“Upon the subject of education...I can only say that I view it as the most important subject which we as a people can be engaged in.”

ABRAHAM LINCOLN
THANK YOU FOR YOUR GENEROSITY

As Chair of the Board of Directors and CEO/President of the University of Illinois Foundation, we want to thank you for all you do for the University of Illinois. If you joined us for our Annual Meeting on October 7, we appreciate your attendance. Whether you were able to join us or not, we hope you will mark October 13, 2017 on your calendar and plan to attend next year.

It is our pleasure to share with you this year’s Foundation Annual and Endowment Report, which illustrates a number of examples of the impact of your philanthropy. This report provides an overview of the philanthropic activities and investment fund performance during fiscal year 2016 (July 1, 2015–June 30, 2016). While the 2016 calendar year is coming to a close, the spirit of Thanksgiving remains with us. Thank you for being a partner in philanthropy and for your generous investments in the University of Illinois. We are fortunate to have a broad community of donors who believe in our mission and our capacity to deliver excellence like few other public universities can.

For nearly 150 years, the University of Illinois has been a great investment. For the past 81 years, the UI Foundation has been securing and managing private gifts from generous donors like you, who have a shared belief in the value of the University and its impact on the world. Thank you for your continued support, and for being part of another tremendous year where philanthropy helped move the University forward with $286.2 million in new gifts and commitments.

The University of Illinois is transforming lives. In the pages that follow you will learn about how the power of philanthropy at the University of Illinois is making a difference at home and around the globe. Thank you for being a member of the University of Illinois family, and thank you for investing your time, skills, and resources across the University of Illinois System.

We hope you find the 2016 Annual and Endowment Report informative, enlightening, and inspiring. Many thanks again for your generous support of the University of Illinois and the University of Illinois Foundation.

Sincerely,

GREGORY B. LYKINS
Chair, Board of Directors
University of Illinois Foundation

JAMES H. MOORE, JR.
President/CEO
University of Illinois Foundation
“Thank you for being a partner in philanthropy and for your generous investments in the University of Illinois.”

GREGORY B. LYKINS, CHAIR, UIF BOARD
JAMES H. MOORE, JR., PRESIDENT/CEO, UIF
ABOUT THE FOUNDATION

Established in 1935, the University of Illinois Foundation is an independent nonprofit corporation responsible for raising and administering private gifts that advance the University and its excellence in teaching, research, public service, and economic development across the three universities.

MISSION STATEMENT

The University of Illinois Foundation is a nonprofit corporation responsible for encouraging and administering private gifts made to further the University’s mission. Although the Foundation is a separate legal entity from the University of Illinois, the Foundation’s sole reason for existence is to serve the University.
The Foundation’s dedicated staff is part of a comprehensive University advancement team of more than 400 talented professionals and visionary campus leaders. As the primary repository of private support to the University of Illinois, the University of Illinois Foundation is committed to best practices, continuous improvement, quality service, upholding our fiduciary duties, and—most importantly—honoring donor intent.
“Our standing as a go-to destination for students and discovery is firmly rooted in generations of people like all of you who have stepped up to help create a University System that is synonymous with excellence. The difference between world-class and run-of-the-pack is philanthropy. Our universities are the engines that drive progress and prosperity, and our donors’ generosity provides the fuel to feed it.”

TIMOTHY L. KILLEEN
President, University of Illinois
ANNUAL FOUNDATION BUSINESS MEETING

Almost 400 Foundation Members, alumni, faculty, and friends of the University System joined us in October 2016 for the 81st Annual Foundation Business Meeting. Foundation and University leadership shared financial information and discussed the impact of giving, focusing on the importance of philanthropy in the new funding model for higher education. Foundation Members elected five new members to the Board of Directors, and President Killeen moderated a panel of students who shared their perspectives, experiences, and challenges.
ANNUAL FOUNDATION MEETING LUNCHEON

The Annual Meeting luncheon displayed philanthropy in person as faculty took the stage. The chancellors engaged exceptional members of their faculty in conversations about the ways in which giving has impacted their lives and careers. Each faculty member shared personal stories of how philanthropy allowed them to support their students, pursue groundbreaking research, and improve the world.

Top Row: Robert J. Jones, Chancellor, University of Illinois at Urbana-Champaign
Tami Bond, Nathan M. Newmark Distinguished Professor in Civil and Environmental Engineering, John D. and Catherine T. MacArthur Fellow, College of Engineering, University of Illinois at Urbana-Champaign

Middle Row: Timothy L. Killeen, President, University of Illinois
Michael D. Amiridis, Chancellor, University of Illinois at Chicago
Jose Oberholzer, MD, Chief, Transplant Surgery; Professor of Surgery, Bioengineering and Endocrinology; Director, Cell and Pancreas Transplantation; C & B Frese and G. Moss Professor of Surgery, University of Illinois at Chicago

Bottom Row: Susan J. Koch, Chancellor, University of Illinois Springfield
Marc Klingshirn, PhD, Director of CAP Honors and Associate Professor, Chemistry, University of Illinois Springfield
At the University of Illinois at Springfield, extraordinary faculty and staff invest daily in the success of students, preparing them for productive lives as professionals, leaders and members of their communities. As UIS continues to grow in reputation, visibility and enrollment, your generous support is making a profound difference by making education more affordable and by enabling us to provide the opportunities and experiences that maximize our students’ educational transformation.

SUSAN J. KOCH
Chancellor, University of Illinois Springfield

“Our path forward will always be paved with a gracious spirit, a willingness to support bold ideas and the unyielding belief that an education is the most powerful force on the planet. Your gifts are literally investments in people – in the students and the faculty who continually force the world to redefine the word ‘impossible.’”

ROBERT J. JONES
Chancellor, University of Illinois at Urbana-Champaign

“The University of Illinois at Chicago is the city’s public research engine and an incubator for innovation. Through our teaching we foster an informed citizenry and promote community engagement. Through our research we break down barriers for a more sustainable future. Through our health science colleges and our hospital and clinics we promote healthier lives. Through our scholarship and creative achievements in the humanities, we enrich our culture. And your support and investment makes it all happen!”

MICHAEL D. AMIRIDIS
Chancellor, University of Illinois at Chicago

“At the University of Illinois at Springfield, extraordinary faculty and staff invest daily in the success of students, preparing them for productive lives as professionals, leaders and members of their communities. As UIS continues to grow in reputation, visibility and enrollment, your generous support is making a profound difference by making education more affordable and by enabling us to provide the opportunities and experiences that maximize our students’ educational transformation.”

SUSAN J. KOCH
Chancellor, University of Illinois Springfield
$286,186,972

Sources

Alumni: 30.6%
Friends: 12%
Foundations: 13.8%
Corporations: 31.5%
Other: 12.1%

Distribution

$232.3M
- Urbana-Champaign

$45.4M
- Chicago

$4.3M
- Springfield

$4.2M
- Other
$286.2M

- **RESEARCH** 17%
- **STUDENT SUPPORT** 17%
- **FACILITIES** 10%
- **ACADEMIC PROGRAMS** 9%
- **FACULTY SUPPORT** 5%
- **PUBLIC SERVICE** 4%
- **OTHER** 1%
- **UNRESTRICTED** 37%

*These gifts are restricted to a campus, college, department, or program, but unrestricted in their use at the discretion of the dean or unit head.*
$49.4M IMPACT
Research capabilities are expanding at the University of Illinois at Urbana-Champaign where the College of Engineering is partnering with IBM to create a new Center for Cognitive Computing Systems Research (C3SR). The Center will help research extend the boundaries of cognitive computing by developing new systems to receive and analyze large amounts of data, allowing students and faculty to answer the world’s most pressing questions.
$47.4M IMPACT ON
STUDENT SUPPORT

SEELER’S PHILANTHROPY AND TEACHING TRANSFORMS STUDENTS’ LIVES

Longtime College of Medicine faculty member, Ruth Seeler, is transforming the lives of students at the University of Illinois at Chicago. Ruth established the Ruth Andrea Seeler, MD, Scholarship Endowment fund, which will provide scholarships for fourth-year medical students who choose to enter primary care fields. Not only will a new generation of doctors benefit from Ruth’s generosity, but so will the many communities they’ll serve.
$27.3M IMPACT
University of Illinois Springfield alumnus Dick Osborne, MBA ’73, and his wife Char are supporting a construction project that will enhance the student experience and feeling of community on campus. Their $1.5 million commitment to build a new, first-class student union will allow students to connect with their classmates, create lifelong relationships with their campus, and come together for student leadership development and major public events and activities.
$15.2M IMPACT ON
RETZKYS' GIFT WILL CREATE UIC'S FIRST DEANSHIP

Herbert Retzky, '46 PHARM, and his wife Carol, are making a difference for faculty at the University of Illinois at Chicago's College of Pharmacy. Their $5 million commitment to fund the Herbert and Carol Retzky Deanship will create UIC’s first Deanship and will help the college continue its rise in the rankings, while building awareness about the crucial role that pharmacists play in our society.
$25.9M Impact on Academic Programs
Alumnus Thomas Siebel, ’75 LAS, MBA ’83, MS ’85 ENG, HON ’85 ENG, and his wife Stacey, are impacting academic programs by enhancing design thinking at the University of Illinois at Urbana-Champaign. Their recently announced gift of $25 million will establish the Siebel Center for Design. A new two-story, 60,000 square foot, state-of-the-art building will be a campus-wide hub for student-focused design and learning for both undergraduate and graduate students in multiple colleges.

Siebel Center for Design Rendering, ©Bohlin Cywinski Jackson
$10.6M IMPACT ON PUBLIC SERVICE
Public service takes center stage at the University of Illinois Springfield, where a commitment to the community is introducing thousands of area children to the experience of attending live professional performing arts through the Staley Class Acts Program. Fueled by donors Liz Staley and her husband Bob, Class Acts is in its 30th year and brings K-12 students from Central Illinois to performances at the Sangamon Auditorium. Liz Staley passed away this year, but her legacy continues.
GIFT PLANNING
Many donors choose to leave a lasting legacy through a variety of gift planning instruments executed with the University of Illinois Foundation to benefit their desired campus, unit, or interest.

FY 2016 NEW COMMITMENTS

<table>
<thead>
<tr>
<th>Commitment</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>REVOCABLE ESTATE PLAN COMMITMENTS</td>
<td>$54,360,932</td>
</tr>
<tr>
<td>CHARITABLE REMAINDER TRUSTS*</td>
<td>$2,304,100</td>
</tr>
<tr>
<td>CHARITABLE GIFT ANNUITIES*</td>
<td>$1,534,900</td>
</tr>
</tbody>
</table>

*Irrevocable gift arrangements administered by UIF

NEW REVOCABLE AND IRREVOCABLE COMMITMENTS IN FY 16

$58.2M
The premier donor recognition program of the University of Illinois Foundation, the President’s Council recognizes individuals who make significant philanthropic investments in the University totaling $25,000 or more.

Since 1964, more than 16,300 alumni and friends have been welcomed into the membership based on cumulative lifetime gifts and commitments (outright, pledged, and deferred) across all three universities.
Of all forms of private giving, endowments are perhaps the most influential investments in higher education—providing both immediate and continuing impact on the University. The permanent financial support created by endowed funds builds self-renewing, living legacies that span generations.

A strong endowment also increases the University’s ability to forecast one of its core revenue streams with greater predictability. The Foundation manages many endowment funds that collectively produce earnings used to support designated University programs, faculty, and students across our three universities in Springfield, Chicago, and Urbana-Champaign.
THE FOUNDATION ACTIVE ENDOWMENT REACHED

$1.55 BILLION

FIVE THOUSAND FOUR HUNDRED NINETY-THREE ENDOWED FUNDS

OVER

$65M

IN GIFT DOLLARS ADDED
TO THE UIF ENDOWMENT POOL

OVER

$51M

DISTRIBUTED
TO THE UNIVERSITY

5.5%

14.9%

1.0%

78.6%

$1.22B

URBANA-CHAMPAIGN

$231.4M

CHICAGO

$14.8M

SPRINGFIELD

$85.3M

OTHER

THE FOUNDATION ENDOWMENT POOL REACHED

$1.4 BILLION

(93.2% OF THE TOTAL FOUNDATION ACTIVE ENDOWMENT)
Ellen Ellison joined the Foundation in January 2013 to build and lead its first independent investment team in Chicago. While managing the Foundation’s $1.4 billion active endowment pool, she monitors capital markets and economic forecasts and provides guidance on investment-related matters including asset allocation decisions, portfolio management, and best practices. Ellen also works closely with the Investment Policy Committee of the Foundation’s board.

In 2010, Ellen was named one of the 10 Best University Endowment Managers by Business Insider. She has more than 30 years of experience in investment and endowment management—having served most recently as the executive director of investments at the University of Miami. Previously, she served as the chief investment officer at J.I.K. Investment Services, Inc., a family office in Miami, Florida, and as a senior vice president at Fiduciary Trust Company International in both New York and Miami. Ellen is a registered Charted Financial Analyst (CFA) and received a bachelor’s degree in French literature from Mount Holyoke College as well as an MBA from Columbia University Business School.
I. MARKET & ECONOMIC REVIEW

The U.S. was a safe haven for global investors during a tumultuous and uncertain year. Overall, risky asset classes struggled, but U.S. equities appreciated 4.0%, faring much better than international equities.

U.S. stocks, bonds, and currency all benefited from turmoil abroad as international markets wrestled with uncertain economic growth and the new normal of negative interest rates. Despite this relative success, U.S. stocks experienced two major dips in the past 12 months: the S&P 500 declined by 13% in the third quarter of 2015, and 15% in the first quarter of 2016. Although these moves do not indicate a bear market, the psychological damage was significant. Investors have been conditioned to “buy on dips,” but these violent episodes send a clear message: proceed with caution!

Within developed and major international equity markets, the U.K. ended the year at the bottom of the list (-12.1%) for dollar-based investors such as the University of Illinois Foundation. This is not surprising given the sharp drop in the British pound to a thirty-year low following the “Brexit” vote June 23rd on the future of that country’s membership within the European Union. Japan, plagued by its own growth fits and starts (-8.9%), and the rest of Europe, despite loads of innovative monetary stimulus (-10.8%), were not far behind the U.K. equities.

Emerging market equities also declined significantly (-11.7%) during the past year despite an excellent run by Brazil and Colombia that began on January 1, 2016. China dominated the headlines in the summer of 2015 when a small but poorly-communicated yuan devaluation caused global panic on the true state of Chinese economic growth. Chinese equities—in U.S. dollar terms—declined 23.2%.

While rising wages support consumption and housing growth in a mature economy, the only way for companies to continue to grow earnings—as wages increase—is to increase productivity. Labor productivity has been far lower in the last decade (+1.3%) if compared to the period from 1995–2005 when it grew 2.8%. Experts cite a number of reasons for this trend including job mismatch—when people made sub-optimal career choices just to find work—coming out of the financial crisis of 2008. Companies also have been cautious about committing to large, long-term capital spending projects due to global uncertainties, opting instead to return excess cash to shareholders in the form of dividends or share buybacks. Another factor for decreased productivity may be the Silicon Valley explanation that outdated government statistics are not sophisticated enough to measure the new digital and ‘gig’ economy. We believe productivity will eventually kick in with higher long term, capital spending and as a direct result of more robust wage growth. For eight years, we have experienced a bad hangover from the deep job cuts and corporate risk aversion that came in the aftermath of the global financial crisis. Deleveraging income going forward: the S&P 500 is valued at 20 times earnings; the bull market is now in its seventh year; and U.S. companies are in a “profits recession” with second quarter earnings declining for the fifth consecutive time. Of additional concern is that U.S. wages are now growing faster than inflation. In the past fiscal year, U.S. wages grew 2.5% as compared to 1.0% inflation. This implies decreased productivity and a unit labor cost increase of 1.5%.

Despite the U.S.’s obvious appeal to both domestic and international investors, it is challenging for us to be enthusiastic about returns for U.S. equities or fixed income going forward: the S&P 500 is valued at 20 times earnings; the bull market is now in its seventh year; and U.S. companies are in a “profits recession” with second quarter earnings declining for the fifth consecutive time. Of additional concern is that U.S. wages are now growing faster than inflation. In the past fiscal year, U.S. wages grew 2.5% as compared to 1.0% inflation. This implies decreased productivity and a unit labor cost increase of 1.5%.
is painful and, in this instance, has taken its time working through the economy.

The timing of the U.K. referendum unfortunately came when most of the developed and emerging market world was gently improving or at least stabilized. Confidence in the European economy was improving and business activity had firmed leading up to the vote. The majority of the developed world (including the U.S.) was showing stable to improving leading economic indicators after a recent soft patch this past spring. Emerging markets and their economies were also improving. The Brexit vote stopped a lot of that momentum and, in its aftermath, global growth has since been ratcheted down by 0.50%.

The chart below indicates that with the exception of some U.S. sectors (Treasuries, Real Estate Investment Trusts, stocks, the dollar) and gold, very few asset classes did well last year as macroeconomic uncertainty coupled with hyper monetary policy drove investors to pay up—at any valuation—for real or perceived safety.

Investing against this backdrop of strong macroeconomic (versus fundamental) influence where money flows move rapidly around the globe in search of yield has been confounding for most market participants including those who attempt to predict the future in global macro funds. We do not make such claims but do find the current environment to be especially challenging.

<table>
<thead>
<tr>
<th>GLOBAL ASSET CLASS PERFORMANCE: FY 2016</th>
</tr>
</thead>
</table>


*Based on preliminary data.
“Consistent with our long-term strategy, we rebalanced the endowment asset allocation to target asset classes with attractive projected returns with an acceptable level of risk, which should position the portfolio to take full advantage of the expected rebound.”

MARK PYTOSH, ’86 LAS, CHAIR, INVESTMENT POLICY COMMITTEE
WE HAVE IDENTIFIED THREE MAJOR THEMES FROM LAST YEAR:

THEME 1

Monetary policy’s solo reign has ended: it is time for fiscal policy to play a larger role. Extreme monetary policies like zero interest rates have not yet encouraged economic activity and more risk-taking. They have driven risk-taking in the asset/financial markets instead of in the real economy.

The chart below illustrates that since 2014 when negative interest rates were rare, there are now $9.9 trillion in bonds, or 38% of the Barclays Global Aggregate Bond index that are negative yielding. More astounding is the fact that only $2.0 trillion (8%) of bonds yield above 2%. The majority of these are in the U.S. making our bond markets very attractive on a relative basis. U.S. yields should be higher given the health of our economy.

Last year, we expected normalized interest rates in the U.S. during the course of 2016 and the Fed suggested it would like to raise base rates four times in the current calendar year. So far, it has only raised the Fed Funds rate once in December, 2015. Furthermore, at the beginning of 2016, the European Central Bank and Bank of Japan moved in the opposite direction and started experimenting with negative interest rates in an attempt to stimulate growth, lending, and consumer spending. Although it is too soon to draw any firm conclusion regarding the effectiveness of this policy, markets have not reacted well so far. Crossing to the other side of zero has already had unintended consequences in Japan (the Japanese yen should have weakened but instead it appreciated dramatically as a safe haven currency), and elsewhere and returns have been worse in those parts of the world with negative interest rate policies.

We have exhausted the effectiveness of monetary policy. Persistent low to negative interest rates hurt banks and savers; damage business and consumer confidence; increase demand for gold and hard assets; make investment decisions more difficult; and eliminate the normal incentives for business to invest in capital. When the cost of capital is zero, how can we use any traditional valuation tools to assess the risk/reward of opportunities?

We sincerely hope the U.S. will not follow this trend set by Europe and Japan. We would rather see a robust contribution from fiscal spending than negative interest rates if any further support is required this business cycle. Signs point to this being the case based on the bipartisan support for infrastructure and defense spending. After five lean budget years, fiscal spending is forecast to add 0.6% to GDP in the current fiscal year.

### YIELDS OF GLOBAL BONDS

**AS OF 6.30.2016**

<table>
<thead>
<tr>
<th>Yield Category</th>
<th>U.S. Dollar Trillons</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;0%</td>
<td>$9.9</td>
</tr>
<tr>
<td>0% TO 1%</td>
<td>$9.3</td>
</tr>
<tr>
<td>1% TO 2%</td>
<td>$5.1</td>
</tr>
<tr>
<td>&gt;2%</td>
<td>$2.0</td>
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</table>

<table>
<thead>
<tr>
<th>Yield Category</th>
<th>Percentage</th>
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</thead>
<tbody>
<tr>
<td>&lt;0%</td>
<td>38%</td>
</tr>
<tr>
<td>0% TO 1%</td>
<td>35%</td>
</tr>
<tr>
<td>1% TO 2%</td>
<td>20%</td>
</tr>
<tr>
<td>&gt;2%</td>
<td>8%</td>
</tr>
</tbody>
</table>

Sources: Cambridge Associates, LLC, and Barclays.

Notes: As of June 30, 2016, the Barclays Global Aggregate Bond Index total market value was $26.3 trillion, $9.9 trillion (38%) of which carried a negative yield. The number in parentheses represents the percent of the Barclays Global Aggregate Bond Index in each yield category. The Barclays Global Aggregate Bond Index contains only bonds with maturities greater than one year.
 THEME 2

The five year rally in growth over value style continued last year. The low interest rates discussed in our first theme do impact our second: growth investments did better than value investments for a fifth consecutive year.

The chart below illustrates that since 2006, the MSCI World Growth index has outperformed the MSCI World Value index. Although not (yet) at the extremes reached in 1999 with the dotcom bubble and subsequent bust in 2000, the ratio of growth to value on a global scale has persisted.

Some of this valuation difference relates to financially-repressed investors and savers who continue to buy stocks that act like bonds such as consumer staples, utilities, or Real Estate Investment Trusts (REITs) and seek to avoid cyclical sectors like financials, energy, and industrials. Safe sectors attract investors during periods of uncertainty and a flat yield curve. Value indexes are dominated by financials and industrials that are more cyclical and therefore affected more by uncertain global growth outlook. The majority of value style underperformance in the past year relates to the financial sector that has performed poorly as a result of persistently low to negative interest rates. Although we cannot predict when this trend will reverse, we know it will and that the portfolio is positioned to take advantage of the next cycle.

RELATIVE CUMULATIVE WEALTH: MSCI WORLD VALUE VS MSCI WORLD GROWTH


Sources: Cambridge Associates, LLC, FactSet Research Systems, MSCI Inc., and Thomson Reuters Datastream.
MSCI data provided “as is” without any express or implied warranties.
Notes: Relative cumulative wealth calculations are based on total returns net of dividend taxes. Shaded areas represent periods of value outperformance.
THEME 3

The continued outperformance of private investments such as private equity, venture capital, and real estate versus their publicly-traded allocations.

The following charts show that private investments have outperformed their public market equivalents in the most recent measurement period (through December 2015), and over most time horizons going back 20 years. Over the near-term, performance differences between these two major asset categories is due to a time difference: at the beginning or end of an economic cycle, public investments move up or down quickly whereas private investments catch up in terms of valuations with a three to nine month lag.

However, over the long-term, privates should outperform publicly-traded assets because of the illiquidity premium that should reward investors for the risk of committing precious liquidity for 7-12 years. Also, since private equity historically focused on smaller companies (the exception being the run-up to the global financial crisis that saw large cap leveraged buyouts explode), the ability to do more in terms of operational improvements should be greater for private equity investments versus public market equivalents. Today, we are nearing the end of an economic cycle when mergers and acquisitions increase. Private equity sponsors have improved company performance and can now sell them at much higher prices to larger publicly-traded companies that seek to improve earnings growth.

PERFORMANCE OF SELECT CAMBRIDGE ASSOCIATES PRIVATE INVESTMENT INDEXES VS PUBLIC EQUIVALENTS

AS OF 12.31.2015

<table>
<thead>
<tr>
<th>ONE-YEAR</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>CA REAL ESTATE</td>
<td>10.3%</td>
</tr>
<tr>
<td>FTSE® NAREIT COMPOSITE mPME</td>
<td>2.4%</td>
</tr>
<tr>
<td>CA U.S. PRIVATE EQUITY</td>
<td>5.9%</td>
</tr>
<tr>
<td>RUSSEL 3000® mPME</td>
<td>0.4%</td>
</tr>
<tr>
<td>CA U.S. VENTURE CAPITAL</td>
<td>12.9%</td>
</tr>
<tr>
<td>RUSSEL 3000® mPME</td>
<td>0.5%</td>
</tr>
</tbody>
</table>

Sources: Cambridge Associates LLC, Frank Russell Company, FTSE International Limited, National Association of Real Estate Investment Trusts, and Thomson Reuters Datastream.

Notes: Private indexes are pooled horizon-IRRs, net of fees, expenses, and carried interest. CA Modified Public Market Equivalent (mPME) replicates private investment performance under public market conditions. The public index’s shares are purchased and sold according to the private fund cash flow schedule, with distributions calculated in the same proportion as the private fund, and mPME net asset value is a function of mPME cash flows and public index returns.
FIVE-YEAR

- CA REAL ESTATE: 11.5%
- FTSE® NAREIT COMPOSITE mPME: 12.1%
- CA U.S. PRIVATE EQUITY: 13.0%
- RUSSEL 3000® mPME: 12.7%
- CA U.S. VENTURE CAPITAL: 16.2%
- RUSSEL 3000® mPME: 13.9%

TEN-YEAR

- CA REAL ESTATE: 5.0%
- FTSE® NAREIT COMPOSITE mPME: 9.4%
- CA U.S. PRIVATE EQUITY: 11.2%
- RUSSEL 3000® mPME: 8.3%
- CA U.S. VENTURE CAPITAL: 10.9%
- RUSSEL 3000® mPME: 7.7%

TWENTY-YEAR

- CA REAL ESTATE: 7.2%
- FTSE® NAREIT COMPOSITE mPME: 11.1%
- CA U.S. PRIVATE EQUITY: 12.8%
- RUSSEL 3000® mPME: 8.0%
- CA U.S. VENTURE CAPITAL: 31.1%
- RUSSEL 3000® mPME: 8.0%
II. FISCAL YEAR IN REVIEW: 2016

The following report refers to the Foundation’s pooled endowment that totaled $1.4 billion at fiscal year-end.

During the past fiscal year, the Investment Team made great strides to further the portfolio restructure work begun in late 2013 and, as of fiscal year end, 72% of the portfolio has been re-structured. In particular, changes during the previous 12 months included two manager terminations and one fund closing. Twelve new fund commitments or investments were made that represented nine manager relationships. Investments were made in international equity; Asian emerging market equity; seed stage venture capital; Nordic growth (private) equity; and private and public credit. We exploited the two periods of high market volatility mentioned in Part I to add to existing managers who had higher potential for gains and by changing our order of new investment decisions based on the new relative valuations. Regular re-balancing occurred as well when certain asset or sub-asset groups neared the upper or lower ranges as established by the Investment Policy Committee.

We confronted the existing gap in the portfolio’s private equity and real estate pacing cycle and allocations. In 2014, we began work on a portfolio that had no new commitments after the 2006–2008 vintage year investment period—the era of mega-buyouts and expensive commercial and residential real estate that, in retrospect, proved an inopportune time to begin a program. In these asset classes, it is critically important to make manager commitments on a regular basis, through good markets and bad, in order to achieve strong vintage year diversification. Although we have worked as quickly as possible since late 2013-2014 to jump start our internally-managed private equity and real estate portfolios, high valuations have made us cautious with the speed and size of our allocations since we wish to avoid committing significant capital—for the second time—at the top of the cycle. It will take time for our recent decisions to season and provide the returns we seek. As the chart on the following page indicates,
institutions with a minimum of 15% allocated to private investments had the strongest returns as measured by Cambridge Associates from 2005–2015.

In the current interest rate climate, identifying opportunities that made sense in fixed income was another challenge, especially in the public arena. We added two strategies that could be classified as private credit. As the Policy Portfolio in Part IV illustrates, the portfolio has a Global Credit target of 17%. As of July 1st, this allocation stands at 8.0%. We have done a number of unorthodox or “orthogonal” strategies in this area including the emerging field of litigation finance, and the niche, event-driven area of non-agency, residential mortgage-backed securities derivatives. We are sensitive to the fact that many liquid credit managers—faced with the crisis of low returns—slowed or stopped investing altogether rather than assume more risk and/or a lower margin of safety. We do not fault them for throwing in the towel instead of charging fees without a strong expectation of delivering good returns to their investors. We will continue to work toward this target but are being patient relative to what might be the next great credit cycle. Although we do not know when it will begin, there will be a more propitious time to add funds to this area.

### THE 15% FRONTIER

Source: Cambridge Associates, LLC

Notes: Analysis includes 242 endowments and foundations that provided returns and asset allocation for each June 30 from 2005 to 2015. Subgroups are based on each institution’s ten-year average allocation to private investments.
Every year, we review performance from a variety of different perspectives that include both absolute and relative measures of success. First, we measure performance relative to the endowment’s policy portfolio benchmark. The endowment realized a -3.0% return, net of all fees and expenses, relative to the total portfolio benchmark’s return of -1.6%. This resulted in a relative performance shortfall for the fiscal year ended June, 2016 of -1.4%.

The second approach to performance evaluation asks the question: was the realized return sufficient to meet or exceed the minimum required return to support the University and the Foundation? We calculate the minimum required return every year based on the total of the spending distribution, administrative fee, and realized inflation. The minimum required (real) return for the fiscal year just ended was 5.9%, indicating that our return fell short of the minimum required number. Our long term goal is to exceed the minimum required return on an annualized basis over time but we expect that, like the past year, there will be times when we fall short of this objective.

Finally, we consider performance attribution metrics that offer a deeper understanding of the various sources of endowment return, measuring the value added (or subtracted) through active management. The first attribute’s performance is due to asset allocation; that is, the value due to deviations from the portfolio’s target asset allocation.

Based on preliminary figures, Asset allocation (on a net basis) was neutral during the fiscal year relative to the benchmark; and, the resulting net underperformance of -1.4% can be primarily attributed to the following factors that involve Manager Selection/Execution, the majority from within our U.S. Equity and Global Equity managers. We will not have the final quarter’s private investment performance until after the publication of this report but will update the Website once they are available.

- **U.S. Equity**: subtracted approximately -.94% of relative performance. This can be attributed to poor performance by a healthcare manager (-.62%); and the poor execution (or timing) of a reduction in U.S. equities in August, 2015 (-.30%).
- **Global Equity**: subtracted approximately -.37% of relative performance. This can be attributed to manager performance (-.20%); and our selection of the applicable benchmark (-.17).

Although we are certainly not satisfied with the portfolio’s absolute and relative returns, it is important to remember that June 30th is just one snapshot during a fiscal year. We have built (and continue to build) a portfolio designed to do well over the long-term, even as we fully recognize the interim periods of disappointing performance such as the year just ended. It is also important to stress that approximately 72% of the internally-managed portfolio’s managers have been in place for less than three years. Time, patience, and consistency of strategy are critical to our future success now that many of the building blocks are in place.

The chart below shows the current and historical performance relative to various internal and external benchmarks.

<table>
<thead>
<tr>
<th>ENDOWMENT POOL COMPARISON TO BENCHMARKS IN YEARS</th>
<th>ONE</th>
<th>THREE*</th>
<th>FIVE*</th>
<th>TEN*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Return (net of fees)</td>
<td>-3.0%</td>
<td>4.7%</td>
<td>5.5%</td>
<td>4.6%</td>
</tr>
<tr>
<td>Total Portfolio Benchmark</td>
<td>-1.6%</td>
<td>5.4%</td>
<td>6.2%</td>
<td>5.6%</td>
</tr>
<tr>
<td>Relative +/-</td>
<td>-1.4%</td>
<td>-0.7%</td>
<td>-0.6%</td>
<td>-1.0%</td>
</tr>
<tr>
<td>Peer Group Median Return¹</td>
<td>-2.4%</td>
<td>5.7%</td>
<td>6.0%</td>
<td>5.5%</td>
</tr>
<tr>
<td>All Public Institutions Median Return</td>
<td>-2.9%</td>
<td>4.7%</td>
<td>4.8%</td>
<td>4.9%</td>
</tr>
<tr>
<td>Annualized Effective Total Spending Rate²</td>
<td>4.9%</td>
<td>5.0%</td>
<td>5.2%</td>
<td>5.5%</td>
</tr>
</tbody>
</table>

¹Based on the 2015 NACUBO-Commonfund Study of Endowments peer universe of all endowments >$1 billion in AUM.
²Includes administrative fee (spending is pursuant to the Foundation’s policy and in consultation with the University).

The Foundation currently distributes 4% of a six-year moving average of the corpus of most endowment accounts to the University. The policy is reviewed annually by the Foundation’s Board of Directors. For 2016, the 4.9% total spending consists of a 3.6% "effective" spending rate and a 1.3% “effective" administrative fee.

*Three-, five- and ten-year annualized returns expressed in percent per year.
“Time, patience, and consistency of strategy are critical to our future success now that many of the building blocks are in place.”

ELLEN ELLISON, CHIEF INVESTMENT OFFICER
IV. CURRENT ASSET ALLOCATION & THE POLICY PORTFOLIO

The policy portfolio benchmark represents the returns that hypothetically would have resulted if each asset class had been weighted at its policy target weight and generated the average asset class return.

It is reviewed annually by the Foundation’s Investment Policy Committee based on input and recommendations from the CIO and the Investment Team. The policy portfolio is the theoretical, dynamic, long-term mix of assets that will best support “intergenerational equity” or the balance between current spending distributions and future principal growth that can, in turn, support spending in perpetuity.

The policy portfolio is reviewed and discussed annually within the context of both expected returns (on a 10-year forward basis) and estimated risk, but does not typically change from year to year. Although the investment team is highly attuned to the current forces shaping the market, our primary goal is to manage around the long-term policy target allocations within the established ranges. Having an established long-term target within a reasonable range allows us to re-balance the portfolio in a consistent and disciplined manner.

Finally, the policy portfolio provides the Investment Team and the Investment Policy Committee with a strategic blueprint or outline that can enhance our discussions and support rational and disciplined decision-making, especially during difficult market cycles. We strive to avoid making reactive changes to the portfolio under duress as this is often the most common mistake made by investors and investment boards. It is vital to remember that although we do not control what the markets will do, we can as a group of engaged fiduciaries control how we react to the market.

After considerable analysis and discussion, the Investment Policy Committee and Investment Team decided to “re-order” the way we visualize and think about
asset allocation. Our goal was to create a nomenclature that would enhance our dialogue on the true nature of potential return and risks in the endowment. Although this is not a new concept, the main catalyst for this change was the recognition that hedge funds are not an asset class but rather an implementation strategy that can represent any number of different types of assets. Therefore, we eliminated the hedge fund category and now focus on the “underlying” assets and their role in the portfolio.

We also eliminated the term “alternatives” that is applied broadly for all non-traditional categories, because this had lost much of its original meaning after years of ubiquitous usage. We did not change the actual percentages in the process but rather placed them in different categories. Below you will find the new asset allocation taxonomy represented by three main groups: Global Equity; Global Credit; and Global macro risk hedges.

For example, all equity investments, including hedged and private, are included in the new category of Global Equity. This is the growth driver of the portfolio. We moved risk-free bonds, such as Treasuries and other Sovereigns into the Global Macro Risk Hedges portfolio based on the belief that these would not be driving growth but would protect the portfolio during rocky periods such as the past six months. Finally, global credit sits between the two, literally and metaphorically, and helps diversify the sources of return further and includes all types of credit risks. Ideally, this area will provide some growth but with a lower degree of fluctuation relative to Global Equities.

### ACTUAL FY 2016 VS. POLICY PORTFOLIO

<table>
<thead>
<tr>
<th>ASSET ALLOCATION</th>
<th>UIF 2016 ACTUAL</th>
<th>UIF TARGET</th>
<th>CAMBRIDGE ASSOCIATES OVER $1B COMPOSITE GROUP MEANS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GLOBAL EQUITY</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Equity</td>
<td>18.6%</td>
<td>18%</td>
<td>19%</td>
</tr>
<tr>
<td>Non-U.S. Developed</td>
<td>19.2%</td>
<td>12%</td>
<td>20%</td>
</tr>
<tr>
<td>Non-U.S. Emerging²</td>
<td>9.8%</td>
<td>8%</td>
<td></td>
</tr>
<tr>
<td>Global Equity/Hedged Equity</td>
<td>13.8%</td>
<td>15%</td>
<td></td>
</tr>
<tr>
<td>Private Equity³</td>
<td>8.7%</td>
<td>10%</td>
<td>14%</td>
</tr>
<tr>
<td>Hedge Funds⁴</td>
<td>0.0%</td>
<td>0%</td>
<td>20%</td>
</tr>
<tr>
<td><strong>GLOBAL CREDIT</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit/Absolute Return/Distressed</td>
<td>7.0%</td>
<td>17%</td>
<td>4%</td>
</tr>
<tr>
<td><strong>MACRO RISK HEDGES</strong></td>
<td>22.9%</td>
<td>20%</td>
<td>23%</td>
</tr>
<tr>
<td>Global Rates⁵</td>
<td>8.8%</td>
<td>4%</td>
<td>11%</td>
</tr>
<tr>
<td>Global Inflation-Linked Bonds</td>
<td>4.1%</td>
<td>4%</td>
<td>6%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>3.2%</td>
<td>6%</td>
<td></td>
</tr>
<tr>
<td>Natural Resources⁶</td>
<td>6.8%</td>
<td>6%</td>
<td>6%</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>100%</td>
<td>100%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

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¹As affirmed by the Investment Policy Committee in June 2016
²Includes up to 2.5% in dedicated Frontier Market Equity strategies
³Includes LBO, Mezzanine, M&A, Growth Equity, International PE, and Venture Capital
⁴UIF’s hedge fund investments are not treated as a separate asset class
⁵Includes short duration, liquidity assets that may result from portfolio and gift cash flows
⁶Includes private real estate (non-campus), energy, and natural resources (oil and gas, timber, and agriculture)
V. LOOKING AHEAD
We hope for more global growth but plan for continued volatility. As we begin the new fiscal year, we have many challenging questions.

Is it reasonable to continue to rely on the U.S. as an anchor of stability for the rest of the world?

Although we do not pretend to have answers, nor are we in the habit of making sweeping, macro-style pronouncements, we do think the U.S. economy is in decent shape and begins the second half of 2016 on a nice upswing. Higher U.S. wages are a good thing and should eventually stimulate productivity. We welcome the re-introduction of thoughtful and necessary fiscal spending since much of our infrastructure is outdated. As a highly developed economy, we have to focus on what we do best in parts of the economy where there is a lot of value-add. We are probably in the 4th or 5th inning of this economic cycle based on a number of metrics, but caution that with the amount of monetary distortion embedded in the system, any assessment of this type is far less useful today than it would have been historically.

What is the best way for the developed world to achieve a higher rate of economic growth?

Since 2007, $6.0 trillion has been “shaved” from global growth as world GDP transitioned from a long-term growth rate of 3.4% to 2.1%. Since the global financial crisis, economic growth has not returned to normal and this has persisted for eight years. Things are improving but it is taking far longer than initially forecast. Monetary stimulus may now be retarding normal business and economic decision-making. The re-introduction of some robust fiscal policy initiatives from Japan to the U.S. should also help drive global growth closer to 3.0%. Furthermore, the drag of this post-crisis period is forcing many countries in the developed world to embrace what would have been considered radical change just a few years ago. Sometimes, true progress begins when one’s back is against the wall. We note many positive
signs of corporate governance improvements and better economic policies in European countries and in Japan.

Are politics the source of future “Black Swans”—will populism lead to protectionism and new trade wars?

After several decades of politics having no lasting influence on the economy and the markets, things are now different. We think this is due to prolonged slow growth and the uneven distribution of economic benefits across the population. There has been a hollowing out of the U.S. middle class and income inequality has risen. Politics are increasingly polarized in the U.S. and in other developed countries such as the U.K. This has led to greater volatility with the risk of unexpected surprises, such as the Brexit vote. We should anticipate these shocks to the global markets so that we can avoid being reactive when they do occur. However unpleasant, political “Black Swans” may create opportunities for long term investors.

Where are the best near and long-term opportunities for the endowment?

As we look ahead, we wonder if the next big credit cycle could begin in the next year or so. The first big crack occurred in late 2014 in the energy sector. There are growing signs that we are near an inflection point: global growth is moderating; bank lending standards have improved significantly; defaults are rising; and, valuations leave very little room for disappointment. These red flags, albeit present for some time, have been overshadowed by the still unchallenged belief in the power of the Fed to control the economy. We want to be ready for the next distressed credit cycle wherever or however it manifests itself. We have identified and, in some cases, engaged investment managers who specialize in this area so that we can take advantage of market dislocations when they occur.

In 2016, we have finally enjoyed some strong returns for the first time in five years within Emerging Markets (EM) as the next stop on investors’ global search for yield. Despite their recent rise, we think that EM remains attractive, particularly in emerging Asia and in Latin America. Emerging Market equities are undervalued relative to U.S. equities. It will be important to identify how the next phase of development plays out in these economies now that the commodity “super cycle” is over and China’s demand has waned for the types of raw materials that countries like Brazil and Mexico produce.

The bull and then subsequent bear market in Emerging Market equities, debt, and related commodities was tightly correlated with the boom and bust in commodities and energy. This “super cycle,” ignited by strong Chinese demand for basic materials and commodities, rolled over in 2011 when the Chinese government signaled its intent to transition the economy toward internally-driven consumption. The Chinese economy has slowed, but there are big and important changes going on within the middle class of brand new consumers. We are following closely the growth of the Chinese middle class and its desire for greater food, water, and product safety; travel; leisure; healthcare; and consumer goods. We are also interested to see how Brazil will emerge from its current governmental and economic crisis. Global agriculture/agribusiness and healthcare represent two other important themes within the developing world that we continue to watch and exploit.

In conclusion, despite the myriad challenges of the past year, we are confident that the endowment portfolio is structured to meet our goals. We avoid leverage; we pursue value strategies that provide “built-in” insurance; we keep some “dry powder” to be able to act when others behave irrationally; and, finally we have partnered with investment managers who share our philosophy and are equally immune to the siren call of short term results. Although we understand the current investor logic of getting defensive in light of the global uncertainty we face—especially if one’s investment horizon is short—we will not pursue this type of strategy.

“Safe” investments are priced for perfection and in our estimation are the epitome of unsafe and will not help us attain our investment return goals.

We anchor investment decision-making to valuation because we believe that the price one pays (or enters into an investment strategy) will have the biggest influence on our long term success.
“Philanthropy will have a greater impact on the future University of Illinois. It already does and will continue to change lives for the better. We have the opportunity as donors to invest in faculty and students who invent and build tomorrow’s society.”

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