UNIVERSITY
OF
CALIFORNIA

Office of the Treasurer
of The Regents

Quarterly Investment Performance Review: *December 31, 2012*

EXECUTIVE SUMMARY – MARKET REVIEW

Macro issues continued to drive Investor sentiment in 2012 (See attachments IA-IB)

The market environment in 2012 benefitted from accommodative central bank policies set against a backdrop of continued macro uncertainties.

- In the wake of the European Central Bank's 3-year Long Term Refinancing Option (LTRO) in support of banks late last year, assets rallied in the first quarter of 2012, only to fall again in the second quarter as the European debt crisis, lowered growth and profit guidance, and fears of a China hard landing reemerged as flash-points.
- The third quarter rally reversed the losses in the prior quarter, as central banks resolved "to do what it takes" in support of strengthening GDP growth. The promise and extension of liquidity in the banking system supported risk assets to rally, which largely continued into the fourth quarter.
- Among risk assets rallying in 2012, equities showed strength across the globe with the MSCI World Index surging 16.5%. High yield continued to outperform within fixed income, climbing 15.4%, as institutional investors showed a preference for high yield in an environment of negative real yields to cash and treasuries.
- Both the EM debt and equity markets rallied over the year: EM debt, based on the JPM EMBI+ Index, surged 18.1% over the year, on pace with the return to EM equities, which gained 18.2%. The top performing index was Global REITs, which topped 29.9%. Real estate investments saw resurgence in investor demand as historically depressed valuations showed signs of normalizing.

In the Fourth Quarter, U.S. Equity markets were flat while non-U.S. markets strengthened

The fourth quarter was characterized by a rally in International Equities, whereas U.S. risk asset returns were mixed.

- Uncertainties surrounding the election outcome and continuing fiscal cliff political negotiations kept U.S. equity investors at bay. For the quarter the MSCI World ex U.S. climbed 5.9%, while the Dow Jones Industrial Average fell -1.7% and the Russell 3000 was flat, gaining 0.3%.
- As the year closed, a resolution to the debt ceiling talks remained inconclusive; however, investors' perception of an eventual resolution prevailed, with U.S. equities firming late in December.

Risk levels have eased as investors discount risk to pre-crisis levels (See Attachment IC)

Global equity markets entered a more quiescent period in 2012. Although uncertainties remained around larger macro issues, the magnitude of moves in the market were more tempered than the crisis years preceding it. Investors have grown confident that central bankers remain committed to providing the liquidity necessary for a recovery. This has dampened tail risk and the VIX index (a measure of the S&P's volatility tied to futures markets) reflected this.

- Over the fourth quarter, despite uncertainty surrounding the fiscal cliff, the VIX has continued to level off to the mid teens, levels last seen prior to the start of the financial crisis.

EXECUTIVE SUMMARY – PLAN REVIEW

UC Plans delivered robust absolute and relative gains for the year (See Attachments IIA – IIE)

The **UC Entity** returned 2.08% or 0.22% in excess of the benchmark for the quarter. For the calendar year, the entity climbed 11.46%, 1.18% ahead of policy.

At year-end the total UC Entity, which includes all plans managed by the Treasurer's Office, reached $75.1 billion, topping the peak asset levels reached in September 2007, prior to the start of the financial crisis. For both the quarter and 2012 calendar year, all plans generated solid absolute returns and provided solid levels of alpha over the policy benchmark. (See Attachment IIA.)

The **UCRP Retirement Plan**, with assets under management of $43.8 billion returned 2.52% or 0.16% in excess of the benchmark for the quarter. The UCRP gained 13.68%, 0.99% above the policy return of 12.69% over the calendar year.

- The UCRP's gains over policy were primarily driven by asset selection. Over the year, Core Fixed Income and Absolute Return Diversified performed best relative to policy in terms of asset selection. The UCRP portfolio has maintained a fairly tight tracking error to the policy benchmark, given the shifting levels of risk aversion over the year arising from the debt crisis in Europe and fiscal cliff concerns later in the year. The modest asset underweights to Core Fixed Income and TIPS benefitted the portfolio's performance. (See attribution details in Attachments IIB and IIC.)

The **General Endowment Pool**, with assets under management of $6.8 billion, returned 2.75%, or 0.44% in excess of the benchmark for the quarter. For the full calendar year, the GEP returned 12.80%, a significant gain of 1.77% over the policy return of 11.03%.

- The GEP's gains for the year as well as the recent quarter were driven by strong asset selection, particularly in Absolute Return, Public Equities, and Core Fixed Income. Asset allocation was slightly accretive for the year primarily due to the Core Fixed Income and TIPS underweights. Our modest underweight is based on historically low treasury yields in a period of unprecedented monetary policy expansion. (See attribution details in Attachments IIB and IID.)

The **Short Term Investment Pool**, with assets under management of $8.4 billion, returned 0.61% or 0.55% in excess of the benchmark for the quarter and 2.43% for the calendar year, which was significantly above the policy return of 0.21%.

- STIP continues to show strong gains relative to the risk free rate. Returns benefitted from effective yield curve positioning and attractive spreads on high quality corporate securities purchased in early 2009 as credit markets began to rally. Securities Lending income continues to add incremental yield to the portfolio.

The **Total Return Investment Pool**, with assets under management of $4.5 billion, returned 2.02% or 0.06% in excess of the benchmark and 12.53% for the full calendar year, or 0.68% ahead of the policy return of 11.85%.

- TRIP consistently meets The Regents' objective of delivering more yield and return to the University's operating portfolio with less risk. Security selection was the primary driver of returns for the quarter. At quarter end, TRIP was 55% exposed to core fixed income, 35% in equities and REITs, and 10% in high yield debt. (See Attachments IIB and IIE.)

EXECUTIVE SUMMARY - ASSET CLASS REVIEWS

PUBLIC EQUITY REVIEW (See Attachment III for a detailed review)

U.S. Equity Markets

U.S. stocks moved sideways during the quarter as two factors broadly offset one another. On the positive side, economic news was somewhat better than expected, as unemployment drifted lower and the housing market added to earlier gains. While economic conditions showed signs of temperate recovery, stocks were unable to move higher as worries over the fiscal cliff – a collection of large tax increases and spending cuts that would become law on January 2, 2013 unless Congress and the President reached agreement on a different package – overshadowed the minds of investors.

U.S. Equity Portfolio

The U.S. Equity portfolio outperformed the Russell 3000 Index by 0.14% and 0.35% during the fourth quarter and 2012 calendar year periods, respectively.

- In 2012 the actively managed portion of the U.S. equity portfolio outperformed by 1.31%, its best year since 2009 when it outperformed by more than 5%. In 2012 the differences in individual stock returns moved higher, enabling good stock pickers to outperform. All areas of the active U.S. equity portfolio outperformed the Russell 3000 Index and their respective benchmarks with the exception of small-cap core.

- Utilities and Energy were weaker performers relative to the broader index return in 2012, with returns of 2.27% and 3.92% respectively based on Russell sector indices. Our underweight in both sectors added to performance.
- For the calendar year, the large-cap core managers performed well with an outperformance of 2.65% over the Russell 1000 Index (19.07% vs. 16.42%). Strong security selection in the Health Care and Consumer Discretionary sectors contributed significantly to performance.

- During the quarter, large-cap value managers outperformed the Russell 1000 Value Index by 0.71% (2.23% vs. 1.52% index) and the Russell 3000 Index (2.23% vs. 0.25% index). An underweight to Telecom helped performance as the sector was the worst performer in the index.

- Small-cap value contributed to performance during the quarter with an outperformance of 0.85% over the Russell 2000 Value Index (4.07% vs. 3.22% index) and 3.82% over the Russell 3000 Index (4.07% vs. 0.25% index). The outperformance can be mainly attributed to an overweight to Industrials, the best performer in the broad market, and underweight to Utilities, the second worst performer in the broad market.

Non-U.S. Developed Markets

Non-U.S. Equity Developed Markets posted their second consecutive quarter of strong gains as the MSCI World ex. U.S. Index rose 5.93% during the quarter and 16.41% for 2012. Europe continues to be in a recession, but policy activism has given investors reason to increase their exposure to risk assets as the European Central Bank pledged to do “whatever it takes” to keep the European Union together. In Japan, the fourth quarter marked a turning point for the market as recently-elected Prime Minister Shinzo Abe put renewed pressure on the country’s Central Bank to implement substantial amounts of Quantitative Easing.

Non-U.S. Developed Portfolio

The Non-U.S. Developed portfolio gained 5.85% for the quarter, -19 bp behind policy, while the portfolio gained 16.81% for the year, 32 bp over policy.

- 2012 was the tale of two halves for the Non-U.S. Developed Markets as the MSCI World ex. U.S. Index was up only 2.43% in the first half of the year but rallied 13.65% in the second half. The rally was led by the Financials sector and specifically European banks. The active Non-U.S. Developed portfolio outperformed in the first half by 0.96% (3.39% vs. 2.43%) while lagged the second half by -0.67% (12.98% vs. 13.65%).
- In calendar year 2012, strong stock selection in the Technology sector was a contributor to performance. Stock selection in the Industrials sector was another contributor to performance in 2012.
- The underperformance in the quarter and the second half of 2012 was attributed to an underweight to Financials as the sector solidly outperformed the broader market. The majority of our active managers have continued to underweight European banks due to them being undercapitalized and worrisome levels of sovereign debt commitments to other troubled banks.
- Japan was the biggest detractor to performance from a regional perspective during the quarter and 2012. The majority of Japan underperformance came during December, when Japanese exporters and financials rallied based on expectations of Quantitative Easing from Japan's Central Bank (BOJ).

Emerging Markets

The MSCI EM Index rose 5.6% for the quarter and was up 18.2% for 2012. Markets in the region were buoyed by optimism that the U.S. budget negotiations could be resolved and the Federal Reserve's decision to expand its bond-buying plan. Signs of measured improvement in the global economy as well as easing tension in the Eurozone also lifted sentiment.

Emerging Markets Portfolio

The EM Equity portfolio gained 5.89% for the quarter, 31 bp ahead of policy, and soared 20.01% for the year, 179 bp ahead of policy.

- The actively managed portion of the portfolio did especially well, returning 21.33% for the year while the benchmark gained 18.22%, an outperformance of 3.11%.
- Positive stock selection across the portfolio, an overweight to Consumer Staples, and overweights to Turkey and Thailand enabled the portfolio to outpace the benchmark in the fourth quarter and outperform in 2012.
- Consumer Staples (25.4%) and Financials (25.5%) outperformed the broader emerging markets for the year. For the quarter, returns were equally strong in Consumer Staples (7.6%) and Financials (10.0%).
- China and India also rebounded significantly and were up 22.7% and 26.0% respectively for 2012. The portfolio was affected by a -6% underweight to China, as the country outperformed the index by 7.5% in the fourth quarter.

FIXED INCOME REVIEW (See Attachment IV for a detailed review)

Core Fixed Income Market

The Barclay's U.S. Aggregate Index returned 0.21% in the fourth quarter and 4.21% for 2012. The breakout of returns within the Index for the quarter mirrored that of the full year, with Credit significantly outperforming the Government and Collateralized sectors. Credit returns were driven by flows into the sector from non-traditional Credit buyers crowded out of the other two major Index components (Treasuries and MBS) by Federal Reserve purchases. Excess returns in Credit were 117 basis points in the quarter and 693 basis points for the year, despite having to digest all-time record new issuance. Credit spreads tightened 86 basis points during the year, even as leverage ratios began to creep higher in the second half of the year due to share repurchases and increased dividend payouts.

Core Fixed Income Portfolio

The Core Fixed Income portfolios posted another positive quarter on both a total and excess return basis. Core Fixed Income for UCRP and GEP climbed 5.96% for the year, 175 bp over policy and 0.51% for the quarter, 30 bp over policy.

- The overall return conceals a divergence in returns among the three core sectors. The credit and collateralized sectors returned significantly more than the government sector. An underweight to the government sector contributed to both quarterly and annual outperformance.
- For the calendar year, active credit returned 10.77% versus 3.25% for governments and 5.52% for collateralized. An overweight to credit as well as sector outperformance generated excess returns of 175 basis points for actively managed Core UCRP and GEP.
- The collateralized sector outperformed the most on a relative basis, outperforming its benchmark by 75 basis points for the quarter and 251 basis points for the year. Performance was driven by the continued recovery in the non-agency MBS market and strong returns in CMBS.

High Yield Debt Market

The High Yield market continued its march to lower yields during the fourth quarter, driven by a reasonable fundamental backdrop, low default rates, and a hunt for yield in a low rate environment. Improving fundamentals led to a reduction in the 2012 default rate to 2%, from 2.4% in 2011, while high levels of cash flow into the sector led to record new issuance during the year. Over 50% of new issuance was used to refinance outstanding debt as companies took advantage of low rates and high cash balances to reduce interest costs and extend maturities. The ongoing rally in High Yield securities has driven yields to all-time lows in some sectors. However, the 5.10% additional spread over Treasuries available in High Yield is still attractive versus the 6/2003-6/2008 average of 3.92%.

High Yield Debt Portfolio

The High Yield portfolios delivered robust performance in the quarter, returning 3.40%. The calendar year return was 16.11%, an excess return of 0.67%.

- Outperformance in the externally managed portfolios more than offset some slight underperformance in the internally managed portfolios.
- Internal portfolios lagged partially due to an underweight in the financial sector, which was one of the top performing sectors for the year with a return of 29%.

Emerging Market Debt Market

Emerging markets maintained momentum in the fourth quarter, returning 3.24%. This capped another stellar year for the asset class which returned 18.08% for the year as measured by the JPM EMBI+ Index. Emerging Markets experienced record fund inflows of $94 billion, driven by the search for yield in a low yield world; liquidity created by quantitative easing; flight away from other developed market sovereigns such as Spain and Italy; and continued growth prospects in the emerging economies versus the developed markets. The flows into the sector led to record new issuance. Sovereign issuers have slowed the pace of issuance as local markets continue to develop and financing needs are minimal, while corporate emerging market issuance exploded to a record $329 billion, accounting for a large percentage of issuance in the asset class.

Emerging Market Debt Portfolio

Emerging Market debt showed strength gaining 3.04% for the quarter and rallied 16.74% for the calendar year. For the quarter the portfolio lagged policy by -20 bp but was in line with the index for 2012.

- Performance slightly lagged in the fourth quarter. Returns were lower in the internally managed portfolio, which were underweight the lower quality, higher yielding sovereigns such as Nigeria and Hungary, which were top performers.
- The external local currency EM manager, Wellington Management Co., was the star performer for the quarter, returning 6.13%, an excess return of 2.0% over the local currency benchmark.
- For the calendar year, EM managed to perform in-line with the benchmark, outperforming by two basis points. Underperformance in the internal portfolio was offset by strong performance by Wellington.

TRIP

TRIP Core has an 83% policy weight to the Credit Sector versus a 27% weight in the other Core portfolios. The credit-heavy TRIP portfolio has benefitted from that allocation in 2012, returning 9.27% versus the UCRP/GEP Core return of 5.96% for 2012.

TIPS

TIPS, along with U.S. Treasuries, continue to be the most expensive asset class in dollar-denominated fixed income. Through its QEIII program, the Fed is trying to keep real yields low and for the most part is succeeding. As such, we remain structurally underweight to the asset class and overweight High Yield, Emerging Market Debt and Investment Grade Credit. Active return in TIPS was generated primarily by security selection.

STIP

STIP continues to benefit from corporate securities purchased 3-4 years ago. As those securities mature and the proceeds are reinvested at current, low yields, the income return will inevitably fall. At the same time, the maturity profile of STIP is slowly being adjusted to take advantage of an eventual increase in interest rates.

ALTERNATIVE INVESTMENTS REVIEW

Alternative Investments assets were among the key drivers of relative value added to the overall plan returns for both the quarter and calendar year.

Private Equity (See Attachment V for a detailed review)

- Private equity gained 2.89% for the fourth quarter, modestly outperforming the entity return, primarily driven by increased values in the venture capital portfolio and strong performance in the co-investment portfolio. These returns were partially offset by weak buyout returns for the quarter.
- The private equity portfolio has been in build up mode the past decade. However, 2012 was the first year in many years that the private equity portfolio received more cash back from managers than cash contributed to managers as the portfolio is approaching maturity. Distributions over the fourth quarter were very strong, up 132% compared to the prior year period and capital calls were on par with the prior year period.
- The UC made a total of eighteen investments throughout 2012 which represents $637 million in commitments. Buyout funds represented 76% of new commitments while venture capital accounted for 12%. Co-investments accounted for the remaining 12% of the commitments for the calendar year.

Absolute Return (AR) Diversified Portfolio (See Attachment VI for a detailed review)

- During the quarter, the UC AR portfolio posted a gain of 2.98%, outperforming its HFRX benchmark by 202 basis points. All major strategies in the portfolio were positive contributors to performance during the quarter and calendar year.
- The largest positive contributors to performance during the quarter were Emerging Markets, Relative Value, and Event Driven strategies.
- The team continues to make tactical adjustments across strategies within the portfolio. During the quarter we added to Hedged Equity and Distressed strategies, and decreased the size of the Global Macro portfolio.
- We continue to reduce the number of hedge fund managers in an effort to concentrate the portfolio.

Cross-Asset Class (CAC) (See Attachment VII for a detailed review)

- Cross-Asset Class (“CAC”) strategy closed the year with returns short of the policy. The portfolio gained 12.21% for the year, -25 bp behind policy and gained 1.45% for the quarter, -90 bp short of the policy.
- The focus on risk diversification across economic regimes under uncertain market conditions has been beneficial since inception of the portfolio, where average annual returns of 10.18% are well in excess of the policy’s return of 4.16%. However, as equity markets have rallied relative to treasuries, our risk weighted exposure to nominal fixed income has dampened returns over the recent period.
- We continue to focus our new funding efforts on satellite strategies which can invest in areas which have shown steep pricing dislocations.
- A residential mortgage whole loan pool strategy was funded late in the fourth quarter. We are already seeing contributions from loan workouts and income, despite an expected ramp up period for the investment.

Real Assets (See Attachment VIII for a detailed review)

- The Real Assets portfolio decreased by -0.09% for the quarter, 25 bp ahead of policy. Returns were positively impacted by the Energy portfolio, which was up 1.31% for the quarter, the Infrastructure portfolio, which was up 0.70% for the quarter, and the Timberland portfolio, which was up 0.39% for the quarter. The Commodities and Opportunistic portfolios detracted from performance with quarterly returns of -2.80% and -0.47% respectively.
- Real Assets were up 4.36% for the calendar year resulting in 41 basis points of excess return. Strong returns by the Infrastructure and Opportunistic portfolios were positive contributors while relative excess performance was driven by outperformance by the Commodities portfolio. As the Real Assets portfolio is still in its build-up phase the J-curve remains a drag on performance. Staff expects the J-curve to have less influence in the coming years as unfunded commitments are drawn and Staff continues its focus on fee-efficient co-investments.
- Staff made six new investments (including two co-investments and one secondary purchase) during the quarter, bringing the portfolio to a net asset value of $853 million with $700 million in unfunded capital commitments and a total exposure of $1.5 billion. The portfolio is now comprised of 36 investments.

Real Estate (See Attachment IX for a detailed review)

- The Private Real Estate Portfolio continued its steady recovery during the second fiscal quarter, with UCRP gaining 1.37% and GEP adding 2.49%. The UCRP portfolio fell short of the benchmark by 1.16%, while the GEP portfolio kept pace, with slight underperformance of 0.04%.
- The real estate portfolio outperformed the benchmark by 1.40% for 2012, driven by stronger than benchmark appreciation gains in the open-end fund portfolio, the successful sale of a large value add asset, and a development asset from the separate account portfolio.
- Three additional acquisitions, all in California, were made for the separate account portfolio during the second fiscal quarter: one value-add office property, one opportunistic office property, and one stable office property, with an aggregate net value of $124 million.
- During the second fiscal quarter, a $35 million investment was made to an open-end industrial fund. In total during the 2012 calendar year, $125 million in equity was committed to three commingled funds.

In Summary, the Treasurer's Office was able to reap significant gains over the year for the core diversified plans including UCRP, GEP and TRIP of 13.68%, 12.80%, and 12.53% respectively against a backdrop of an uncertain recovery from deleveraging cycles both here and abroad. Despite the high returns achieved over the year, the Treasurer's Office is cognizant of maintaining a diversified and risk balanced portfolio in a period of continued uncertainty surrounding the debt ceiling and the unresolved debt crisis in Europe.

ATTACHMENTS

Contents

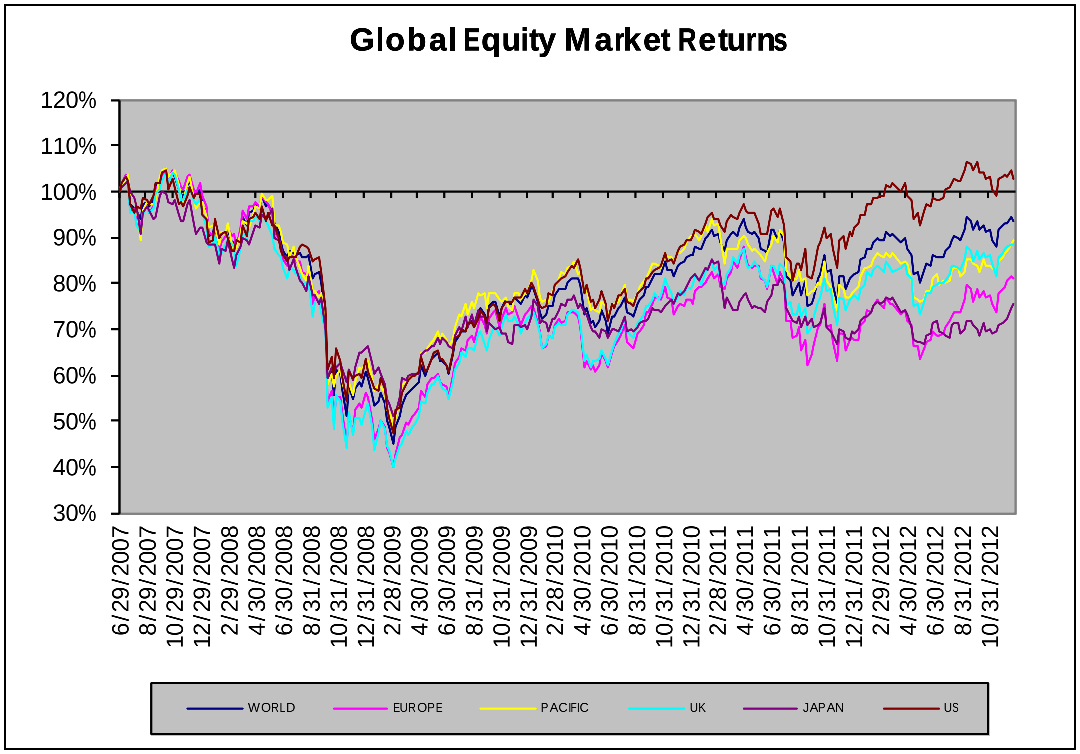
MARKET INDICES PERFORMANCE REPORT

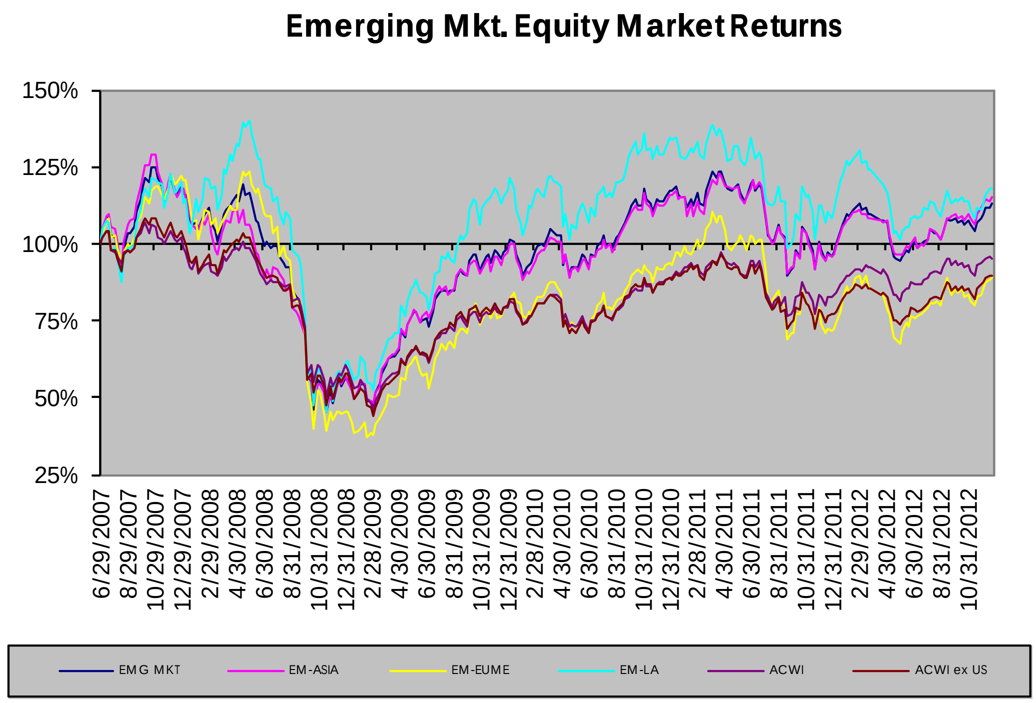
Period Ended December 31, 2012

		Returns	
		Quarter (%)	1-Year (%)
U.S. Equity			
	S&P 500	-0.38	16.00
	Russell 3000	0.25	16.42
	Dow Jones Industrial Average	-1.74	10.24
Non-U.S. Equity			
	MSCI World ex-U.S.	5.93	16.41
	MSCI Emerging Markets	5.58	18.22
U.S. Fixed Income			
	Barclays Aggregate	0.21	4.21
	Barclays TIPS	0.69	6.98
	BofA ML High Yield U.S. Corporate	3.15	15.43
Non-U.S. Fixed Income			
	JP Morgan EMBI + Index	3.28	18.08
Real Estate			
	FTSE EPRA NAREIT Global	6.31	29.85
Cash Equivalents			
	91 Day Treasury Bill	0.04	0.11
	Consumer Price Index	-0.98	1.53

GLOBAL EQUITY MARKET RETURNS

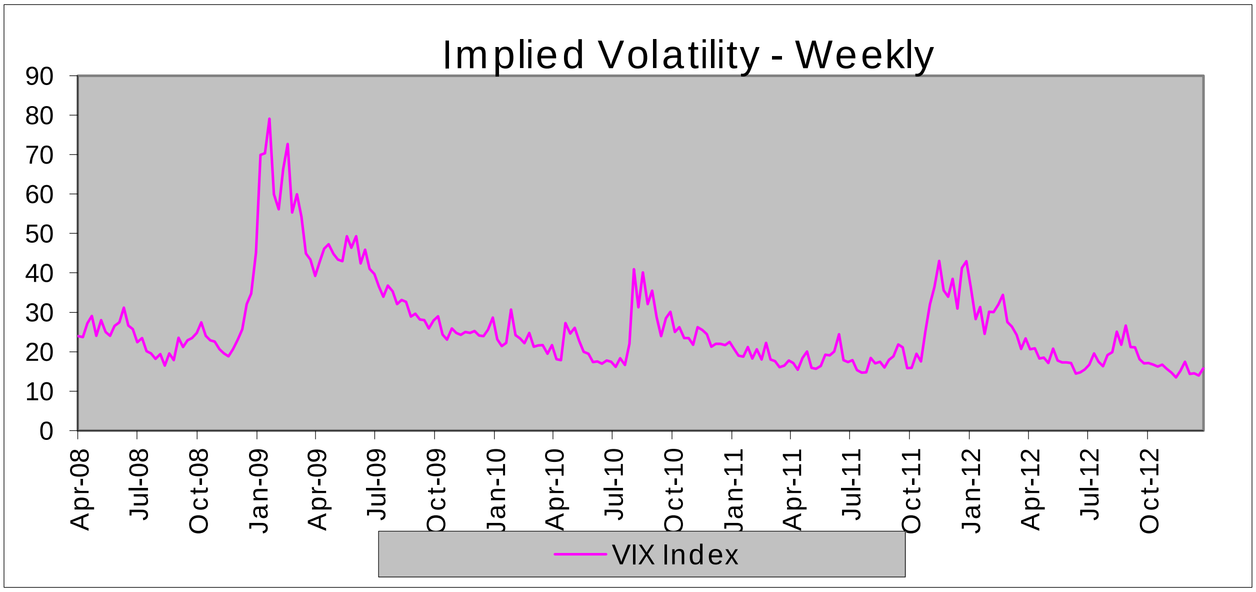
Period Ended December 31, 2012

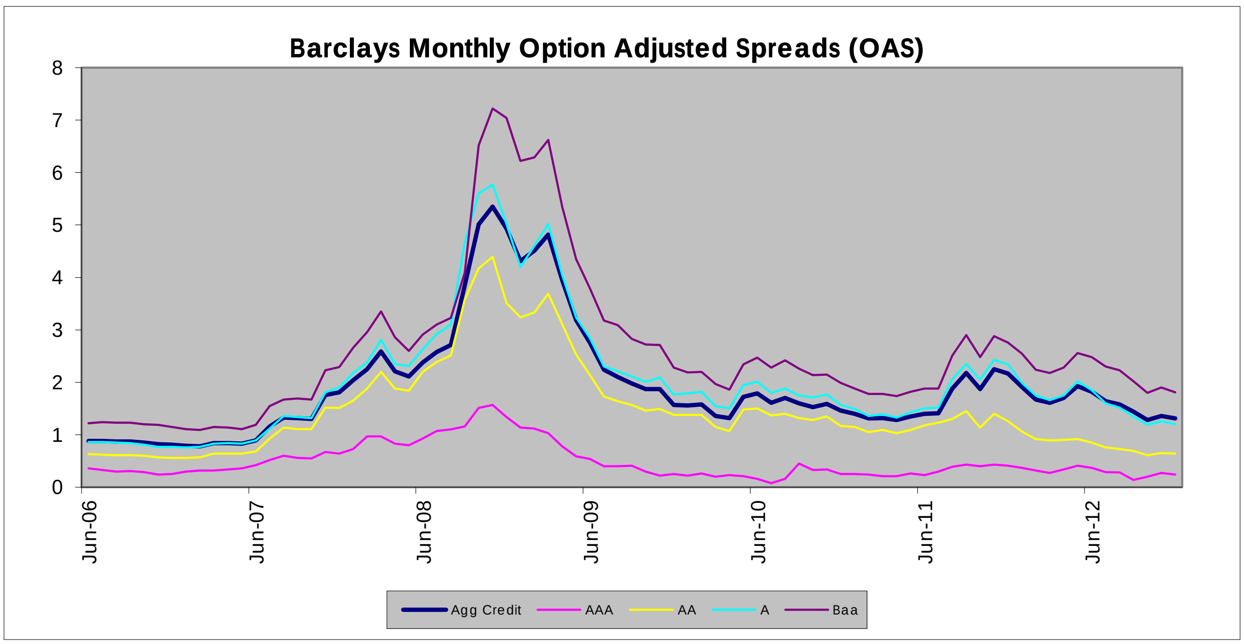




RISK TRENDS

Period Ended December 31, 2012





INVESTMENT PERFORMANCE REPORT

Period Ended December 31, 2012

UCRP, GEP, AND TRIP ASSET CLASS PERFORMANCE

UC Entity		Return		
	Market Value ($M)	**Quarter (%)**	**Fiscal YTD (%)**	**Calendar YTD (%)**
UCRP	$43,817	2.52	7.50	13.68
Policy Benchmark		2.36	7.13	12.69
Variance to Benchmark		*+0.16*	*+0.37*	*+0.99*
GEP	$6,829	2.75	7.27	12.80
Policy Benchmark		2.31	6.53	11.03
Variance to Benchmark		*+0.44*	*+0.74*	*+1.77*
STIP	$8,376	0.61	1.24	2.43
Policy Benchmark		0.06	0.10	0.21
Variance to Benchmark		*+0.55*	*+1.14*	*+2.22*
TRIP	$4,510	2.02	6.06	12.53
Policy Benchmark		1.96	5.85	11.85
Variance to Benchmark		*+0.06*	*+0.21*	*+0.68*
Total Assets	$75,428	2.08	6.19	11.46
Entity Benchmark		1.86	5.70	10.28
Variance to Benchmark		*+0.22*	*+0.49*	*+1.18*

Period Ended December 31, 2012

UC RETIREMENT PLAN	Market Value ($M)	Total Return: Recent Quarter	Total Return: Fiscal YTD	Total Return: Calendar YTD	Excess Return: Recent Quarter	Excess Return: Fiscal YTD	Excess Return: Calendar YTD
	$43,817	**2.52%**	**7.50%**	**13.68%**	***+0.16%***	***+0.37%***	***+0.99%***
EQUITIES							
U.S. Equity	11,147	0.49	6.90	16.86	*+0.15*	*+0.22*	*+0.35*
Non-U.S. Equity-Developed	8,493	5.87	13.52	16.79	*-0.17*	*-0.36*	*+0.30*
Emerging Market Equity	3,248	5.78	13.66	19.87	*+0.20*	*-0.09*	*+1.65*
Global Equity	879	2.99	10.04	16.47	*+0.00*	*+0.00*	*+0.09*
FIXED-INCOME SECURITIES							
Core Fixed Income	4,594	0.51	3.26	5.99	*+0.30*	*+1.46*	*+1.78*
High Yield Bond	1,341	3.39	7.97	16.09	*+0.24*	*+0.10*	*+0.65*
Emerging Market Debt	1,182	3.03	9.52	16.71	*-0.21*	*+0.05*	*-0.01*
TIPS	2,963	0.73	3.01	7.29	*+0.04*	*+0.19*	*+0.31*
ALTERNATIVE ASSETS							
Private Equity	3,347	2.89	3.24	10.84	-	-	-
Absolute Return-Diversified	2,573	2.98	5.87	8.35	*+2.02*	*+3.15*	*+6.12*
Absolute Return-Cross Asset Class	964	1.44	7.09	12.14	*-0.92*	*-0.04*	*-0.55*
Real Assets	725	-0.19	1.35	4.48	*+0.25*	*+0.17*	*+0.42*
Public Real Estate	216	5.77	11.73	28.16	*-0.54*	*-1.03*	*-1.69*
Private Real Estate	2,090	1.37	3.66	11.87	*-1.16*	*-1.22*	*+1.40*

GENERAL ENDOWMENT POOL	Market Value ($M)	Total Return: Recent Quarter	Total Return: Fiscal YTD	Total Return: Calendar YTD	Excess Return: Recent Quarter	Excess Return: Fiscal YTD	Excess Return: Calendar YTD
	$6,829	**2.75%**	**7.27%**	**12.80%**	***+0.44%***	***+0.74%***	***+1.77%***
EQUITIES							
U.S. Equity	1,128	0.40	6.81	16.80	*+0.06*	*+0.13*	*+0.29*
Non-U.S. Equity-Developed	923	5.83	13.46	16.92	*-0.21*	*-0.42*	*+0.43*
Emerging Market Equity	451	5.95	13.82	20.33	*+0.37*	*+0.07*	*+2.11*
Global Equity	2	2.99	10.04	16.48	*+0.00*	*+0.00*	*+0.10*
FIXED-INCOME SECURITIES							
Core Fixed Income	344	0.51	3.62	5.73	*+0.30*	*+1.82*	*+1.52*
High Yield Bond	194	3.40	7.99	16.08	*+0.25*	*+0.12*	*+0.64*
Emerging Market Debt	195	3.07	9.68	16.94	*-0.17*	*+0.21*	*+0.22*
TIPS	186	0.70	2.99	7.16	*+0.01*	*+0.17*	*+0.18*
ALTERNATIVE ASSETS							
Private Equity	628	2.89	3.24	10.89	-	-	-
Absolute Return-Diversified	1,505	2.98	5.87	8.35	*+2.02*	*+3.15*	*+6.12*
Absolute Return-Cross Asset Class	193	1.50	7.22	12.59	*-0.81*	*+0.69*	*+1.56*
Opportunistic Equity	445	-	-	-	-	-	-
Real Assets	128	0.42	1.44	3.84	*+0.76*	*+0.24*	*-0.11*
Public Real Estate	31	5.86	11.91	28.18	*-0.45*	*-0.85*	*-1.67*
Private Real Estate	467	2.49	5.18	11.06	*-0.04*	*+0.30*	*+0.59*

TOTAL RETURN INVESTMENT POOL	Market Value ($M)	Total Return: Recent Quarter	Total Return: Fiscal YTD	Total Return: Calendar YTD	Excess Return: Recent Quarter	Excess Return: Fiscal YTD	Excess Return: Calendar YTD
	$4,510	**2.02%**	**6.06%**	**12.53%**	***+0.06%***	***+0.21%***	***+0.68%***
EQUITIES							
U.S. Equity	672	0.37	6.69	16.80	*+0.03*	*+0.01*	*+0.29*
Non-U.S. Equity-Developed	682	7.50	12.47	17.01	*+0.70*	*+0.48*	*+0.71*
FIXED-INCOME SECURITIES							
Core Fixed Income	2,479	0.81	4.37	9.27	*-0.02*	*+0.45*	*+1.17*
High Yield Bond	449	2.79	6.40	13.3	*-0.29*	*-1.27*	*-1.33*
ALTERNATIVE ASSETS							
REITS	229	2.56	2.71	17.76	*+0.01*	*+0.02*	*-0.22*

UCRP ASSET CLASS PERFORMANCE ATTRIBUTION

Period Ended December 31, 2012

UCRP Attribution	Recent Quarter			Calendar Year to Date		
	Asset Allocation %	Asset Selection %	Total	Asset Allocation %	Asset Selection %	Total
EQUITY						
U.S. Equity	(0.00)	0.04	0.04	0.04	0.08	0.13
Non-U.S. Equity	0.01	(0.03)	(0.03)	0.00	0.04	0.04
Emerging Market Equity	0.01	0.01	0.03	(0.01)	0.09	0.08
Global Equity	0.00	-	0.00	0.01	0.00	0.01
FIXED INCOME						
Core Fixed Income	0.02	0.04	0.06	0.08	0.20	0.28
High Yield Debt	0.01	0.01	0.01	0.02	0.01	0.03
Emg Mkt Debt	0.00	(0.01)	(0.00)	0.00	0.00	0.00
TIPS	0.02	0.00	0.02	0.05	0.02	0.07
ALTERNATIVES						
Private Equity	0.00	-	0.00	(0.02)	-	(0.02)
Abs Return - Diversified	(0.00)	0.12	0.12	(0.01)	0.35	0.35
Abs Return - CAC	(0.00)	(0.02)	(0.02)	(0.00)	(0.01)	(0.02)
Real Assets	(0.01)	0.00	(0.00)	(0.01)	0.00	(0.01)
Real Estate - Private	(0.00)	(0.07)	(0.07)	(0.01)	0.05	0.04
Real Estate - Public	0.00	0.01	0.01	(0.01)	(0.01)	(0.02)
Cash	(0.00)	-	(0.00)	0.01	-	0.01
TOTAL	**0.05**	**0.11**	**0.16**	**0.15**	**0.84**	**0.99**

GEP ASSET CLASS PERFORMANCE ATTRIBUTION

Period Ended December 31, 2012

GEP Attribution	Recent Quarter			Calendar Year to Date		
	Asset Allocation %	Asset Selection %	Total	Asset Allocation %	Asset Selection %	Total
EQUITY						
U.S. Equity	0.00	0.01	0.02	0.03	0.05	0.08
Non-U.S. Equity	0.03	(0.03)	(0.01)	(0.02)	0.05	0.03
Emerging Market Equity	0.02	0.02	0.04	(0.00)	0.10	0.10
Global Equity	(0.01)	-	(0.01)	(0.01)	0.00	(0.01)
FIXED INCOME						
Core Fixed Income	0.01	0.02	0.03	0.04	0.08	0.12
High Yield Debt	0.01	0.01	0.01	0.01	0.02	0.02
Emg Mkt Debt	0.00	(0.01)	(0.00)	(0.01)	0.01	0.00
TIPS	0.02	0.00	0.02	0.05	0.01	0.05
ALTERNATIVES						
Private Equity	0.01	(0.00)	0.01	(0.03)	(0.00)	(0.03)
Abs Return - Diversified	0.02	0.47	0.49	(0.02)	1.38	1.36
Abs Return - CAC	(0.00)	(0.02)	(0.02)	0.01	0.02	0.03
Opportunistic Equity	(0.01)	-	(0.01)	(0.01)	-	(0.01)
Real Assets	0.00	0.01	0.01	(0.01)	0.00	(0.01)
Real Estate – Private	(0.01)	(0.13)	(0.14)	(0.01)	0.03	0.02
Real Estate - Public	0.00	(0.03)	(0.03)	(0.04)	(0.01)	(0.05)
Cash	0.00	-	0.00	0.04	-	0.04
TOTAL	**0.11**	**0.33**	**0.44**	**0.02**	**1.74**	**1.76**

TRIP ASSET CLASS PERFORMANCE ATTRIBUTION

Period Ended December 31, 2012

TRIP Attribution	Recent Quarter			Calendar Year to Date		
	Asset Allocation %	Asset Selection %	Total	Asset Allocation %	Asset Selection %	Total
EQUITY						
U.S. Equity	(0.00)	0.01	0.00	(0.00)	0.04	0.04
Non-U.S. Equity	0.01	0.10	0.10	0.01	0.10	0.11
FIXED INCOME						
Core FI – Govt.	(0.00)	0.00	0.00	0.01	0.03	0.04
Core FI - Credit	(0.01)	(0.03)	(0.04)	0.03	0.50	0.53
Core FI - Collateral	0.01	0.01	0.02	0.02	0.06	0.08
High Yield Debt	(0.00)	(0.03)	(0.03)	0.01	(0.12)	(0.10)
ALTERNATIVES						
REIT	(0.00)	0.00	(0.00)	0.01	(0.01)	(0.00)
TOTAL	**0.00**	**0.06**	**0.06**	**0.08**	**0.60**	**0.68**

PUBLIC EQUITY

Period ended December 31, 2012

Public Equity Returns	Total Return		Excess Return	
	Quarter (%)	1-Year (%)	Quarter (%)	1-Year (%)
US Equity – Combined (UCRP & GEP)	0.48	16.86	0.14	0.35
US Equity - UCRP	0.49	16.86	0.15	0.35
US Equity - GEP	0.40	16.80	0.06	0.29
Non-US Developed - Combined (UCRP & GEP)	5.85	16.81	-0.19	0.32
Non-US Developed Equity - UCRP	5.87	16.79	-0.17	0.30
Non-US Developed Equity – GEP	5.83	16.92	-0.21	0.43
Emg. Mkt. Equity - Combined (UCRP & GEP)	5.89	20.01	0.31	1.79
Emg. Mkt. Equity - UCRP	5.78	19.87	0.20	1.65
Emg. Mkt. Equity - GEP	5.95	20.33	0.37	2.11

Highlights of the Public Equity Asset Class

- All three public equity portfolios outperformed in 2012. In 2010 and 2011 stocks traded more on economic news and policy activism and less on their individual business performance, but in 2012 stocks traded more on their specific business results. That helped the actively managed portion of the U.S. equity portfolio outperform by 1.31% in 2012.
- The U.S. Equity portfolio is overweight Technology. There are two reasons why. First, demand is strong, from companies seeking to enhance productivity as well as demand for consumer electronics. Second, valuations are modest. Technology is trading at prices in line or slightly below the broader market. Strong demand and modest prices suggests that Technology represents good investment value going forward.
- The Non-U.S. Developed Markets portfolio is notably underweight Financials due to the sovereign debt problems plaguing European governments and banks. The portfolio has a positive tilt toward Technology and toward companies doing additional business with Emerging Markets. The technology overweight is backed by the same sector dynamics as in the U.S. The tilt toward companies doing additional business in Emerging Markets is due to the higher economic growth in those markets as compared to Europe and Japan.
- The Emerging Markets portfolio is underweight large multi-national emerging market companies that rely more on exports, due to weak economic growth in developed markets. The portfolio is overweight companies with exposure to local demand and emerging market countries that trade with each other. The portfolio is also overweight Consumer Staples and Consumer Discretionary, due to strong wage growth, low unemployment, and rising living standards in most emerging countries.
- Valuations are slightly below long-term averages, which could bode well for long-term future returns. The price-earnings ratio of the U.S., Non-U.S. Developed Markets, and Emerging Markets portfolios are currently 13.9, 11.9, and 12.3, respectively.

Public Equity Portfolio Review

The U.S. Equity Portfolio* edged up 0.48% for the quarter while the Russell 3000 Tobacco Free index inched up 0.34%, an outperformance of 0.14%. For the year the portfolio gained 16.86% while the index returned 16.51%, an outperformance of 0.35%.

- In 2012 the actively managed portion of the U.S. equity portfolio outperformed by 1.31%, its best year since 2009 when it outperformed by more than 5%.
- Utilities and Energy were weaker performers relative to the broader index return in 2012, with returns of 2.27% and 3.92% respectively based on Russell sector indices. Our underweight in both sectors added to performance.
- Large Cap Value and Small Cap Value managers significantly outperformed their benchmarks by 0.71% and 0.85%, respectively, during the quarter.
- For the calendar year, the large-cap core managers performed well, rallying 19.07% with an outperformance of 2.65% over the Russell 1000 index. Strong security selection in the Health Care and Consumer Discretionary sectors contributed significantly to performance.

Non-U.S. Developed Equity Portfolio* gained 5.85% during the quarter while the MSCI World ex-U.S. index rose 6.04%, an underperformance of 0.19%. For all of 2012, the portfolio gained 16.81% while the index returned 16.49%, an outperformance of 0.32%.

- 2012 was the tale of two halves for the Non-U.S. Developed Markets as the MSCI World ex. U.S. Index was up only 2.43% in the first half of the year but rallied 13.65% in the second half. The rally was led by the Financials sector and specifically European banks. The active Non-U.S. Developed portfolio outperformed in the first half by 0.96% (3.39% vs. 2.43%) while lagged the second half by -0.67% (12.98% vs. 13.65%).
- In calendar year 2012, strong stock selection in the Technology sector was a contributor to performance. Stock selection in the Industrials sector was another contributor to performance in 2012.
- The underperformance in the quarter and the second half of 2012 was attributed to an underweight to Financials as the sector solidly outperformed the broader market. The majority of our active managers have continued to underweight European banks due to them being undercapitalized and worrisome levels of sovereign debt commitments to other troubled banks.
- Japan was the biggest detractor to performance from a regional perspective during the quarter and 2012. The majority of Japan underperformance came during December, when Japanese exporters and financials rallied based on expectations of Quantitative Easing from Japan's Central Bank (BOJ).

Emerging Markets Portfolio* rose 5.89% during the quarter while the MSCI Emerging Markets index gained 5.58%, an outperformance of 0.31%. For all of 2012 the portfolio returned 20.01% while the benchmark gained 18.22%, an outperformance of 1.79%.

- The actively managed portion of the portfolio did especially well, returning 21.33% for the year while the benchmark gained 18.22%, an outperformance of 3.11%.
- Positive stock selection across the portfolio, an overweight to Consumer Staples, and overweights to Turkey and Thailand enabled the portfolio to outpace the benchmark in the fourth quarter and outperform in 2012.
- Consumer Staples (25.4%) and Financials (25.5%) outperformed the broader emerging markets for the year. For the quarter, returns were equally strong in Consumer Staples (7.6%) and Financials (10.0%).

- China and India also rebounded significantly and were up 22.7% and 26.0% respectively for 2012. The portfolio was affected by a -6% underweight to China, as the country outperformed the index by 7.5% in the fourth quarter.

Looking Forward

- In all three active portfolios – U.S., Non-U.S. Developed Markets, and Emerging Markets – we are increasing our allocation to active managers that are particularly different than their benchmarks. These strategies should do well in an environment where a company's stock price moves more in tandem with their specific business results rather than economic news.
- GEP's Opportunistic Equity portfolio was implemented in December 2012. The remainder will be invested in the first quarter of 2013. The investment objective of the Opportunistic Equity portfolio is to earn higher excess returns than is usually earned in traditional long-only strategies by investing in public equity in more differentiated strategies.

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*Combined UCRP and GEP.

FIXED INCOME

Period ended December 31, 2012

Fixed Income Returns	Total Return		Excess Return	
	Quarter (%)	1-Year (%)	Quarter (%)	1-Year (%)
Core FI - Combined (UCRP & GEP)	0.51	5.96	0.30	1.75
UCRP – Core FI	0.51	5.99	0.30	1.78
GEP – Core FI	0.51	5.73	0.30	1.52
High Yield Debt - Combined (UCRP & GEP)	3.40	16.11	0.25	0.67
Emg. Mkt. Debt - Combined (UCRP & GEP)	3.04	16.74	-0.20	0.02
STIP	0.61	2.43	0.55	2.22
TRIP-Core FI	0.81	9.27	-0.02	1.17

Fixed Income Highlights

The quarter presented a familiar performance profile across fixed income sectors. Securities with credit exposure such as corporates, high yield, and emerging market bonds outperformed U.S. government securities.

From an active return perspective, the best performer in the actively-managed Core portfolios was once again the Collateralized sector. UCRP/GEP Core Collateral outperformed its benchmark by over 0.75% for the quarter and by 3.54% for the fiscal-year-to-date. The main contribution to excess return came from the legacy non-agency RMBS holdings, which has returned 17% versus the Collateralized benchmark return of 1.17% for the fiscal-year-to-date. Non-agencies represent 10% of the portfolio and should continue to provide alpha.

The best overall return during the quarter was provided by High Yield, with the UCRP/GEP combined portfolio returning 3.4%. For the year, Emerging Market Debt had the best outcome, returning 18.1%.

Fixed Income Portfolio Review

Core Fixed Income

- For the year, active credit returned 10.77% versus 3.25% for governments and 5.52% for collateralized. An overweight to credit as well as sector outperformance generated excess returns of 175 basis points for actively managed Core UCRP and GEP.
- The collateralized sector outperformed the most on a relative basis, outperforming its benchmark by 75 basis points for the quarter and 251 basis points for the year. Performance was driven by the continued recovery in the non-agency MBS market and strong returns in CMBS.

High Yield Market

- The High Yield portfolios delivered another strong quarter, returning 3.40%. The calendar year return was 16.11%, an excess return of 0.67%.
- Outperformance in the externally managed portfolios more than offset some slight underperformance in the internally managed portfolios.

- Internal portfolios lagged partially due to an underweight to the financial sector, which was one of the top performing sectors for the year with a return of 29%.

Emerging Market Debt

- Performance lagged slightly in the fourth quarter. Returns were lower in the internally managed funds, which were somewhat underweight, the lower quality, higher yielding sovereigns such as Nigeria and Hungary which were top performers.
- The external local currency EM manager, Wellington Management Co., was the star performer in Q4, returning 6.13%, an excess return of 2.0% over the local currency benchmark.
- For the full year, EM managed to perform in-line with the benchmark, outperforming by two basis points. Underperformance in the internal portfolio was offset by strong performance by Wellington.

TRIP

TRIP Core has an 83% policy weight to the Credit Sector versus a 27% weight in the other Core portfolios. The credit-heavy TRIP portfolio has benefited from that allocation in 2012, returning 9.27% versus the UCRP/GEP Core return of 5.96% for 2012.

TIPS

TIPS, along with US Treasuries, continue to be the most expensive asset class in dollar-denominated fixed income. Through its QEIII program, the Fed is trying to keep real yields low and for the most part is succeeding. As such, we remain structurally underweight and overweight High Yield, Emerging Market Debt and Investment Grade Credit. Active return in TIPS was generated primarily by security selection.

STIP

STIP continues to benefit from corporate securities purchased 3-4 years ago. As those securities mature and the proceeds are reinvested at current, low yields, the income return will inevitably fall. At the same time, the maturity profile of STIP is slowly being adjusted to take advantage of the eventual hike in interest rates.

Looking Forward

The Federal Reserve Bank lowered the Fed funds rate to 0.25% in December of 2008 and has kept it there since. They have had three distinct programs of so called “Quantitative Easing,” buying literally trillions of RMBS and U.S. Treasury securities endeavoring to keep longer term market interest rates low and flooding the banking system with reserves. Any forward-looking discussion of the economy and financial markets has to take into account the eventual unwinding of this unprecedented monetary stimulus.

Core portfolios have been structurally underweight Government securities and overweight IG Credit, Collateralized, High Yield and Emerging Market bonds. This positioning has contributed to outperformance over the last year and should create excess return in the initial stages of Fed tightening.

PRIVATE EQUITY

Period Ended December 31, 2012

Private Equity Returns	Total Return	
	Quarter (%)	1-Year (%)
Private Equity – combined (UCRP & GEP)	2.89	10.85
Private Equity – UCRP	2.89	10.84
Private Equity – GEP	2.89	10.89
Co Investments – UCRP & GEP	8.50	41.50
Buyouts – UCRP & GEP	0.57	7.41
Venture Capital – UCRP & GEP	6.91	15.76

Private Equity Highlights

- Returns for the quarter were driven by the co-investment and venture capital segments of the portfolio while the buyout segment experienced weak returns.
- The UC made a total of eighteen investments throughout 2012 which represents $637 million in commitments. Buyout funds represented 76% of new commitments while venture capital accounted for 12%. Co-investments accounted for the remaining 12% of the commitments for the calendar year.
- The UC closed five co-investments in 2012 representing $74 million. Additionally, two co-investments concluded diligence in late 2012 and are expected to close in early 2013. The co-investment pipeline continues to remain healthy.
- Staff continues to pursue a secondary purchase strategy for select funds but has shifted its focus to actively pursuing a sale of select non-core funds with a goal of enhancing future returns.
- The private equity portfolio has been in build up mode the past decade. However, 2012 was the first year in many years that the private equity portfolio received more cash back from managers than cash contributed to managers as the portfolio is approaching maturity. Distributions over the fourth quarter were very strong, up 132% compared to the prior year period and capital calls were on par with the prior year period.

Private Equity Portfolio Review

- The private equity returns for the fourth quarter modestly outperformed the entity return primarily driven by increased values in the venture capital portfolio and strong performance in the co-investment portfolio. These returns were partially offset by weak buyout returns for the quarter.
- The fourth quarter investment activity was robust as many companies were bought and sold due to expected tax increases in 2013. This investment activity was aided by a strong debt market that provided managers with access to attractive low cost covenant-lite debt.
  - As a result, fourth quarter distributions of $325 million were very strong versus $140 million for the prior year period. Capital calls of $215 million over the fourth quarter were strong, but flat compared with the prior year period.

- For calendar year 2012, distributions reached their highest level since the dot com bubble of 2000 with $820 million distributed versus $507 million for the prior year period. Capital calls were also strong with $792 million called versus $709 million called in the prior year.

Commitment Pacing and Other Activity

- Calendar year 2012 commitments were $637 million which was slightly below the strategic target of $700 million for the year. This was lower than initially projected due to managers shifting fundraising into the 2013 calendar year as a result of a difficult fundraising environment.
- Staff committed $123 million to three new investments in the fourth quarter. This consisted of two new fund investments and one co-investment.
- The UC is continuing to build out its co-investment program to enhance returns. For calendar year 2012, Staff sourced twenty-four transactions and completed five transactions, one of which closed in the fourth quarter. This was consistent with the strategic target for the year of five completed co-investments.

Looking Forward

- The private equity portfolio is expected to reach maturity in 2015 based on the current strategic asset allocation target. The portfolio is expected to be cash flow positive in 2013 and in future years barring a difficult economic environment where the exit environment for companies will be poor. Currently, the portfolio is experiencing a strong M&A market driving both acquisitions and exits. The IPO market continues to face uncertainty and many companies have pushed off going public until increased demand for new IPO's returns to the market.
- The target allocation to co-investments was significantly increased in 2012 to help foster enhanced returns from savings on management fees and carry. The current portfolio has also demonstrated strong returns as a result of deal selection. The target deal activity in 2013 is significantly higher than 2012 with a target of $200 - $250mm of total commitments to co-investments which is about 30% of the target commitments for private equity. This requires the team to be able to complete 8 – 10 co-investments for the year.
- Calendar year 2013 commitments are expected to be around $750 million, up slightly from $637 million in 2012.
- Staff is continuing its process in seeking to sell select non-core assets if we are able to obtain pricing that enhances our long-term portfolio returns.

ABSOLUTE RETURN

Period Ended December 31, 2012

Absolute Return - Div	Total Return	
	Quarter (%)	1-Year (%)
UC AR Portfolio	2.98	8.35
HFRX AR and MD Blended Index	0.96	2.23
HFRI Fund of Funds	1.34	4.81
S&P 500	-0.38	16.00
Barclays Aggregate Bond Index	0.21	4.21

Absolute Return Highlights

- The team continues to make tactical adjustments across strategies within the portfolio. During the quarter we added to Hedged Equity and Distressed strategies, and decreased the size of the Global Macro portfolio.
- We continue to reduce the number of hedge fund managers in an effort to concentrate the portfolio.
- There was meaningful dispersion across the HFRI strategy indices for the quarter and the year.
  - For the quarter, Emerging Markets was the top-performing major HFRI strategy with a +4.9% gain, while Macro was the bottom-performing major HFRI strategy with a -1.0% loss.
  - For the full year, Relative Value Arbitrage was the top-performing major HFRI strategy with a +10.7% gain, while Macro was the bottom-performing major HFRI with a -0.1% loss.
  - 2012 was the fourth consecutive calendar-year gain for the Relative Value Arbitrage strategy.
- Total capital invested into the global hedge fund industry increased to a record $2.25 TN on positive performance and net inflows, according to Hedge Fund Research for the quarter.
  - Investors allocated $3.4 BN of net new capital to hedge funds during the quarter, bringing 2012 net inflows to $34.4 BN.
  - Relative Value Arbitrage strategies received $6.5 BN of inflows during the quarter, bringing full-year capital inflows to $41.4 BN. Relative Value Arbitrage became the largest hedge fund strategy for the first time since 1991 with $609 BN in assets.

Absolute Return Portfolio Review

- During the quarter, the UC AR portfolio posted a gain of +3.0%, outperforming its HFRX benchmark by 202 basis points. For comparative purposes, the HFRI Fund of Funds Index gained +1.3% over the same period.
- All major strategies in the portfolio were positive contributors to performance during the quarter and the calendar year.
- The largest positive contributors to performance during the quarter were Emerging Markets, Relative Value, and Event Driven strategies.
  - Emerging Markets equities had strong returns during the quarter, which helped bolster the performance of the Emerging Markets strategy in the portfolio.

- Relative Value profited from tightening high yield credit spreads, an improvement in the U.S. housing market which buoyed the RMBS market, and a positive European ABS market.
- Event Driven benefitted from idiosyncratic corporate and sovereign events, positive earnings announcements for select portfolio companies, and increased M&A activity.

Looking Forward

- Investors are cautiously optimistic with expectations for an improving global economic outlook.
- While there has been a reduction in tail risks, there are still a number of potential headwinds including the U.S. debt ceiling and budget sequester, the Euro zone crisis, and constrained economic growth in China.
- As regulators heighten their scrutiny of hedge fund managers, we will maintain the strength of our internal due diligence and monitoring processes.
  - Insider trading continues to be a high priority area for financial regulators and federal prosecutors. Over the last three years, the SEC has filed more insider trading actions (168 in total) than in any three-year period in the agency's history.

CROSS-ASSET CLASS

Period Ended December 31, 2012

Absolute Return - CAC	Total Return		Excess Return	
	Quarter (%)	1-Year (%)	Quarter (%)	1-Year (%)
AR CAC – Combined (UCRP & GEP)	1.45	12.21	-0.90	-0.25

Cross Asset Class Highlights

- The Cross-Asset Class (“CAC”) strategy closed the year with returns short of the policy. The focus on risk diversification across economic regimes under uncertain market conditions has been beneficial since inception of the portfolio, where average annual returns of 10.18% are well in excess of the policy’s return of 4.16%. However, as equity markets have rallied relative to treasuries, our risk weighted exposure to nominal fixed income has dampened returns over the recent period.
- We continue to focus our new funding efforts on satellite strategies which can invest in areas which have shown steep pricing dislocations. In the fourth quarter we expanded our investment in a diversified residential mortgage loan pool purchased at deeply discounted prices to the underlying collateral.
- Although the mortgage loan pool strategy had its most recent funding in the recent quarter, we are already seeing contributions from loan workouts and income, despite an expected ramp up period for the investment.
- As of December 31, the Cross Asset Class Absolute Return holds $1.2B under management within the UC Retirement (UCRP) and Endowment (GEP) plans, accounting for over 2% of each of the respective plan’s exposure.

Cross Asset Class Portfolio Review

- The CAC strategy has lagged over the quarter and calendar year periods primarily due to a significant exposure to risk balanced portfolios which are meant to provide balanced exposures in periods of rising and falling growth. For the quarter, episodic risk rallies as the result of policy initiatives to address the fiscal cliff were dampened by risk adjusted exposure to sovereign debt and nominal bonds.
- For the quarter, broad asset allocation strategies among our managers were generally positive, including an overweight to high yield relative to core fixed income. The drag in the quarter came from four key areas: the more significant exposure to fixed income from our risk parity managers, the increase in tail risk hedging by one of our strategic partners to protect against uncertainty from the fiscal cliff, a write down in one of our holdings, and ramp up costs in executing a new mortgage loan modification strategy.
- As the markets continued to show unevenness and sharp reversals over the year, a newly introduced tactical strategy was launched by a manager. The low beta equity strategy aims to deliver well over half the beta of the global equity market, while incurring half the market volatility. This strategy did especially well as a substitute for a pure equity allocation within the strategic partner’s portfolio as markets reacted to European debt uncertainties in the second quarter. However, the strategy will lag a pure beta market exposure in a sharp recovery period as it did late in the fourth quarter.

Looking Forward

- We have recently increased our investment in a loan modification strategy, which specifically targets enhancing the loan profile of deeply discounted distressed, as well as re-performing mortgage whole loans, and selling them at a premium to purchase price, through work-outs or refinancing.
  - This specific strategy also highlights the importance of selecting and training the right servicer to conduct loan work-outs with the borrower.
  - Staff has also considered expanding our thesis of a residential housing recovery to other direct residential housing investments, including buy to lease programs, which still have potential to benefit from further pricing appreciation.
- Staff continues to evaluate the merits of incubating strategies which take advantage of current market dislocations and strategies providing diversification and risk control. These additions would be more modest satellite allocations framing our key strategic partnerships. Given the smaller capital commitments, the Cross Asset Class satellite strategies may be a testing ground for potentially larger scale application within the aggregate plan.
- We are reviewing at least one additional Cross-Asset Class strategic partner who will be selected for their flexibility and expertise across global asset classes. Given the rapidly shifting landscape, as economies recover from various cycles of deleveraging, we are looking to managers who can provide a lens on the global landscape, and have skill to provide value add through tactical allocation.

REAL ASSETS

Period Ended December 31, 2012

Real Assets Returns	Total Return[1]		Excess Return	
	Quarter (%)	1-Year (%)	Quarter (%)	1-Year (%)
Real Assets - Combined (UCRP & GEP)	-0.09	4.36	0.25	0.41
Real Assets – UCRP	-0.19	4.48	0.25	0.42
Real Assets – GEP	0.42	3.84	0.76	-0.11

Real Assets Highlights

- The Real Assets composite decreased by -0.09% for the quarter. Returns were positively impacted by the Energy portfolio, which was up 1.31% for the quarter, the Infrastructure portfolio, which was up 0.70% for the quarter, and the Timberland portfolio, which was up 0.39% for the quarter. The Commodities and Opportunistic portfolios detracted from performance with quarterly returns of -2.80% and -0.47% respectively.
- Real Assets were up 4.36% for the calendar year resulting in 41 basis points of excess return. Strong returns by the Infrastructure and Opportunistic portfolios were positive contributors while relative excess performance was driven by outperformance by the Commodities portfolio. As the Real Assets portfolio is still in its build-up phase the J-curve remains a drag on performance. Staff expects the J-curve to have less influence in the coming years as unfunded commitments are drawn and Staff continues its focus on fee-efficient co-investments.
- Staff made six new investments (including two co-investments and one secondary purchase) during the quarter, bringing the portfolio to a net asset value of $853 million with $700 million in unfunded capital commitments and a total exposure of $1.5 billion. The portfolio is now comprised of 36 investments.
- Investment activity was strong during the quarter with total cash outflows of $126.9 million, which included $56.9 million to the Energy portfolio, $46.1 million to Infrastructure, and $23.8 million to the Opportunistic portfolio. This level of activity is consistent with Staff's strategic plan given the relative immaturity of the Real Assets portfolio.
- Since inception on April 1, 2010, the Real Assets composite has generated an annualized return of 12.58%, which has been accretive to entity level returns. The Real Asset portfolio's returns have been broad based with all of the underlying portfolios demonstrating positive returns since inception.

Real Assets Portfolio Review

- The Real Assets composite decreased by -0.09% for the quarter. Returns were positively impacted by the Energy portfolio, the Infrastructure portfolio, and the Timberland portfolio while the Commodities and Opportunistic portfolios detracted from overall performance.
- The Commodity portfolio currently comprises 20% of the Real Assets composite. It was a negative contributor to absolute performance for the quarter with a return of -2.80%, but outperformed the S&P GSCI Reduced Energy Index return of -3.99% by 119 basis points. Relative outperformance during the fourth quarter was largely attributable to the portfolio's underweight to natural gas and the agriculture sector, which declined -11.0% and -10.1%, respectively. Since inception (August 2010), the portfolio has delivered positive alpha with an annualized return of 7.94% versus 5.93% for the benchmark.

- The Energy portfolio currently comprises 30% of the Real Assets composite. It was a positive contributor to overall performance for the quarter with a return of 1.31%. The portfolio saw positive returns across several its key investments. Since January 2010, the Energy portfolio has generated an annualized return of 17.45%. Three new investments were added to the portfolio during the quarter, including a secondary purchase and a co-investment in an upstream energy company.
- The Infrastructure portfolio was a positive contributor for the quarter with a 0.70% return. The portfolio currently represents 22% of the overall Real Assets portfolio. Staff completed two new investments in this portfolio during the quarter including a co-investment within the midstream energy sector.
- The Timberland portfolio was a positive contributor for the quarter with a 0.39% return. The portfolio remains heavily dominated by one asset that has an attractive long-term return profile, but a low current cash yield, particularly in the early years. The portfolio currently represents 16% of the overall Real Assets portfolio. This allocation is expected to decrease over time as Staff focuses on more compelling opportunities across other segments of the portfolio.
- The UC has committed to five Opportunistic investment strategies, including a new investment made during the quarter in a fund targeting the mining and minerals sector. This portfolio currently represents 11% of the Real Assets portfolio.
- Investment activity was strong during the quarter with net cash outflows of $109.5 million as a result of capital calls made by existing managers, new investments, and follow-on investments in the Commodity portfolio. This level of activity was higher than the previous quarter, which saw cash outflows of $83.2 million. Since the portfolio is still in the early stages of the J-curve, the portfolio's cash distributions are expected to be lower than the long-term expectation.

Looking Forward

- Staff has a robust pipeline of new investments that are currently being evaluated and we expect to see significant co-investment deal flow in 2013. Staff created three co-investment vehicles in the second half of 2012 that will seek to participate in select deals alongside managers. These structures should help drive significant transaction activity for the UC in the coming years.
- The current pipeline of opportunities includes investments within the midstream energy sector, a drug royalty fund, an agriculture strategy, and a re-up with an existing infrastructure fund. Staff is currently actively involved in conducting diligence on a near-term infrastructure co-investment that is expected to close during the first quarter.
- The secondary market has become generally less attractive relative to primary opportunities due to seller pricing expectations. However, Staff is continuing to actively review secondary opportunities on a select basis.
- Staff continues to take a measured and constructive approach in evaluating new opportunities. Areas of particular interest include the midstream energy sector, metals and mining, international timberland, and royalty-based strategies.

REAL ESTATE

Period Ended December 31, 2012

Real Estate Returns	Total Return		Excess Return	
	Quarter (%)	1-Year (%)	Quarter (%)	1-Year (%)
Private Real Estate – UCRP	1.37	11.87	-1.16	1.40
Private Real Estate – GEP	2.49	11.06	-0.04	0.59
Public Real Estate – UCRP	5.77	28.16	-0.54	-1.69
Public Real Estate – GEP	5.86	28.18	-0.45	-1.67

Real Estate Highlights Period Ended December 31, 2012

- The UCRP real estate portfolio outperformed the benchmark by 1.4% for the year, given the stronger than benchmark appreciation gains in the open-end fund portfolio, the successful sale of a large value add asset and a development asset from the separate account portfolio.
- Three additional acquisitions, all in California, were made for the separate account portfolio during the quarter – one value-add office property, one opportunistic office property, and one stable office property, – with an aggregate net value of $124 million (which is not yet reflected in the portfolio net asset value). In addition, a purchase and sale agreement was entered for one more office property, and the planned sale of an industrial property closed during the second fiscal quarter, with total proceeds of $20 million. In total during the 2012 calendar year, $281 million in equity was deployed to the acquisition of 11 assets for the separate accounts.
- During the quarter, a $35 million investment was made to an open-end industrial fund. In total during the 2012, $125 million in equity was committed to three commingled funds.

Real Estate Portfolio Review

- The **Private Real Estate Portfolio** continued its steady recovery during the quarter, with UCRP gaining 1.37% and GEP adding 2.49%. The UCRP portfolio fell short of the benchmark by -1.16%, while the GEP portfolio kept pace, with slight underperformance of -0.04%.
- Core investments continued to report steady income and appreciation, outperforming the benchmark by 1.9% during the quarter; they were among the biggest contributors to total return during the period. This was driven by solid returns from the open-end commingled fund portfolio, as well as appreciation gains recognized in the core separate account portfolio as assets were revalued after external appraisals were conducted.
- In contrast, value added and opportunistic investments lagged the benchmark in terms income and appreciation return; this is not unexpected while assets are in the execution phase of their business plan.
- The Separate Account composite, taken alone, underperformed the benchmark, and was largely impacted by the recognition of a success fee in relation to the profitable sale of one large asset.
- In general, returns for Private Real Estate continued to trend positive, but to a more moderate degree. There remains a more positive outlook than a year ago, but valuation gains moderated as valuation assumptions and the economic outlook stabilized.

- The **Public Real Estate portfolio** returned 5.77 % in UCRP and 5.86% in GEP during the quarter, underperforming the policy benchmark by 0.54% and 0.45%, respectively. For the year, both the UCRP and GEP returned 28.2% as global REIT markets rallied, though this performance was shy of the benchmark by 1.7%.
- An allocation to a passive manager comprises the bulk of the Public Real Estate portfolio. The passive portfolio comprises developed market securities only, while the policy benchmark is inclusive of emerging markets companies as well. The emerging markets component of the index returned 42.4% in 2012, outperforming developed markets and causing the portfolio's underperformance relative to the benchmark.
- In the active portfolio, stock selection was slightly positive during the second fiscal quarter, with relative strength in Hong Kong, China and Western Europe holdings. Regional allocation was positive, with an overweight to Singapore, which outperformed other regions during the quarter. At quarter end, the portfolio manager rebalanced to shift Singapore to an underweight, and used the cash proceeds to move from an underweight to neutral within the U.S. and Japan, with a strong overweight exposure to Japanese developers. By property type, the portfolio is overweight to office, retail, and hotels.
- For the year, stock selection in the active portfolio was mixed, with strong results in Canada, Western Europe, Japan, and Singapore, but weakness elsewhere. Regional allocation was positive, with an overweight to Singapore and an underweight to Canada and the U.S., which underperformed.

Looking Forward

- The existing portfolio is constructed with the flexibility to reposition or adjust the strategy in changing market conditions. More than 50% of UC's investment commitments are to structures that provide some degree of liquidity (i.e. separate accounts, open-end funds, and REITs).
- There is currently $500 million in unfunded commitments in the Private Real Estate portfolio (including separate accounts and commingled funds), available to invest into lower pricing in a post-correction market.
- Committed capital continues to be deployed by the separate account managers, who report an increasingly robust pipeline of opportunities. Additional separate account managers and strategies are under consideration for addition to the portfolio.
- Opportunities presented by dislocation and distress in the credit markets are under review, with interest especially in debt-to-own strategies, certain types of loan origination, as well as acquisition and servicing of large loan portfolios.
- Also of interest are strategies that capitalize on the bank distress within Europe, and Asian and Latin American funds well-positioned to benefit from growth and development in those regions.