

ENDOWMENT FUND ANNUAL REPORT

JUNE 30, 2005



*Maine's
Public
Universities*

UNIVERSITY OF MAINE SYSTEM

ANNUAL ENDOWMENT REPORT

University of Maine System Endowment

The Endowment funds of the University of Maine System are subject to the restrictions of gift instruments requiring that the principal be invested and current expenditures be funded from related income and appreciation.

Management

The following persons meet quarterly to provide oversight of the Endowment and to make portfolio management and investment management decisions for the fund:

- Board of Trustees Investment Committee
- Investment Consultant – New England Pension Consultants – Cambridge, MA
- Joanne Yestramski, - CFO & Treasurer, UMS
- Michael Soucy - Assistant Treasurer, UMS

Governing Policy

A formal investment policy governs the Endowment Investment Process. The Investment Policy details:

- Total return and risk objectives
- Spending Policy
- Permitted and Excluded Investments
- Asset Allocation guidelines with defined targets and permissible ranges
- Evaluation benchmarks by asset class and for the portfolio as a whole
- Risk and Diversification requirements by asset class
- Use of Derivatives
- Performance Standards and Evaluation
- Responsibilities of all parties concerned

The Investment Policy established by the Investment Committee targets a long run minimum return objective of 9.0%. The spending policy for FY06 has been set at 5.0%.

Performance

The Endowment did very well in FY05, with a net of fees return of 10.1%. This return represents appreciation and income received from the investments of over \$9.1 million. This performance ranks the Endowment in the top 20% of all Endowment funds for the trailing one year period as of 6/30/2005. Active management added considerable value to the portfolio, outperforming passive benchmarks by 90 basis points (.9%). For the sake of comparison, the S&P 500 returned 6.3% over this same period, and the Lehman Brothers Aggregate Bond Index returned 6.8%.

Diversification

The Endowment fund is well diversified by style and asset class, as well as internationally. The fund is diversified amongst 11 different asset classes and is managed by 10 different investment managers. The size of the fund permits fuller diversification (which enhances risk adjusted returns) as well as access to attractive asset classes/managers that smaller funds don't have access to.

Additionally, larger investments benefit from reduced investment manager, consultant and custodial fees.

As of 6/30/05, about 47% (\$47.4 million) of the fund was invested in **Domestic Equities**, which is further segmented into Passively Managed, Large Cap, and Small/MidCap investment categories. Within the Large Cap and Small/MidCap categories, the investments are further diversified into growth and value styles.

Roughly 15% of the fund is invested in **international stocks**, to provide diversification benefits and to pursue attractive equity investments worldwide.

Approximately 24% of the assets were invested in **fixed income** strategies. Roughly 18% was in a Global Multi-Strategy Bond fund (invests in the most attractive fixed income sectors worldwide), and 6% was in High-Yield bonds (tactical position to benefit from high income payments and improving economy).

About 15% of the fund was invested in Alternative Strategies, with 7% in Market Neutral investments (to improve stability of return), and 8% in a Global Absolute Return strategy (which seeks to invest in those asset classes worldwide which offer the best relative value).

The following information is provided as of June 30, 2004 for the total endowment fund for FY05.

Total Endowment at Market Value - June 30, 2005	\$100,688,916
Total Endowment at Market Value - June 30, 2004	\$92,541,856

The FY05 increase of **\$8,147,060** is comprised of:

Inflows:

Gifts (UMS and UMS affiliated organizations)	3,149,922
Charitable Gift Annuities	13,320
Investment Returns:	
Income	3,467,347
Net Appreciation	6,571,450
Fees/Expenses	<u>(899,040)</u>
	9,139,757

Outflows:

5.25% Spending for Scholarships & Operations	(4,201,684)
Transfers	<u>45,845</u>
	(4,155,839)

Net of Inflows and Outflows: \$8,147,060

Attachment I reports the total returns for the Pooled Endowment fund on a net of fees basis and the fund's growth for the past 5 years, as well as the asset allocation for the fiscal years ended June 30, 2004-2005.

UNIVERSITY OF MAINE SYSTEM
 POOLED ENDOWMENT FUND
 AS OF JUNE 30, 2005

The following tables present the System's Pooled Endowment Fund asset allocation for the fiscal years ended June 30, 2004 and June 30, 2005, the growth of the Endowment, and the total return figures net of fees since FY01.

June 30, 2004

Total Pooled Endowment: \$92,542 (000's)	
	% of Total
Domestic Equities	\$ 44,220 44%
Int'l Equities	11,480 11%
Fixed Income	16,811 17%
High Yield Bond	5,742 6%
Market Neutral	7,585 8%
Global Absol.Return	6,579 7%
Cash	125 0%
Total	\$ 92,542 92%

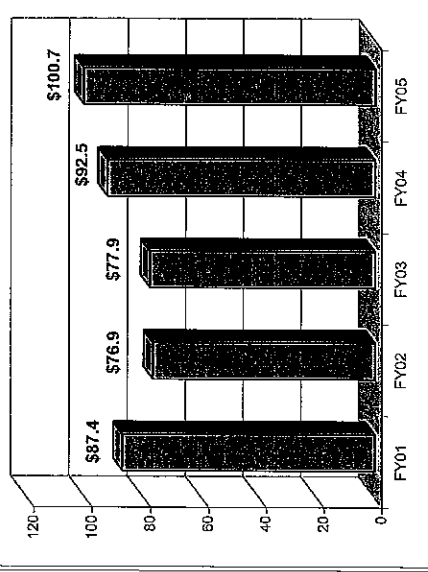
June 30, 2005

Total Pooled Endowment: \$100,689 (000's)	
	% of Total
Domestic Equities	\$ 47,378 47%
Int'l Equities	15,020 15%
Fixed Income	17,617 18%
High Yield Bond	5,866 6%
Market Neutral	6,945 7%
Global Absol.Return	7,721 8%
Cash	143 0%
Total	\$ 100,689 100%

Endowment Fund Total Returns (Net of Fees)



Fiscal Year-End Endowment Fund Market Values (\$ in millions)



MUS-08/30/05 ES0(12)

Note - The ending Endowment values reported by NEPC on flash reports or otherwise will not reconcile with the Roll-Up calculation performed by Accounting, due to the extra cash that comes in that is retained to make Endowment spending payments to the campuses. The roll-up contains this cash amount; the investment managers do not have this money. Therefore, increase the cash amount reported by NEPC by the difference in the total Endowment values.

Fiscal Year	Total Return
FY98	0.198
FY99	0.126
FY00	0.073
FY01	(0.079)
FY02	(0.091)
FY03	0.048
FY04	0.192
FY05	0.101

These numbers were obtained from the 07 Endowment spreadsheet. See total fund tab.

Fiscal Year	Endowment Fund Market Value (\$ in millions)
FY99	92.4
FY00	96.9
FY01	87.4
FY02	76.9
FY03	77.9
FY04	92.5
FY05	100.7