



## LETTER FROM THE CEO

November 26, 2008

To the Rector and Visitors of the University of Virginia, Foundation Trustees, and other members of the University community:

Given sensational news of stock market losses and the precarious state of the global financial system, many are understandably concerned about the University's endowment investments. In this letter, I report our performance for periods ending October 31, 2008 with market context. I then review our investment strategy and discuss our present position. Finally, I provide answers to some common questions received over recent weeks.

The value of the investment pool managed by the University of Virginia Investment Management Company (UVIMCO) has declined by 21% over the twelve months ended October 31, 2008, equating to a loss of about \$1 billion. To be sure, this is a startlingly large loss. When put into appropriate context, however, it starts to seem less disturbing.

Our loss is much less than losses in public securities markets. Over the twelve months ended October 31, 2008, the US stock market dropped by 36% and the global stock market by 43%.

Our recent loss is less than our gain over the previous several years. Over the three-year period ended June 30, 2008, we earned \$1.6 billion. Then we lost \$1 billion in the last four months. Putting the two periods together, from June 2005 to October 2008, our investment return is a gain of \$600 million. We have also received many large gifts over these past three years.

Our long-term performance, even after our recent loss, is remarkably strong. Our ten-year annualized compound investment return for the period ending October 31, 2008, is 12%. Over the same ten years, the S&P 500 Index provided a return of 0%, and the typical institutional investor earned about 3% per year. We are more concerned about this long-term compounding of wealth than the inevitable short-term volatility of market prices.

How did we achieve a 12% return for ten years when the stock market was flat? We employ skilled managers within all asset classes and regions of the world. Many of our managers focus in niches. Some invest in private markets. Many use leverage and/or sell securities short. All of these market-beating strategies require a long time horizon and patience. For this reason, our pool is less liquid than a traditional portfolio of publicly traded securities.

We invest a substantial amount of the UVIMCO pool in "drawdown" funds, which provide access to private investments. Private fund managers "call" the committed capital as they identify compelling opportunities over time, typically two to five years from the commitment

date. When these long-term investments are realized, the managers distribute money back to us. At October 31, 2008, we have \$1.8 billion in uncalled commitments to drawdown funds across many strategies including private equity, real estate, resources, and credit. Again, the investment period for these funds is broad, and we expect calls will be spread out over the next five years.

Under normal circumstances, we receive regular distributions from these private funds and expect those distributions to exceed capital calls. In recent quarters, however, we have received much lower distributions than usual, and we expect to receive few distributions over coming quarters. Despite this cessation in distributions, we expect to invest about \$600 million over the coming year in private drawdown funds to which we have existing commitments. As discussed in our recent annual report, we have planned for such a contingency.

We have ample liquidity to meet all of our obligations. At October 31, we have \$370 million in cash and government bonds, \$500 million in other liquid investments, and no borrowing. In addition to this short-term liquidity, over coming quarters we can redeem most of our \$1.6 billion invested in long/short and absolute return hedge funds if necessary. We expect to redeem only a fraction of what is available.

To make new investments we must exit others. The price at which we can sell investments in today's market creates a high hurdle for new investments. For this reason, we have encouraged our private managers to call capital only to make investments that offer returns high enough to justify selling our other assets in today's difficult market. We expect our managers to continue investing and have reassured them that we will meet all of our capital calls. We have strong and cooperative relationships with all of our investment managers. We trust their judgment.

For several years now, we have reported our intention to reduce our allocation to hedge funds. Even after the redemptions we plan to make over coming years, we expect to have more than a quarter of the pool invested in long/short and absolute return hedge funds. We have communicated our plans to our hedge fund managers. They have assured us that they will have no trouble meeting our redemption requests. Our relationships remain strong with these exceptional managers.

Answers to some common questions that I and others at the University have received over recent weeks are attached. We appreciate your concern and are pleased to provide necessary information. On behalf of the entire UVIMCO organization, thank you for the privilege of managing the University's investment assets.

Regards,  
Chris Brightman  
CEO

**Answers to common questions posed to UVIMCO over recent weeks:**

Q: Did UVIMCO make a recent policy decision to increase private investments?

A: Yes. The UVIMCO Board decided over the past four years to diversify by reducing hedge funds and increasing many other strategies, including private equity, real estate, and resources. The Board reviews its investment policy including such strategy allocations annually.

Q: Has UVIMCO declined to meet recent capital calls from private managers?

A: No. We have met and will meet all of our obligations.

Q: Does UVIMCO need or plan to borrow money to meet capital calls?

A: No.

Q: Does UVIMCO need or plan to sell its investments in private funds?

A: No. We do not need to sell private investments, but we are exploring the secondary market and will consider buying or selling private funds at attractive prices.

Q: Does UVIMCO invest in mortgage-backed securities?

A: Yes. We recently hired investment managers to purchase distressed residential mortgage-backed securities. Those managers purchased about \$250 million dollars of such securities on our behalf in recent months.

Q: Is UVIMCO exposed to derivatives?

A: No. In October, we chose to close all of our derivative positions and repay all short-term borrowing to reduce our counterparty risk. We closed these positions at substantial gains, which increased our cash position.

Q: Does UVIMCO have illiquid instruments in its cash or bond accounts?

A: No. Our current cash balance of over \$100 million is invested in the most liquid Treasury Bills and overnight government repurchase agreements. Our bond portfolio of \$250 million is invested entirely in liquid U.S. Treasury Securities.

Q: Is the endowment model of illiquid investing now broken?

A: No. This model remains appropriate for skilled investors with a long-term investment horizon.