This was a landmark year for Miami in which the total of the investment pools broke the $500 million threshold.

FISCAL YEAR 2006 HIGHLIGHTS
Miami University and Miami University Foundation’s investment portfolios performed very well for the fiscal year ended June 30, 2006, with average returns of more than 13 percent for the endowment and foundation pools, and exceeding 8 percent for the more conservatively managed non-endowment pool. These strong returns improved upon a solid 2005, in which the portfolios earned 10 percent and 5 percent returns, respectively.

“This was a landmark year for Miami in which the total of the investment pools broke the $500 million threshold,” said Beverly Thomas, associate vice president for finance and associate treasurer. This asset growth was made possible by a 15 percent jump in the two endowment pools, which climbed to a combined total of $315 million. Together the endowment and foundation pools distributed $13.6 million in operating support for the university’s 2006 fiscal year.

INVESTMENT POOLS
As of June 30, 2006, investments held by Miami University and the Miami University Foundation exceeded $509 million, up from $477 million at the previous year end. These assets are allocated among several investment pools:

<table>
<thead>
<tr>
<th>Pool</th>
<th>Type of Funds</th>
<th>Invested as of June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>University non-endowment</td>
<td>Working capital and cash reserves to support operating activities</td>
<td>$172,732,000</td>
</tr>
<tr>
<td>University endowment</td>
<td>Funds donated to the university to establish endowments in perpetuity</td>
<td>$132,436,000</td>
</tr>
<tr>
<td>Foundation</td>
<td>Funds donated to the foundation; most are endowed in perpetuity</td>
<td>$182,952,000</td>
</tr>
<tr>
<td>Trusts, annuities, and separately invested assets</td>
<td>Gifts managed independently of the pooled funds</td>
<td>$ 21,486,000</td>
</tr>
<tr>
<td><strong>Total Investments</strong></td>
<td></td>
<td><strong>$509,606,000</strong></td>
</tr>
</tbody>
</table>

The university non-endowment pool holds the working capital and cash reserves that fund the university’s operating activities. Its balance fluctuates during the course of a year based on the university’s cash flow cycle of receipts and expenditures.

The university endowment pool invests endowed gifts from donors to the university, while the foundation pool invests gifts received by the foundation. Both pools operate under the same overall investment philosophy: as endowment funds they are invested in perpetuity to provide benefits to today’s students as well as to the many generations of Miami students yet to come. Miami invests the funds with the confidence that economic cycles will rise and fall but that a diversified portfolio will provide the long-term growth necessary to preserve the value of the endowments across the generations. The investment policies governing these two pools recognize that the portfolios can tolerate year-to-year fluctuations in return because of their infinite time horizon, and they look beyond short-term fluctuations toward an investment philosophy that provides the best total return over very long time periods.

The university and foundation also hold assets given by donors in the form of trusts, annuities, insurance policies, and similar assets. These funds are separately managed in accordance with the donors’ instructions.
**Asset Allocation**

One of the most important aspects of constructing an investment portfolio is determining the allocation of investments among a variety of asset classes. Miami employs an independent consultant to assist in this judgment. The consultant uses statistical techniques to model various combinations of asset classes under different economic scenarios. These models are evaluated by Miami to determine a strategic asset allocation based on the investment objectives and risk tolerance of each pool.

As of June 30, 2006, the investment pools had the following asset allocations:

**Miami University Non-Endowment Pool**

- Domestic Equities: 10%
- International Equities: 10%
- Alternative Equities: 16%
- Market Hedged: 22%
- Fixed Income: 27%

**Miami University Endowment Pool**

- Domestic Equities: 40%
- International Equities: 19%
- Alternative Equities: 10%
- Market Hedged: 17%
- Cash: 2%

**Miami University Foundation Pool**

- Domestic Equities: 44%
- International Equities: 19%
- Alternative Equities: 10%
- Market Hedged: 17%
- Cash: 5%

Within the non-endowment pool, two to six months of average cash needs are invested in short-term cash equivalents, an additional two to six months of average cash needs are invested in short-term and intermediate-term fixed income investments, and the remainder is invested in longer maturity bonds, absolute return hedged strategies, and equity investments. Because of possible cash flow needs and the low risk tolerance of this pool, more than half of the pool is invested in easily liquidated holdings.

The university and foundation employ external managers with expertise in each asset class to make specific investment decisions. Diversification among a wide range of asset classes is a key strategy in minimizing risk in these portfolios. In total, the university and foundation employ 18 external managers (several with multiple assignments). During the year, new commitments were made to two private equity managers, two hedge fund managers, and two private real estate managers. The independent consultant is engaged to supplement the efforts of Miami staff in monitoring the activities and performance of these managers.

The asset allocation of the endowment and foundation pools has evolved significantly over time, as shown on the accompanying graph. In 1991, the combined university endowment and foundation portfolios were 69 percent in domestic public equities, with no international equity or hedge fund exposure. By 2006, domestic public equity has been reduced to 43 percent, while international equity represented 19 percent and hedge funds were 17 percent of the portfolio. By reducing the portfolio’s exposure to the volatile domestic public equity markets, this shift in the allocation has added greater stability to the portfolios while also providing a meaningful boost to the rate of return.
INVESTMENT RETURNS

The university non-endowment pool earned 8.28 percent for the fiscal year ended June 30, 2006, which is more than one percentage point ahead of its blended benchmark return. Performance for the trailing three years was 6.73 percent. With interest rates at historically low levels, most of the portfolio returns in the past three years have come from the fund’s equity, real estate, and absolute return investments. The university changed its non-endowment investment policy in 2002 to move away from a bond-only portfolio toward greater diversification. This policy change has added more than four percentage points in annualized returns during the four-year period.

The university endowment pool earned 13.16 percent for the fiscal year and 14.70 percent annualized for the trailing three years, while the foundation pool earned 13.83 percent for the fiscal year and 15.10 percent for the trailing three years. These returns exceeded both pools’ policy return targets of 9 percent over complete economic cycles and have now done so in each of the last three years. The following graph shows the combined annual returns for the two pools since 1997 in comparison to the 9 percent policy target (red line).

The university endowment and foundation investment returns are benchmarked against the returns of a blend of published indices. The one-year and three-year performance of both pools exceeded the blended index benchmarks (approximately 12.88 percent and 14.4 percent, respectively), primarily due to broad-based strong returns in most of the portfolios’ asset classes.

Another measure of investment performance is benchmarking against the performance of other institutions. Miami participates in two large surveys of educational institutions, the NACUBO (National Association of College and University Business Officers) Endowment Survey and the Commonfund Benchmarks Study. Both surveys encompass more than 700 institutions. NACUBO gathers data primarily on the details of investment performance and asset allocation, while Commonfund focuses more on endowment policies and practices. Miami University and foundation ranked in the top half of both universes for the one-year, three-year, and 10-year periods in the most recent surveys (for the year ended June 30, 2005).

PROGRAM SUPPORT

Endowments provide a lasting legacy for Miami because their principal is invested in perpetuity, and an annual allocation of income is distributed to support a variety of activities of the university. The spending policies of the university and foundation are intended to achieve a balance between the need to preserve the purchasing power of the endowment principal in perpetuity and the need to maximize current distribution of endowment earnings. Fulfilling these dual objectives is often referred to as achieving “intergenerational equity,” in which no generation of college students is advantaged or disadvantaged in relation to other generations.

The formula under which spending distributions are calculated is a blend of two elements: an inflation element (70 percent of the formula) that increases the prior year’s distribution by the rate of inflation, and a market element (30 percent of the formula) that ties the distribution to the market value of the investments. This formula was adopted in fiscal year 2004 and is intended to reduce volatility caused by “bull” and “bear” market conditions, while maintaining intergenerational equity and preserving the purchasing power of the endowed principal.
The accompanying two charts show how dramatically the spending distributions have grown over the years and the types of programs supported by the 2006 distribution. The combined distribution for 2006 was more than $13.6 million. This amount is triple the $4.8 million distributed a decade earlier and has provided an important source of funding to help offset the decline in state assistance.

A wonderful example of how the endowment directly supports Miami students was announced just after the fiscal year ended. In his inaugural State of the University Address to faculty and staff, President David Hodge launched the Miami Access Initiative, which will benefit new Oxford campus students entering in the fall of 2007. This program, funded largely through a major bequest to the endowment from the late Lois Klawon ’39, will provide tuition and fees for up to four years to Ohio students with family annual income less than $35,000. It is anticipated that this program will initially benefit 125-150 new students annually, helping to make Miami both stronger and more accessible to students of all economic backgrounds.

**GROWTH IN ENDOWMENTS**

We are proud that the endowments of the university and foundation have grown to a combined total of $315 million. The dramatic growth since the 1980s is the product of both investment returns and fund-raising success. In 2005 Miami kicked off its fund-raising campaign *For Love and Honor*. As of August 2006, the campaign had raised $234 million, of which $151 million is pledged to the endowment. We are deeply grateful to the loyal and generous donors who are contributing to the long-term future of the university through its endowments.

Despite this impressive growth, however, Miami ranked only 76th among 230 public institutions in the 2005 NACUBO Endowment Survey in terms of endowment assets per student and would have ranked in the bottom quartile if compared to private institutions. As a public institution, Miami’s endowment of about $14,000 per student trails many of its peers, some of which have endowments in excess of $100,000 per student. Endowment size has a direct impact on an institution’s ability to provide student scholarships, support faculty initiatives, and fund institutional priorities. We continue to work diligently toward achieving an endowment that will rival those of our peers.

President Hodge stated in his State of the University Address, "A university that has existed for nearly 200 years must be doing something right! What we need to do, then, is to intensify those qualities that have made Miami both distinctive and distinguished, in other words to ‘make Miami more Miami,’ taking the best of Miami and making it better.” Miami is proud of its standing among the best public universities in the nation. The Miami University endowment and Miami University Foundation will continue to play a vital role in the mission that lies ahead.