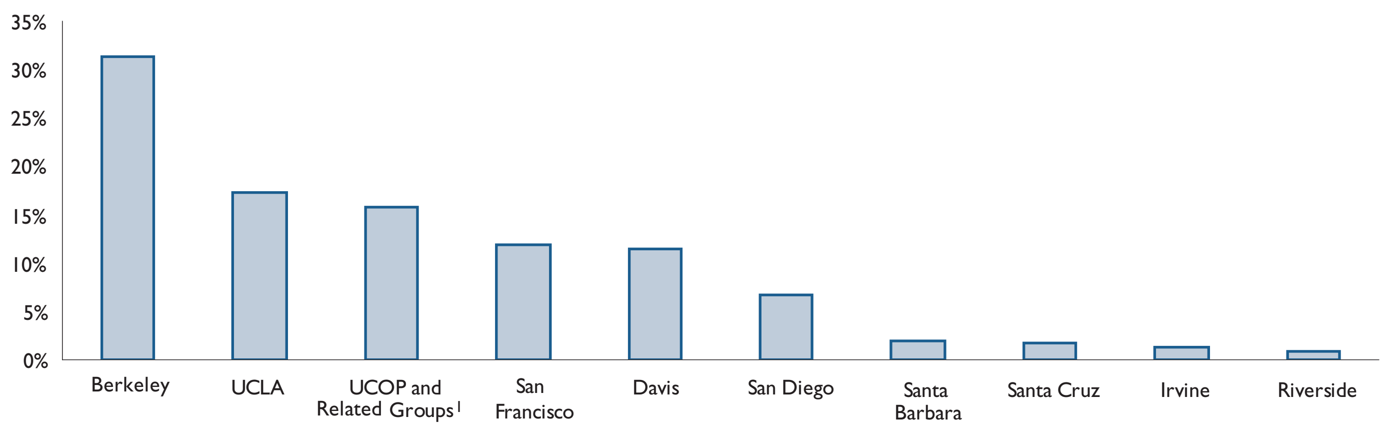
Chart II
GEP Assets Designated by Purpose
June 30, 2003



OTHER ENDOWMENT FUNDS

At June 30, 2003, The Regents had $387 million invested in separately managed endowment funds (including approximately $154.7 million where The Regents are the beneficiaries, but not the trustees). The separately managed funds were established to achieve specified payout requirements for donor and agency monies, as well as to comply with the terms of gift agreements in which donors required funds to be invested separately (e.g., no commingling of funds) and/or placed restrictions on the investment options (e.g., only U.S. Treasury bonds).

Chart III
GEP Assets Designated by Campus
June 30, 2003



[1] UCOP = UCOP-administered programs and multi-campus gifts.

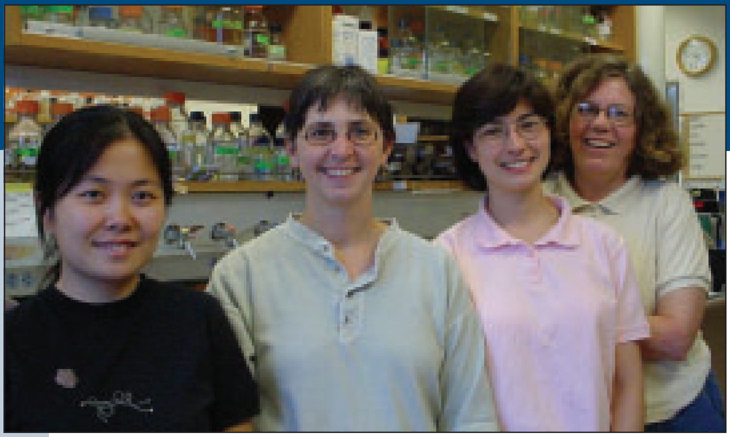
CANCER RESEARCH COORDINATING COMMITTEE

The mission of the Cancer Research Coordinating Committee (CRCC) is the support of promising new directions of research into all aspects of the cancer problem, including its origin, prevention and cure. The CRCC provides one-year seed grants to faculty on the ten campuses, with the expectation that the most promising research will thereafter be funded by larger, long-term grants from other agencies. In recent years CRCC grant awardees have reported very high success rates in competition for external funds from agencies such as the National Institutes of Health, in the form of 3-5 year grants of $750,000 to over $1,000,000. At the present time, the CRCC awards grants to new faculty to initiate cancer research projects, to established investigators in areas of research other than cancer to initiate cancer research projects, and to established investigators to initiate studies in new areas.

Over 40 grants were provided this past year and in keeping with the mission of the CRCC, they funded hypothesis-driven research proposals, supported by established science, rigorous logical reasoning, and appropriate experimental design.

Funding for CRCC grants derives entirely from the annual income generated by some 35-40 accounts that have been established as endowments by private donors to the University of California for the purpose of supporting cancer research. These accounts are held within the General Endowment Pool and managed to produce both growth of principal and a growing payout stream. They include:

Edith E Alsbach Cancer Research Fund
Florence May Alsop Cancer Research Fund
Sally L Barieau-Cox Endowment Fund
A J Bowie Memorial Fund
Scott S Bryant Medical Research Fund
George W Clabrough Fund
Georgiana M Dohner Fund
Amie Driesman Fund
Lota Ellis Cancer Research Fund
George L Everett Cancer Research Fund
Stella Fay Memorial Fund
Edmund C Forbes Cancer Research Fund
Maude Gordon Cancer Research Fund
Alice A Hansen and Charles A Van Damme Fund
Harry Alexander Hill Fund
Albert C Hooper Fund
Naomi King Fund
Rita I Kolb Cancer Research Fund
Henrietta Lewis Cancer Research Fund
M Lovelace Cancer Research Fund
Emilia I Milco Cancer Research Fund
Rouleau and Abadie Morris Trust Fund
Agnes Murray Cancer Research Fund
Edith A Norton Cancer Research Fund
Anita K Paterson Cancer Research Fund
James A Pilkington Memorial Fund
Lester E Reukema Cancer Research Fund
William A and Rachel H Rogers Fund
Estelle Rose Memorial Fund
Emma B Schutz Cancer Research Fund
Wade H Thomas Fund
Christine Luhrs Webster Research Fund
Angeline Zapf Fund



Nunnari Lab Research Team: (left to right) Cheng Song, graduate student; Jodi Nunnari, P.I.; Elena Ingermann, graduate student and Ann Cassidy-Stone, post-doctoral scholar.

CRCC GRANT RECIPIENT RESEARCH PROFILE

Mitochondria are the power centers of the cell and arose from a bacterial ancestor that was engulfed by a primitive host - a pivotal event in the evolution of eukaryotic cells. Mitochondrial division and fusion impact the critical functions of these cells as the division is required for programmed cell death (a process required during development) and in the prevention of the formation of tumors.

In humans, defective mitochondrial fusion is a major cause of dominant optic atrophy (adOA), the most common form of an inherited optic degenerative disease. Using genetic approaches, the Nunnari lab has identified components directly required for mitochondrial division and fusion. Through an analysis of these components, they are beginning to discover the molecular mechanisms that underlie mitochondrial dynamics.

In addition to classical approaches, the Nunnari lab has taken a novel chemical genetics approach that will enable them to gain unique insight into the mechanisms and physiological roles of mitochondrial fission and fusion. Chemical genetics involves identifying small molecule inhibitors and activators in high-throughput screens of a given process to dissect that process. Using this approach, funded by the CRCC, the Nunnari lab has identified small molecules that inhibit mitochondrial division and fusion in human cells.

Given that mitochondrial fission and fusion are intimately tied to processes that are medically important, such as programmed cell death, identification of these compounds could also lead to the development of therapeutic agents for stroke, myocardial infarction, neurodegenerative diseases, cancer, and adOA.

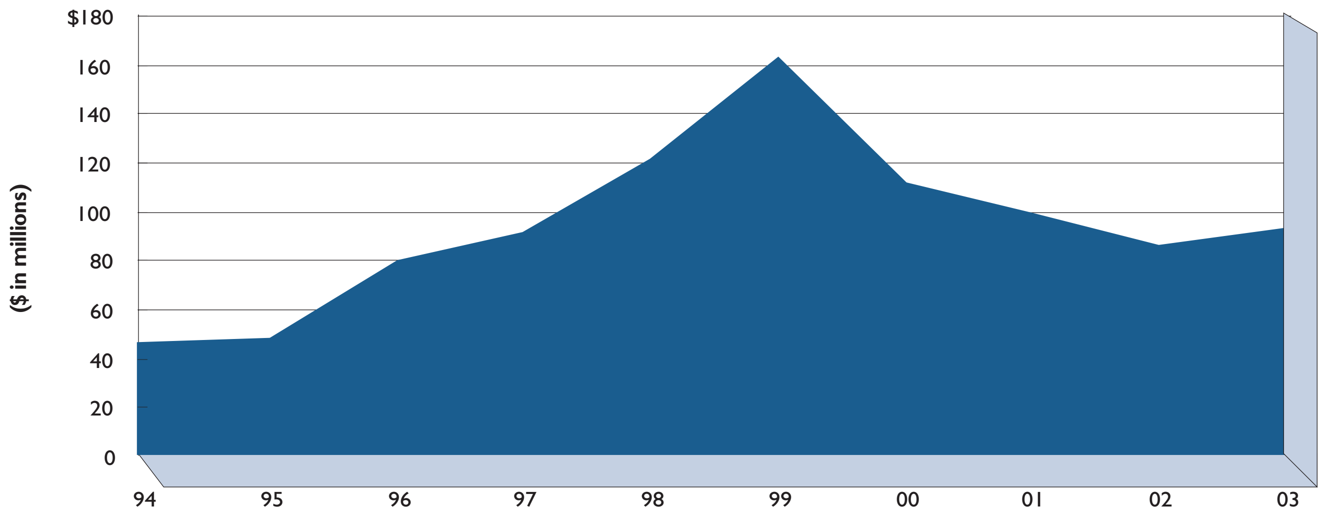
We wish to acknowledge the help of The University of California Office of the President's department of Institutional Advancement. For more information on the CRCC visit their website at http://crcc.ucdavis.edu/.

High Income Pool (HIP)

High Income Pool (HIP)
Summary of Investments[1]
($ in thousands)

	June 30, 2003			June 30, 2002	
	Cost	Market Value	% of Pool	Market Value	% of Pool
HIGH INCOME ENDOWMENT POOL					
EQUITIES	$7,506	$7,867	8.5%	$9,449	11.1%
FIXED-INCOME SECURITIES	$71,350	$81,051	87.9%	$71,527	84.2%
STIP PARTICIPATION	$3,313	$3,313	3.6%	$3,960	4.7%
TOTAL HIGH INCOME ENDOWMENT POOL	$82,169	$92,231	100.0%	$84,936	100.0%

HIP Market Values
(Fiscal Periods Ending June 30)



Note: The total return generated by the High Income Pool in recent years remains positive. However, due to the adoption of a total return payout policy by The Regents in 1998, a number of participants have moved their funds to the University's General Endowment Pool. The High Income Pool continues to pay out income only.

The High Income Pool (HIP) was established in May 1987 to accommodate endowments with high payout requirements and deferred gift giving programs with high contractual payout obligations. As such, HIP is a balanced portfolio comprised primarily of fixed-income securities, along with select higher-yielding equities. The General Endowment Pool (GEP) remains The Regents' primary investment vehicle for endowed gift funds.

The June 30, 2003 market value of HIP was $92.2 million, or $1.88 per share, versus $84.9 million, or $1.70 per share, at the end of fiscal 2002. HIP generated a strong total return of 17.3% for the fiscal year.

Total HIP net investment income for the year was $5.3 million, or $0.104 per share, versus $6.0 million, or $0.111 per share, at the end of fiscal 2002. HIP's current yield on market value at June 30, 2003 was 5.4%.

[1] For fiscal 2002 and fiscal 2003 the cash portion of the various portfolios excludes the unrealized market appreciation or depreciation of STIP investments, accounts receivable and accounts payable and the investments in the security lending collateral pool. Therefore, the balances differ from the University's Annual Financial Report.

SPENDING POLICY

Although The Regents adopted a total return spending policy for GEP in 1998, the income only payout spending policy is being maintained for HIP given the nature of the gifts and their required payouts.

INVESTMENT OBJECTIVE

The overall investment objective for all funds under management is to maximize real, long-term total returns (income plus capital appreciation adjusted for inflation), while assuming appropriate levels of risk.

For HIP, the primary goal is to produce a relatively high and stable level of current income sufficient to meet the needs of the specific funds, with moderate growth of income and preservation of capital.

INVESTMENT STRATEGY

In order to achieve these higher income goals, The Regents' asset allocation strategy for HIP calls for the majority of assets to be invested in fixed-income securities. The Treasurer's Office targets those fixed-income securities and equities that will provide a high level of current income and can also generate moderate growth. The Treasurer's Office may vary the asset mix to maintain a relatively high level of income.

RETURNS

During its 16-year history, HIP has performed very well versus its benchmark, as illustrated in Table III on page 22. HIP's positive return of 17.3% in the fiscal year reflects its emphasis on fixed income investments.

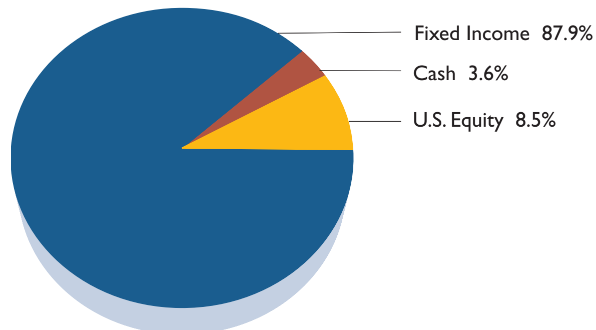
Chart IV on page 22 illustrates HIP's cumulative total returns versus the policy benchmark and inflation since inception.

Table IV on page 23 provides a detailed illustration of the performance of an endowed gift to HIP since inception. During that time, HIP has generated a compound annual total return of 11.6%, and payout distributions have grown at an average annual rate of 2.5%, under the rate of inflation of 3.0%.

ASSET MIX

The following chart represents HIP's asset mix at June 30, 2003.

HIP Asset Mix
June 30, 2003



FIXED-INCOME INVESTMENTS

At year-end, fixed-income investments were 87.9% of HIP, with $81.1 million in market value. HIP's fixed-income investments returned 20.6% during the year.

U.S. Government bonds constituted 59.2% of the fixed-income investments at year-end, while high-grade industrial bonds represented 10.6%, financial bonds 14.1%, Yankee bonds 8.0%, and utility bonds 8.1%. The weighted average maturity of the bond portfolio at year-end was approximately 19.8 years, the average duration was 11.1 years, and the average quality was AA, with 87.6% of the portfolio rated A or higher. The portfolio's five-year average annual turnover rate was 21.2%.

EQUITY INVESTMENTS

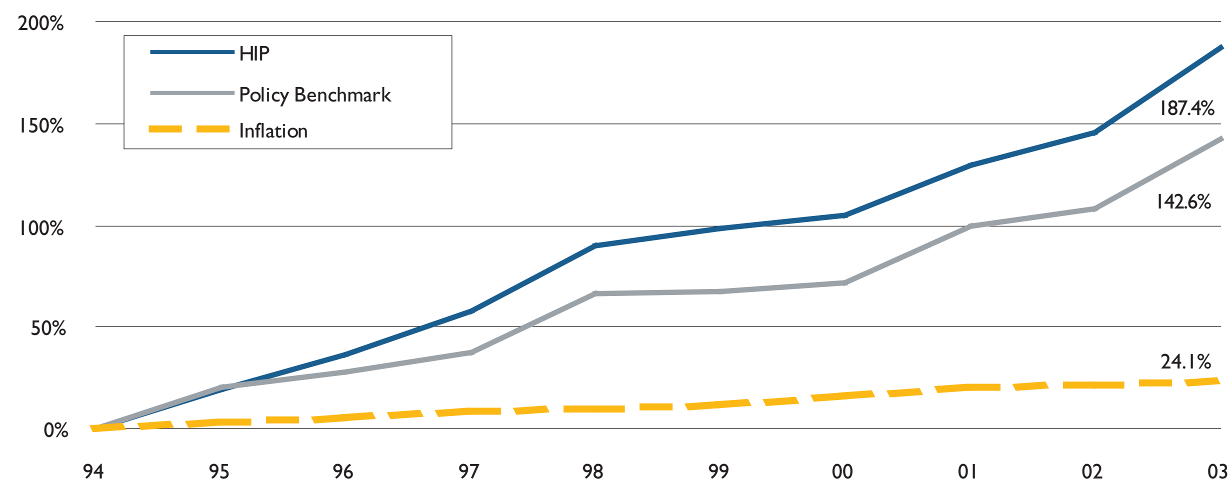
The equity portion of HIP constituted 8.5% of the fund at year-end, with a market value of $7.9 million. HIP's equity portfolio was comprised primarily of REITS and electric utilities. HIP's common stocks returned (4.5%) in the fiscal year, underperforming the broad equity market indices due to its concentration in higher-yielding, more defensive sectors.

Table III
HIP Annualized Performance versus Benchmark and Inflation
June 30, 2003

	Annualized Total Returns			
	1-Year	5-Years	10-Years	10-Year Cumulative
Total Fund				
HIP[1]	17.3%	8.6%	10.1%	187.4%
Policy Benchmark[2]	16.8	7.9	8.4	142.6
Inflation[3]	2.1	2.4	2.4	24.1

	Average Yields			
	1-Year	5-Years	10-Years	10-Year Cumulative
Total Fund				
HIP	5.8%	6.3%	6.5%	64.5%
5-Year U.S. Treasury Notes	3.0	4.7	5.4	53.1

Chart IV
HIP Cumulative Total Returns: 1994-2003
Fiscal Periods Ending June 30



[1] HIP's total returns are based on unit values calculated by UCOP Endowment and Investment Accounting and are net of (after) investment management and administrative expenses of 0.07% of average annual market value, which are automatically deducted from income. The performance of The Regents' total return investment portfolio is calculated by State Street Bank, according to the standard recommended by the Bank Administration Institute (BAI), which uses a time-weighted methodology that essentially neutralizes the effect of contributions and withdrawals so as to measure only the returns on assets. These calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income. Performance calculations are reconciled by the Treasurer's Office.

[2] For the period 7/1/87 - 9/30/89, the benchmark consisted of 80% LB LT G/C; 20% S&P Utilities. For the period 10/1/89 - 6/30/03, the benchmark consisted of 80% LB LT G/C; 20% S&P 500 Electric Utilities.

[3] Inflation as measured by the Consumer Price Index.



Table IV
Example of HIP Investment Performance Fiscal 1987-2003

Endowed Scholarship Fund Growth Example

A Donor made a $100,000 cash gift to the University at the end of fiscal 1987. The Gift entered HIP on the first day of fiscal 1988, purchasing 103,149 shares, or units, in the pool based on a unit price of $0.969. HIP and the gift have performed as follows.

	Per Share Performance			Endowment Gift Performance				
Fiscal Year Ending 6/30	Market Value	Payout	% Change Payout	Market Value	Payout	Yield on Beg. Book	Annual Total Return (1)	Inflation
Enter Pool 7/1/1987	$0.969			$100,000				
1988	0.952	$0.0718		$98,233	$7,403	7.4%	5.99%	3.9%
1989	1.059	0.0761	6.1%	$109,250	$7,855	7.9%	20.20%	5.2%
1990	1.069	0.0839	10.2%	$110,243	$8,657	8.7%	8.99%	4.7%
1991	1.080	0.0848	1.0%	$111,450	$8,743	8.7%	9.47%	4.7%
1992	1.197	0.0833	-1.8%	$123,432	$8,588	8.6%	18.96%	3.1%
1993	1.358	0.0923 (2)	10.8%	$140,087	$9,518	9.5%	21.98%	3.0%
1994	1.160	0.0888	-3.8%	$119,667	$9,154	9.2%	-8.64%	2.5%
1995	1.284	0.0869	-2.1%	$132,487	$8,964	9.0%	19.03%	3.0%
1996	1.374	0.0893	2.7%	$141,774	$9,209	9.2%	14.21%	2.8%
1997	1.494	0.0946	6.0%	$154,084	$9,758	9.8%	16.06%	2.3%
1998	1.699	0.0962	1.8%	$175,209	$9,933	9.9%	20.58%	1.7%
1999	1.674	0.0982	1.9%	$168,358	$10,126	10.1%	4.41%	2.0%
2000	1.615	0.1050	7.0%	$166,624	$10,831	10.8%	3.04%	3.7%
2001	1.694	0.1130	8.4%	$174,735	$11,655	11.7%	12.13%	3.3%
2002	1.696	0.1112	-1.5%	$174,941	$11,474	11.5%	6.80%	1.1%
2003	1.878	0.1036	-6.9	$193,714	$10,686	10.7%	17.30%	2.1%

Compound Annual Total Return for 16 years (Fiscal 1987-2003)

(Capital Appreciation plus Income) 11.6%

Compound Annualized Growth Rate for 16 years (Fiscal 1987-2003)

Payout Per Share 2.5%

Inflation (Consumer Price Index) 3.0%

[1] HIP's total returns are based on unit values calculated by UCOP Endowment and Investment Accounting and are net of (after) investment management and administrative expenses of 0.07% of average annual market value, which are automatically deducted from income. The performance of The Regents' total return investment portfolio is calculated by State Street Bank, according to the standard recommended by the Bank Administration Institute (BAI), which uses a time-weighted methodology that essentially neutralizes the effect of contributions and withdrawals so as to measure only the returns on assets. These calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income. Performance calculations are reconciled by the Treasurer's Office.

[2] Payout per share in fiscal 1993 is approximately $0.0019 higher than normal as a result of an accounting policy change to distribute equity accruals. Without the change, payout per share would have been $0.0904, or $9,325 for the $100,000 gift.

Short Term Investment Pool (STIP)

The Short Term Investment Pool (STIP) is a cash investment pool established in fiscal 1976 by The Regents and is available to all University groups, including retirement and endowment funds. STIP allows fund participants to maximize the returns on their short-term cash balances by taking advantage of the economies of scale of investing in a larger pool and investing in a broader range of maturities.

STIP consists primarily of current funds slated for payroll, operating and construction expenses for all the campuses and teaching hospitals of the University. In addition, funds awaiting permanent investment are invested in STIP to earn maximum daily interest until transferred.

INVESTMENT OBJECTIVE

STIP's investment objective is to maximize returns consistent with safety of principal, liquidity and cash-flow requirements. STIP's investments encompass a broad spectrum of high-quality money-market and fixed-income instruments with a maximum maturity of five years. The Treasurer's Office structures investment maturities to ensure an adequate flow of funds to meet the University's cash requirements.

INVESTMENT STRATEGY

The Treasurer's Office manages STIP as a highly liquid portfolio, using maturity distribution strategies to maximize returns in different yield-curve environments. The Treasurer's Office also employs select swapping strategies by taking advantage of disparities in the market to improve quality and yield, while maintaining liquidity.

YIELDS

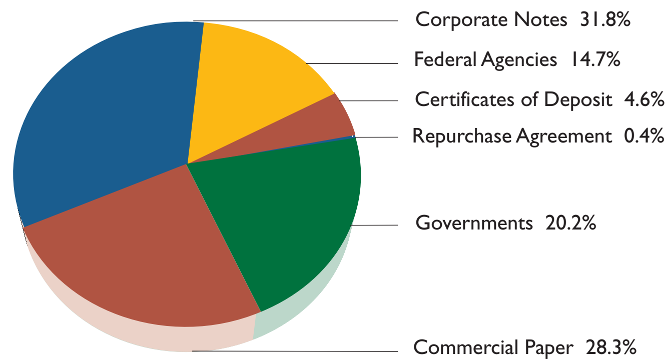
STIP has achieved very attractive returns over the years as illustrated in Table V. For fiscal 2003, STIP's yield of 3.9% exceeded 2-Year U.S. Treasury Notes at 1.8%. During the past 10 years, the average yield on STIP was 5.9%, compared to 5.1% for 2-Year U.S. Treasury Notes.

STIP continued to maintain a high degree of liquidity in the fiscal year to accommodate periodic asset class rebalancing in the longer-term portfolios. During this period, high quality spread products in the 3-5 year maturities were added to enhance the portfolio's yield as the front end of the yield curve steepened.

ASSET MIX

STIP totaled $6.8 billion at June 30, 2003, compared to $6.4 billion at the end of fiscal 2002. STIP's asset mix and maturity distribution as of June 30, 2003 are illustrated below.

STIP Asset Mix
June 30, 2003



STIP Maturity Distribution
June 30, 2003
(Average Maturity = 1.9 years)

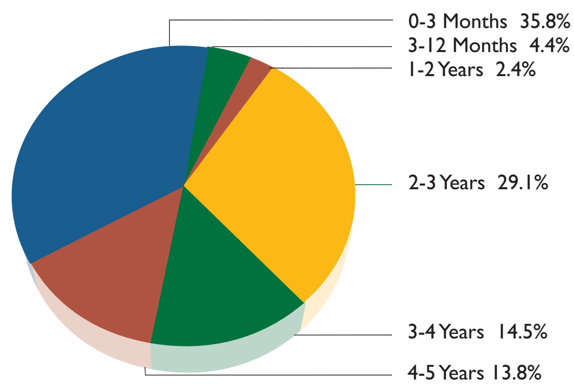
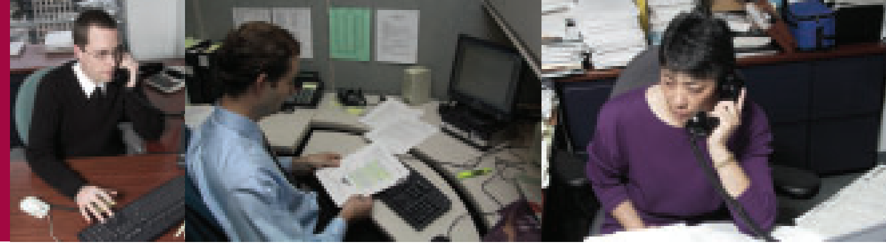


Table V
STIP Annualized Yields[1]
June 30, 2003

	1-Year	5-Years	10-Years	10-Year Cumulative
STIP[1]	3.9%	5.4%	5.9%	76.5%
2-Year U.S. Treasury Notes	1.8	4.2	5.1	63.7
Inflation[2]	2.1	2.4	2.4	24.1

[1] STIP's annualized yields are net of (after) investment management and administrative expenses of 1.5% of average annual income for the fiscal year, which are automatically deducted from income.

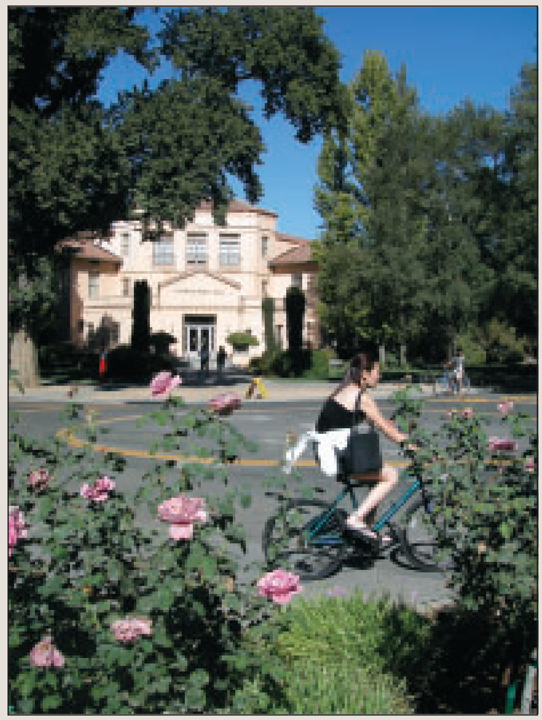
[2] Inflation as measured by the Consumer Price Index.



UNIVERSITY PROGRAMS UTILIZING STIP

In fiscal 1985, The Regents authorized the University of California Mortgage Origination Program, which provides first deed of trust mortgage loans to eligible members of the University's faculty and staff. These loans totaled $52.9 million at June 30, 2003 and were funded by the legally available cash balances in the unrestricted portion of STIP. In March 1999, The Regents authorized the use of the legally available cash balances in the unrestricted portion of STIP to provide liquidity support for the University's Commercial Paper Program.

CHOOSING TO UTILIZE UC-MANAGED POOLS



As of June 30, 2003, the Treasurer's Office manages $795.2 million for the campus foundations and support groups. A donor has two avenues for making a gift to or establishing an endowment at the University of California: either directly to The Regents for a specific campus and/or purpose, or directly to a campus through its Foundation. The campus foundation trustees have discretion in their choice of investment managers and may use the Treasurer's Office or external investment managers.

The Treasurer's Office has worked with The UC Davis Foundation for the past 20 years, helping it manage the campus's private assets to promote and advance the university's mission.

“The staff in the UC Treasurer's Office offer an invaluable understanding of the unique financial requirements of universities. Even in these challenging economic times, they have exceeded performance benchmarks and provided efficient and cost-effective assistance for complex gift transactions, such as gifts involving real estate and stock transactions. The UC Davis Foundation and advancement team have benefited substantially from this special and long-standing partnership.

Celeste E. Rose
Vice Chancellor, University Relations
University of California, Davis

“The UC Treasurer's Office does a great job in providing advice and reporting on our endowment funds. Over the years, we've been very pleased with their investment performance, services and expertise. Having this valuable university resource available to us gives us more time to focus on other important things—such as attracting new private support and advocating on behalf of the Davis campus.”

Charles Soderquist M.S. '73, Ph.D. '78
Chair, Board of Trustees
The UC Davis Foundation

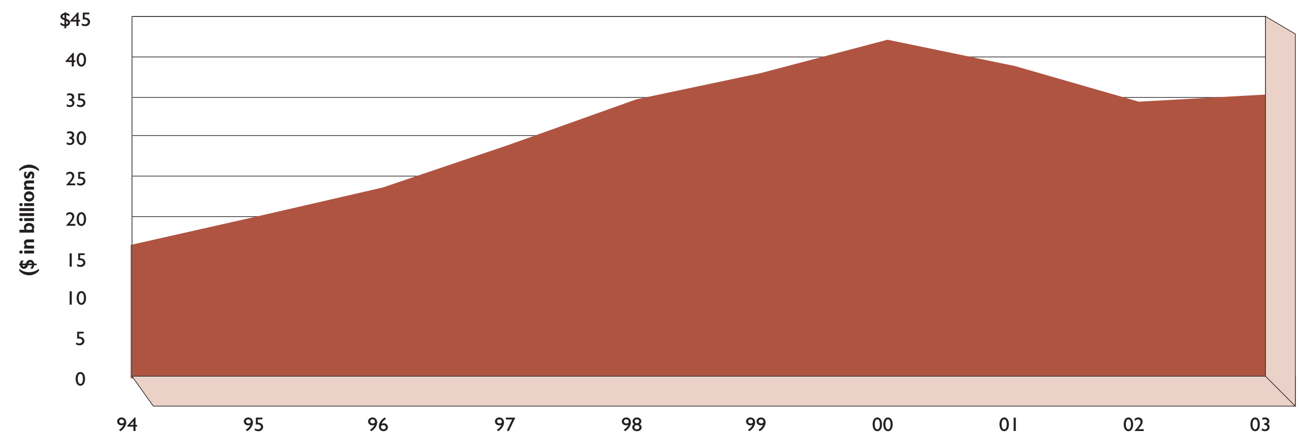
UNIVERSITY OF CALIFORNIA RETIREMENT SYSTEM

Summary of Investments[1]
($ in thousands)

UC RETIREMENT PLAN (UCRP)	June 30, 2003 Cost	June 30, 2003 Market Value	June 30, 2003 % of UCRP	June 30, 2002 Market Value	June 30, 2002 % of UCRP
EQUITIES					
U.S. Equity	$ 21,001,101	$20,470,909	58.1%	$18,369,435	53.6%
Non-U.S. Equity	$ 3,358,469	$ 2,600,513	7.4%	$ 2,417,921	7.0%
Private Equity	$ 825,623	$ 531,347	1.5%	$ 659,455	1.9%
TOTAL EQUITIES	$ 25,185,193	$23,602,769	67.0%	$21,446,810	62.5%
FIXED INCOME SECURITIES					
Bonds	$ 9,013,517	$ 9,881,067	28.0%	$12,607,171	36.8%
TIPS[2]	$ 1,560,042	$ 1,660,552	4.7%	N/A	N/A
TOTAL FIXED INCOME	$ 10,573,559	$11,541,619	32.8%	$12,607,171	36.8%
STIP PARTICIPATION[3]	$ 97,233	$ 97,233	0.2%	$ 238,222	0.7%
TOTAL UCRP	$ 35,855,985	$35,241,621	100.0%	$34,292,203	100.0%

DEFINED CONTRIBUTION (DC) FUNDS	June 30, 2003 Cost	June 30, 2003 Market Value	June 30, 2003 % of DC	June 30, 2002 Market Value	June 30, 2002 % of DC
TOTAL RETURN FUNDS					
EQUITY FUND	$ 2,576,069	$ 2,333,931	34.0%	$ 2,428,097	38.4%
BOND FUND	$ 924,729	$ 966,955	14.1%	$ 760,753	12.0%
INTEREST INCOME FUNDS					
SAVINGS FUND	$ 2,910,964	$ 2,910,964	42.4%	$ 2,618,095	41.4%
ICC FUND	$ 502,975	$ 502,975	7.3%	$ 377,216	6.0%
MONEY MARKET FUND	$ 151,428	$ 151,428	2.2%	$ 140,687	2.2%
TOTAL DC FUNDS[4]	$ 7,066,165	$ 6,866,253	100.0%	$ 6,324,848	100.0%

UCRP Market Values
(Fiscal Periods Ending June 30)



[1] For fiscal 2002 and fiscal 2003, the cash portion of the various portfolios excludes the unrealized market appreciation or depreciation of STIP investments, accounts receivable and accounts payable and the investments in the security lending collateral pool. Therefore, the balances differ from the University's Annual Financial Report.

[2] United States Treasury Inflation Protected Securities (TIPS) are bonds whose principal is adjusted by the Consumer Price Index (CPI) inflation value on a monthly basis. Asset class approved by The Regents in May 2002.

[3] UCRP's STIP investments include assets associated with the UC PERS Voluntary Early Retirement Incentive Program totaling $72.8 million in fiscal 2002 and $71.5 million in fiscal 2003.

[4] Total DC Funds excludes the Multi-Asset Fund, which totaled $602 million at June 30, 2003, and is invested in and reported as part of the Equity, Bond, Savings and Money Market Funds.

The largest pool of assets managed by the Treasurer's Office is the University of California Retirement Plan (UCRP), created in 1961. UCRP is a defined benefit plan, whereby retirement benefits are a function of the employee's age, average salary and length of service. With the plan in surplus, The Regents suspended both employee and employer contributions to UCRP in 1990, but redirected the mandatory employee contributions (less than 2% of annual salary for most employees) to the newly established Defined Contribution Plan.

UCRP is a balanced portfolio of equities and fixed-income securities, which at June 30, 2003 totaled $35.2 billion, versus $34.3 billion at the end of fiscal 2002.

INVESTMENT OBJECTIVE

The overall investment objective for all funds under management is to maximize real, long-term total returns (income plus capital appreciation adjusted for inflation), while assuming appropriate levels of risk.

UCRP's specific objective is to ensure its ability to meet its obligation to beneficiaries by earning returns over the long term that meet or exceed the actuarial rate of return of 7.5%.

INVESTMENT STRATEGY

In order to continue to achieve these investment objectives, The Regents adopted the following asset allocation policy in May 2002:

Asset Class[1]	Policy	Minimum	Maximum
U.S. Equity	53%	48%	58%
Non-U.S. Equity	7%	5%	9%
Private Equity	5%	3%	7%
Fixed-Income	30%	25%	35%
TIPS	5%	3%	7%

The addition of a 5% allocation of United States Treasury Inflation Protected Securities (TIPS) protects this portion of the portfolio from unanticipated inflation. The benchmarks for the individual asset classes are: Russell 3000 Tobacco Free for U.S. Equity; Morgan Stanley Capital International All Country World Index ex-U.S. for Non-U.S. Equity; Russell 3000 Tobacco Free +3% for Private Equity; Salomon Large Pension Fund (LPF) for Fixed Income and Lehman TIPS for TIPS. The total fund benchmark is a target-weighted average of the individual asset class benchmarks.

In November 2002, The Regents approved two core changes to the U.S. equity strategy: move from internal management to multiple external managers and diversify from a single actively managed large capitalization strategy to a range of equity strategies. The internally managed U.S. common stock was transferred into a Russell 3000 Tobacco Free Index fund managed by State Street Global Advisors, which is intended to mirror the returns of the broad U.S. stock market. During 2003-2004, UC will begin to hire active external managers to complete the diversification and will transfer some of these holdings out of the index fund.

In the Non-U.S. Equity category, 85% is invested in a MSCI EAFE Tobacco Free Index fund managed by State Street Global Advisors, designed to mirror the returns of the broad developed foreign stock markets. The remaining 15% is invested in emerging markets commingled institutional funds, to gain exposure to the developing foreign markets.

For Private Equity, the Treasurer's Office seeks opportunities through recognized top-tier venture capital partnerships and select buyout funds.

For Fixed Income investments, the Treasurer's Office analyzes relative value among the core benchmark sectors of Governments, Corporates, and Mortgage-backed securities and overweights those sectors and securities offering attractive real returns, while maintaining a risk level commensurate with the benchmark index.

RETURNS

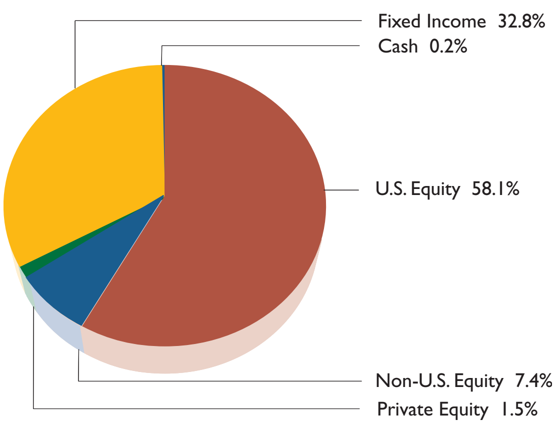
UCRP has exceeded its investment objectives over the long-term. It has also performed well versus its policy benchmarks. UCRP's return of 5.6% in the fiscal year reflects strong fixed income returns as yields fell to multi-year lows, along with flat U.S. equity markets after two years of negative returns. UCRP's annualized total return for the past 10 years through June 30, 2003 was 10.1%, outperfoming its benchmark at 9.9%. Chart VI on page 28 illustrates the cumulative total returns for UCRP for the past 10 years relative to the policy benchmark and inflation.

ASSET MIX

The following illustrates UCRP's asset mix at June 30, 2003.

UCRP Asset Mix

June 30, 2003

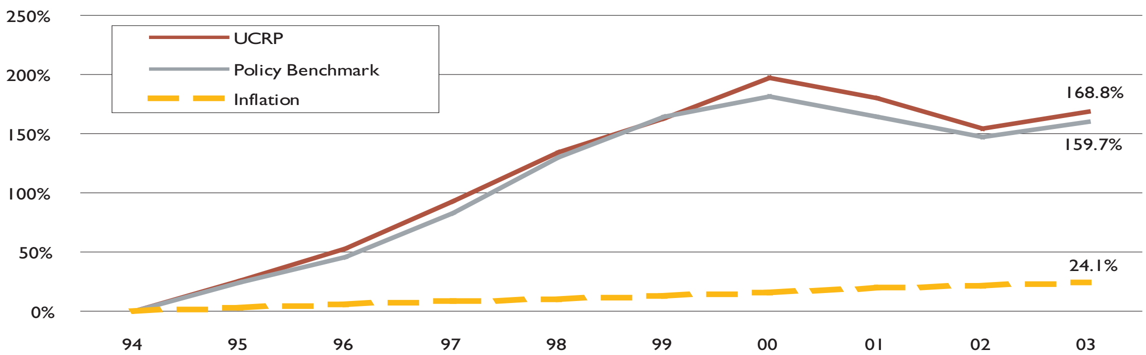


[1] A 5% Real Estate allocation, adopted 5/14/03 will be included in 2003-2004 fiscal year report.

Table VI
UCRP Annualized Total Returns[1] versus Benchmarks and Inflation
June 30, 2003

	1-Year	5-Year	10-Year	10-Year Cumulative
Total Fund				
UCRP	5.6%	2.8%	10.1%	168.8%
Policy Benchmark[2]	5.4	2.3	9.9	159.7
Inflation[3]	2.1	2.4	2.4	24.1
U.S. Equity				
UCRP	0.3%	(1.4%)	8.8%	131.9%
Policy Benchmark[4]	0.7	(1.2)	10.3	165.7
Non-U.S. Equity				
UCRP	(4.0%)	(3.8%)	1.1%	11.7%
Policy Benchmark[5]	(4.2)	(1.1)	(0.4)	(3.4)
Private Equity				
UCRP	(21.5%)	18.6%	26.5%	945.0%
Policy Benchmark[6]	(22.3)	(3.2)	11.8	206.2
Fixed-Income Securities				
UCRP (Bonds)	16.0%	7.7%	10.0%	158.2%
Policy Benchmark[7]	15.1	7.8	8.3	122.2
TIPS				
UCRP	15.7%	N/A	N/A	N/A
Policy Benchmark[8]	15.4	N/A	N/A	N/A

Chart VI
UCRP Cumulative Total Returns: Fiscal 1984-2003
June 30, 2003



[1] UCRP's total returns are net of (after) investment management and administrative expenses of 0.04% of average annual market value. The asset class returns reflect investment returns. The performance of The Regents' total return investment portfolio is calculated by QED, according to the standard recommended by the Bank Administration Institute (BAI), which uses a time-weighted methodology that essentially neutralizes the effect of contributions and withdrawals so as to measure only the return on assets. These calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income. Performance is reconciled by the Treasurer's Office.

[2] Policy Benchmark consists of 58% *less* the actual Private Equity weight from the prior month end times the Russell 3000 Tobacco Free (TF) Index, 30% Citigroup LPF Index, 7% MSCI AC World ex U.S. Index, 5% Lehman TIPS Index and the *actual* Private Equity weight of the previous month end times the Russell 3000 TF Index + 3% (lagged by 3 months); Historical: 65% S&P 500 Index and 35% LB LT G/C Index. Annual index returns assume monthly rebalancing.

[3] Inflation as measured by the CPI.

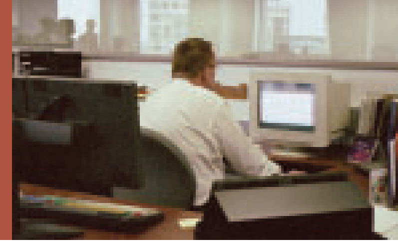
[4] Russell 3000 TF Index; Historical: S&P 500 Index.

[5] MSCI AC World ex U.S. Index; Historical: MSCI EMF Index.

[6] Russell 3000 TF Index + 3% (lagged by three months); Historical: S&P 500 Index + 5%.

[7] Citigroup Large Pension Fund Index; Historical: LB LTG/C Index.

[8] Lehman TIPS Index.




EQUITY INVESTMENTS

Total Equities represented 67.0% of UCRP at year-end, with a market value of $23.6 billion.

U.S. Equity represented 58.1% of the fund at year-end, with a market value of $20.5 billion. In a flat year for the U.S. stock markets, UCRP's U.S. Equity returns grew by 0.3%, underperforming the benchmark return of 0.7%. UCRP's U.S. Equity return of 8.8% for the 10-year period underperformed the benchmark return of 10.3%.

The following are the 10 largest equity holdings and sector breakdown of the U.S. Equity portfolio as of year end reflective of the underlying index:

Largest Equity Index Holdings	
General Electric	2.3%
Pfizer Inc.	2.2%
Exxon Mobil	1.9%
Microsoft	1.9%
Citigroup Inc.	1.8%
Johnson & Johnson	1.2%
Wal-Mart Stores Inc.	1.2%
Intel Corp.	1.1%
Merck & Co. Inc.	1.1%
IBM	1.1%
	15.8%

Major Index Sector Allocations	% of Total
Financials	23%
Non-Cyc. Consumer Goods	21%
Cyclical Services	15%
Information Technology	15%
General Industrials	8%
Resources	6%
Non-Cyclical Services	4%
Basic Industries	3%
Utilities	3%
Cyclical Consumer Goods	2%
	100%

Non-U.S. Equity represented 7.4% of UCRP at year-end, with a market value of $2.6 billion. UCRP's Non-U.S. Equities declined 4.0% in the fiscal year, yet outperformed the benchmark return of (4.2%). The longer-term returns for this asset class represent the emerging markets funds only, so comparisons are not yet meaningful.

Private Equity represented 1.5% of UCRP at year-end with a market value of $531 million. Returns for this asset class in the fiscal year lagged public equity markets; however over the past 5 and 10 years UCRP's private equity returns of 18.6% and 26.5% have been an important contributor to total fund return. Longer-term, this category should provide attractive returns, although likely more modest than those of the previous decade.

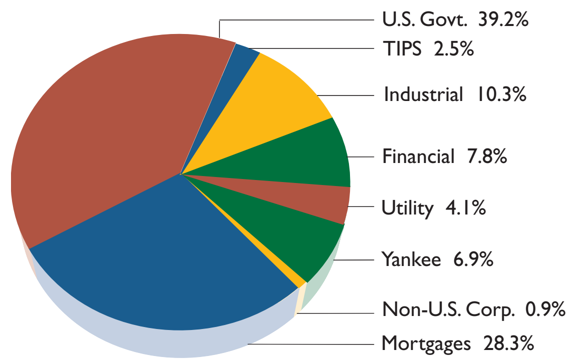
FIXED-INCOME INVESTMENTS

At year-end, Fixed-Income investments constituted 32.8% of the portfolio, with a market value of $11.5 billion.

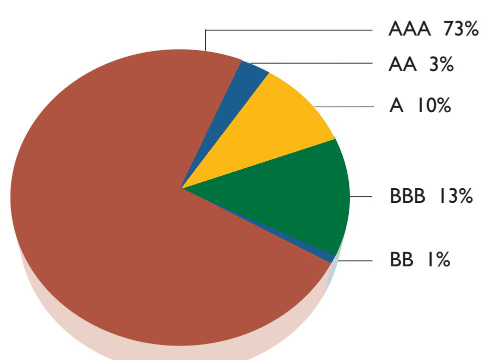
UCRP's fixed-income investments returned an attractive 16.0% during the year, well above the benchmark return of 15.1%. Over the long-term, UCRP's fixed-income returns of 7.7% and 10.0% for the 5- and 10-year periods have consistently exceeded the benchmark.

The weighted average maturity of the portfolio at the end of the year was approximately 13.6 years, the weighted average duration 7.2 years, and the average credit quality was AA, with more than 86% of the fixed-income securities rated A or higher. The following pie charts illustrate the sector mix and quality breakdown of the UCRP bond portfolio.

UCRP Fixed-Income Sector Mix
June 30, 2003



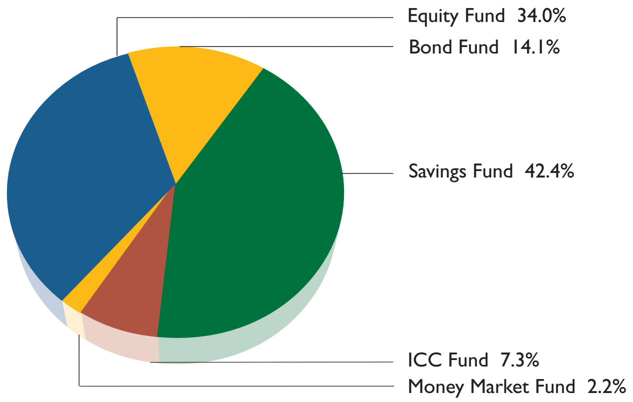
UCRP Fixed-Income Quality Mix
June 30, 2003
(BBB and higher = investment grade)



In addition to the defined benefit program (UCRP), the University offers three defined contribution plans to provide its employees with supplemental retirement benefits—the mandatory Defined Contribution Plan (DC Plan), the Tax-Deferred 403(b) Plan and the Defined Contribution Plan After-Tax Account. These programs differ from UCRP in that the benefits received by participants are based on the employee's contributions to the plans and the returns earned on those contributions over time and that each participant chooses a mix of asset classes (funds) consistent with his or her own investment objectives and risk tolerance.

When investing their defined contribution funds, employees may choose among six University Defined Contribution (DC) Funds managed internally by the Treasurer's Office or numerous external funds. The six University-managed funds include three total return funds—the Equity Fund, Bond Fund and Multi-Asset Fund—and three interest income funds—the Savings Fund, Insurance Company Contract (ICC) Fund and Money Market Fund.

Total DC Assets by Fund[1]
June 30, 2003



INTERNALLY MANAGED UC FUNDS

University-managed funds offer employees the opportunity to achieve attractive, long-term investment performance by investing in one or more funds of their choice. These funds represent diversified portfolios of high-quality, growth-oriented global stocks and bonds, as well as more conservative interest income funds with attractive above market yields. As Table VII on page 31 illustrates, most of these funds consistently rank above average in performance comparisons. In addition, the University-managed funds are extremely low cost relative to external fund options: Annual expenses are only 0.15% of average annual market value, compared to the industry average of 1.4%[2].

TOTAL RETURN FUNDS

EQUITY FUND

The second largest of the University-managed DC funds is the Equity Fund, established in August 1967. The Equity Fund is a total return fund with the primary objective of maximizing long-term capital appreciation with a moderate level of risk. The Regents adopted the following asset allocation policy in March 2000:

Asset Class	Policy	Minimum	Maximum
U.S. Equity	80%	75%	85%
Non-U.S. Equity	15%	10%	20%
Private Equity	5%	3%	7%

At June 30, 2003, the total market value of the Equity Fund was $2.3 billion. The portfolio consisted of 82.0% U.S. Equity, 13.7% Non-U.S. Equity, 3.9% Private Equity and 0.4% cash.

In November 2002, The Regents approved two core changes to the U.S. equity strategy: move from internal management to multiple external managers and diversify from a single actively managed large capitalization strategy to a range of equity strategies. The internally managed U.S. common stock was transferred into a Russell 3000 Tobacco Free Index fund managed by State Street Global Advisors, which is intended to mirror the returns of the broad U.S. stock market. During 2003, UC will begin to hire active external managers to complete the diversification and will transfer some of these holdings out of the index fund.

For the fiscal year, the Equity Fund's return of (1.2%) matched its policy benchmark return. The Equity Fund's longer-term returns are shown in Table VII on page 31. As shown, the fund's 5-year return of 0.1% outperformed its policy benchmark and its peers, as measured by the Morningstar Domestic Equity Funds Median. The 10-year return of 9.1% underperformed its policy benchmark, but outperformed its peers.

[1] Includes balances invested for the Multi-Asset Fund, which at 6/30/03 totaled $602 million and consisted of 41% in the Savings Fund, 26% in the Equity Fund, 23% in the Bond Fund, and 10% in the Money Market Fund.

[2] Source: Morningstar, Inc. Although gathered from reliable sources, data completeness and accuracy cannot be guaranteed.

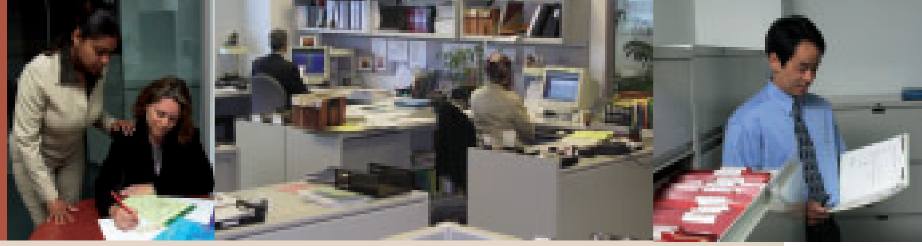


Table VII

University-Managed Defined Contribution Funds Returns[1]

June 30, 2003

	1-Year	5-Years	10-Years
TOTAL RETURN FUNDS			
Equity Fund	(1.2)%	0.1%	9.1%
Policy Benchmark[2]	(1.2)	(1.5)	10.1
Morningstar Domestic Equity Funds Median[3]	(0.4)	0.0	8.3
Bond Fund	12.5	7.0	9.7
Policy Benchmark[4]	10.4	6.8	7.8
Morningstar Taxable Bond Funds Median[3]	9.8	5.9	5.9
Multi-Asset Fund[5]	4.5	4.3	8.0
Policy Benchmark[6]	3.6	3.7	7.1
INTEREST INCOME FUNDS			
Savings Fund	4.7%	5.7%	6.1%
2-Year U.S. Treasury Notes	1.9	4.4	5.1
ICC Fund	6.3	6.9	7.3
5-Year U.S. Treasury Notes	3.2	4.9	5.6
Money Market Fund	1.5	4.3	4.7
91-Day U.S. Treasury Bills	1.5	4.1	4.6
Inflation[7]	2.1	2.4	2.4

BOND FUND

The Bond Fund is a total return fund established by The Regents in January 1978. The primary objective of the Bond Fund is to maximize real (adjusted for inflation) long-term total return through a combination of interest income and price appreciation, subject to maturity and quality constraints. The Treasurer's Office invests the Bond Fund in a diversified portfolio of primarily high-quality, global debt securities for an attractive real return.

At June 30, 2003, the total market value of the Bond Fund was $967 million. U.S. Treasury securities constituted 32.5% of the fund, while TIPS represented 2.1%, high-grade industrials 10.3%, financial bonds 6.1%, Yankee bonds 4.7%, utility bonds 4.1%, mortgage-backed securities 35.8%, and asset backed securities 4.4%. The weighted average maturity of the portfolio at year-end was approximately 8.6 years, the weighted average duration 4.3 years, and 88.6% of the portfolio was rated A or better.

In fiscal 2003, the Bond Fund returned 12.5%, outperforming both its benchmark and the Morningstar Taxable Bond Funds Median. As shown in Table VII (above), the Bond Fund's long-term returns of 7.0% and 9.7% for the 5- and 10-year periods have also exceeded those of its Morningstar peers and its benchmark by healthy margins.

1 All returns and yields for the University-managed funds are net of (after) investment expenses of 0.15% and are based on unit values for the Equity, Bond and Multi-Asset Funds and on interest factors for the Savings, ICC and Money Market Funds. The Treasurer's Office calculates returns and yields by dividing the new unit value or interest factor by the previous unit value or interest factor supplied by UC Human Resources and Benefits. The Treasurer's Office compares these results to the gross investment returns calculated by State Street Bank. State Street Bank's calculations comply with the Association for Investment Management and Research (AIMR) standards, which require time-weighted rates of return using realized and unrealized gains plus income.

2 Policy Benchmark consists of 85% *less* the actual Private Equity weight from the prior month end times the Russell 3000 TF Index, 15% MSCI ACWI ex U.S. Index and the *actual* Private Equity weight of the previous month end times the Russell 3000 TF Index + 3% (lagged by 3 months); Historical: S&P 500 Index.

3 Source: Morningstar, Inc. Although gathered from reliable sources, data completeness and accuracy cannot be guaranteed.

4 Lehman Aggregate Index; Historical: LB LTG/C Index.

5 Contributions to the Multi-Asset Fund are invested 40% Savings Fund, 30% Equity Fund, 20% Bond Fund and 10% Money Market Fund. The fund is not rebalanced.

6 The Market Index Mix consists of 40% 2-Year U.S. Treasury Notes, 30% Russell 3000 TF Index, 20% Lehman Aggregate Index, and 10% 91-Day U.S. Treasury Bills.

7 Inflation as measured by the CPI.

MULTI-ASSET FUND

In September 1990, the University Administration established the Multi-Asset Fund as an investment option. The Multi-Asset Fund is not a managed fund, per se, but is a combination of four existing University-managed funds, whereby contributions are invested according to a fixed percentage: 30% in the Equity Fund, 20% in the Bond Fund, 40% in the Savings Fund and 10% in the Money Market Fund. As such, the Fund invests in a conservative blend of 70% fixed-income assets and 30% equity assets. Although employee contributions enter the Multi-Asset Fund in a fixed percentage, the Multi-Asset Fund is not rebalanced.[1] The actual mix of the Multi-Asset Fund will vary over time as the market values of the component funds fluctuate at different rates.

The market value of the Multi-Asset Fund at June 30, 2003 was $602 million, and the actual asset mix was 26.1% Equity Fund, 23.0% Bond Fund, 41.3% Savings Fund and 9.6% Money Market Fund.

The Multi-Asset Fund's returns are a function of the performance of its component funds.

INTEREST INCOME FUNDS

SAVINGS FUND

The Savings Fund, the largest DC fund, is an interest income fund created in July 1967. The investment objective of the Savings Fund is to maximize interest income returns, while protecting principal, in order to provide a safe, low-risk investment with attractive and stable returns. As such, the Savings Fund invests 100% in government, government-guaranteed and government agency securities of up to five years in maturity. The Treasurer's Office maximizes returns by altering the Fund's maturity structure in different yield curve environments.

The Savings Fund totaled $2.9 billion at June 30, 2003, and was invested 100% in AAA-rated U.S. Treasury and federal agency securities. The weighted average maturity of the Savings Fund was 3.0 years at June 30, 2003.

The Savings Fund has historically provided a yield greater than that of 2-year U.S. Treasury Notes. In fiscal 2003, the Savings Fund generated a yield of 4.7%, exceeding the 1.9% yield on 2-year U.S. Treasury Notes. During the past 10 years the Savings Fund generated an average yield of 6.1% versus 5.1% on 2-year U.S. Treasury Notes.

INSURANCE COMPANY CONTRACT FUND

The Regents approved the Insurance Company Contract (ICC) Fund as an investment option in September 1985. The investment objective of the ICC Fund is to maximize interest income while protecting principal. The Treasurer's Office invests contributions to the ICC Fund in insurance company contracts offered by select, highly rated, financially sound insurance companies. Under such contracts, the insurance companies guarantee a fixed annual rate of interest for a specified time period and the repayment of principal at the end of that time period. The contracts are backed by the assets of the insurance companies, and ICC Fund participants receive the blended rate of all contracts in the fund. The Treasurer's Office uses staggered maturities to systematically manage the reinvestment of maturing contracts and to provide return stability.

At June 30, 2003, the ICC Fund totaled $503 million, with a weighted average maturity of 2.9 years.

Since inception, the ICC Fund has generated yields that have exceeded those of 5-year U.S. Treasury Notes by a comfortable margin. In fiscal 2003, the ICC Fund generated a 6.3% return versus 3.2% on 5-year U.S. Treasury Notes and during the past 10 years generated a 7.3% return compared to 5.6% on 5-year U.S. Treasury Notes.

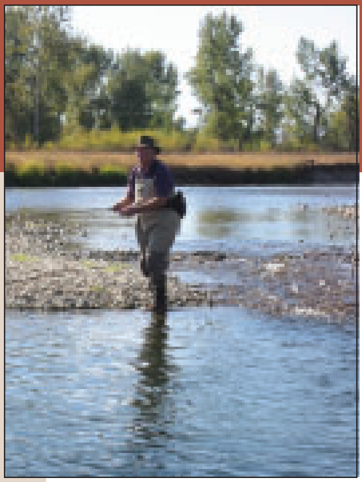
MONEY MARKET FUND

The Regents approved the Money Market Fund as an investment option in September 1985 on the recommendation of the University Administration. The Fund's investment objective is to maximize interest income while protecting principal. The Treasurer's Office invests the Money Market Fund in a diversified portfolio of high-quality, short-term securities. The weighted average maturity of the Fund may not exceed 90 days and no individual maturity may exceed 13 months.

The Money Market Fund totaled $152 million at June 30, 2003 and had a weighted average maturity of 85.0 days. The portfolio was invested 51% in commercial paper, 21% in federal agencies and 28% in U.S. government securities.

The Money Market Fund's yields compare favorably to those of 91-Day U.S. Treasury Bills. In fiscal 2003, the Money Market Fund generated a 1.5% return equal to 1.5% on 91-Day U.S. Treasury Bills. During the past 10 years, the Money Market Fund generated an average return of 4.7% compared to 4.6% on 91-Day U.S. Treasury Bills.

[1] The fund's asset mix and rebalancing policies are being reviewed and will be adjusted during fiscal year 2003-2004.



ANNUITANT PROFILE

In the late nineties, Bob Curry and his wife Jan were in the market for a second home. Hoping to find a place in Montana where they could vacation close to family members, the search took on new meaning as Bob realized he was in the enviable position of being able to retire earlier than planned. Instead of a second home, they purchased a new primary residence with a view of the Bitterroot Mountains. Looking back over his career, he recognizes his proudest accomplishment as providing them with that choice. It took planning, time and patience.

Bob came to the University of California Irvine as Assistant Physical Plant Administrator in October 1980 having started out his career as a draftsman in the aerospace industry and subsequently working at Cal State. He was pleased to have this opportunity for growth and over the next 18 years Bob continued to advance, ultimately retiring as Associate Director Maintenance & Operations. During his tenure the facilities management area grew, as did its focus on providing excellent customer service to its many clients within the University. His goal was to stay open to new ideas and to allow the University to be in a position to select and implement the best of those ideas.

Bob joined the University at a stage in his career and marriage where he and his wife began taking retirement planning more seriously, so he opened a 403(b) account and chose to fund the account with funds managed by the University. Fueled by their mounting interest in a successful retirement, the availability of UC retirement investing information, access to motivated benefits staff and a cooperative market, the Curry's retirement savings grew.

Over the years Bob and Jan continued to learn about investing, track their investments' progress, and read UC benefits newsletters. Even armed with that knowledge, Bob states, "I don't consider myself an 'investment-savvy' person and our interests don't lie in money management." He feels the real secret of their retirement success was leaving the investing to the professionals within the University.

While choosing the option to retire early was easy, transitioning into retirement was more of a challenge and Bob admits, "It took me a while to give myself permission to do nothing." Now five years into retirement, he notes they are living comfortably off their pension payments and that their supplemental retirement savings are, as yet, untouched. He stays busy working on their house, flying model planes and, of course, fly-fishing. Having no regrets about his time with UC, he urges current employees throughout the University system to "continue to do a great job and remember to spend time getting to know your colleagues and showing them that you support them."

Bob Curry

Victor, Montana

Retired

18 years with the University of California Irvine

Associate Director Maintenance & Operations

We wish to acknowledge the help of the UC Irvine Human Resources staff in preparing this information.

Investment Operations

Supporting the management of the portfolios is an experienced Operations staff. The staff consists of a Director, Assistant Director, and Supervisor with an average of 14 years experience in banking and/or investment operations and eight analysts with an average of 15.5 years experience in investment accounting and operations. This unit is responsible for investment accounting and reporting, as well as the central management of all cash services for the University.

INVESTMENT ACCOUNTING

- Track all investment security transactions (foreign and domestic) from origination to settlement.
- Monitor and collect all investment income.
- Reconcile daily all investment assets with the master custodian.
- Monitor all transactions and holdings and reconcile all custodial records to in-house-investment databases.
- Verify, analyze and report investment performance.
- Coordinate incoming gifts with campuses and/or donors and monitor and report receipt of security and cash gifts.
- Review and upgrade portfolio accounting systems on an ongoing basis in order to remain current with industry standards.
- Provide the UCOP Endowment and Investment Accounting Office with investment accounting entries for input into the general ledger.

INVESTMENT REPORTING

In addition to monitoring all investment security transactions and holdings, the Investment Operations staff verifies, analyzes and reports all performance and provides investment accounting entries for input into the UCOP Endowment and Investment Accounting general ledger. The investment group provides all investment information for the following reports:

- All required reports to The Regents' Committee on Investments.
- Performance reports on the various portfolios and separately invested funds.
- All required governmental and other regulatory agency reports.
- The Treasurer's Annual Report.
- The Retirement Investment Funds Brochure.

CASH MANAGEMENT

- Sweep all depository accounts daily and transfer funds to the University's main accounts.
- Provide UCOP funds to cover all checks and electronic fund transfers for vendor and payroll accounts.
- Provide the Endowment and Investment Accounting Office with accounting entries for input into the general ledger for all cash and STIP transactions.

The management of the portfolios is also supported by state-of-the-art information systems and a well-established custodial relationship with a leading industry provider, ensuring sound safekeeping and recording of assets.

FISCAL YEAR CHANGES

During the past fiscal year, State Street Bank became the official "book of record" for the University's investment accounting and performance calculations. The Operations group successfully implemented the required changes and data flows to the general ledger and reporting systems to make this transition.

Additionally, system changes with State Street Bank were implemented for a new Fixed Income classification system, a new Private Equity Vintage Year Pool structure and the new Absolute Return asset class.

This *Treasurer's Annual Report 2002-2003* is unaudited, however these investments are included in the following audited financial statements of the University of California: *The University of California Annual Financial Report 2002-2003* (available on the internet at www.ucop.edu/ucophome/busfin/reports.html), *The University of California Defined Contribution Plan and Tax-Deferred 403(b) Plan 2002-2003*, and *The University of California Retirement Plan 2002-2003* (both available on the internet at http://atyourservice.ucop.edu/forms_pubs/categorical/annual_reports.html).

FOR FURTHER INFORMATION

For more information on the University-managed funds, please refer to *Retirement Investment Funds - December 2002* or log on to our website (http://www.ucop.edu/treasurer). You may contact us in writing at the University of California, Office of the Treasurer, P.O. Box 24000, Oakland, CA 94623-1000.

www.ucop.edu/treasurer Tel. (510) 987-9600 Fax. (510) 987-9651 email.Treas.Regents@ucop.edu

Office of the Treasurer

June 2003

David H. Russ, MA – **Treasurer and Vice President for Investments**
Melvin L. Stanton, MBA – **The Assistant Treasurer**
Randolph E. Wedding, MBA – **Managing Director – Fixed Income**
Marie N. Berggren, MS – **Managing Director – Alternative Investments**
Jesse L. Phillips, CFA, MBA, MA – **Managing Director – Investment Risk Management**
Robert B. Blagden, MBA – **Managing Director – Externally-Managed Investments**

ALTERNATIVE INVESTMENTS

Neetesh Kumar, MBA, MS	Investment Officer	Private Equity Investments
Brett Johnson, MBA	Investment Officer	Private Equity Investments
Leslie Watson, BA	Research Assistant	Private Equity Investments

ABSOLUTE RETURN INVESTMENTS

Steven Algert, CFA, MPPM	Investment Officer	Absolute Return Investments

REAL ESTATE INVESTMENTS

Gary DeWeese, MAI, MBA	Investment Officer	Real Estate Investments

FIXED INCOME INVESTMENTS

Linda Fried, BA	Senior Portfolio Manager, Long-Term Securities, Corporates, Credit
David Schroeder, BA	Senior Portfolio Manager, Long-Term Securities, Governments
Satish Swamy, CFA, MBA	Senior Portfolio Manager, Long-Term Securities, Mortgage Backed Securities
Alice Yee, MBA	Senior Portfolio Manager, Short-Term Securities
Kim Evans, MBA	Head of Credit Analysis
Omar Sanders, CFA, MBA	Credit Analyst
Aaron Staines, BA	Research Assistant

RISK MANAGEMENT/ANALYTICS

Jenny Shen, CFA, CPA, MA	Quantitative Analytics Manager
Carl Ports, BA	Risk Management Analyst

TRADING

Matthew Scoble, CFA, BS	Equity Trader

OPERATIONS

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Ofelia Abaya	Floyd Gazaway, Jr.	Khaleelah Muhammad	Allen Woo
Angelica Beckman	Brian Hagland	Marjan Shomali	

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Michael Comstock	Michael John

COMMUNICATIONS

Susan Rossi, Manager	Alison Johnson

BUSINESS MANAGEMENT

Nelson Chiu, Manager

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