

2007

The Yale Endowment



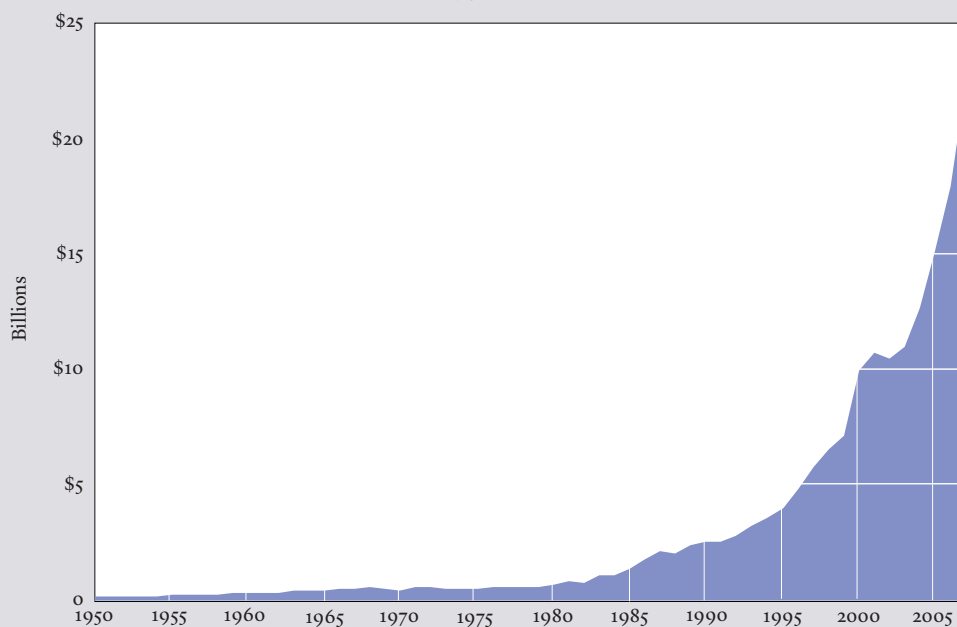
Endowment Highlights

	Fiscal Year				
	2007	2006	2005	2004	2003
Market Value (in millions)	\$22,530.2	\$18,030.6	\$15,224.9	\$12,747.2	\$11,034.6
Return	28.0%	22.9%	22.3%	19.4%	8.8%
Spending (in millions)	\$ 684.0	\$ 616.0	\$ 567.0	\$ 502.0	\$ 470.1
Operating Budget Revenues (in millions)	2,075.0	1,932.0	1,768.0	1,630.8	1,553.7
Endowment Percentage	33.0%	31.9%	32.2%	30.8%	30.3%

Asset Allocation (as of June 30)

Absolute Return	23.3%	23.3%	25.7%	26.1%	25.1%
Domestic Equity	11.0	11.6	14.1	14.8	14.9
Fixed Income	4.0	3.8	4.9	7.4	7.4
Foreign Equity	14.1	14.6	13.7	14.8	14.6
Private Equity	18.7	16.4	14.8	14.5	14.9
Real Assets	27.1	27.8	25.0	18.8	20.9
Cash	1.9	2.5	1.9	3.5	2.1

Endowment Market Value 1950–2007

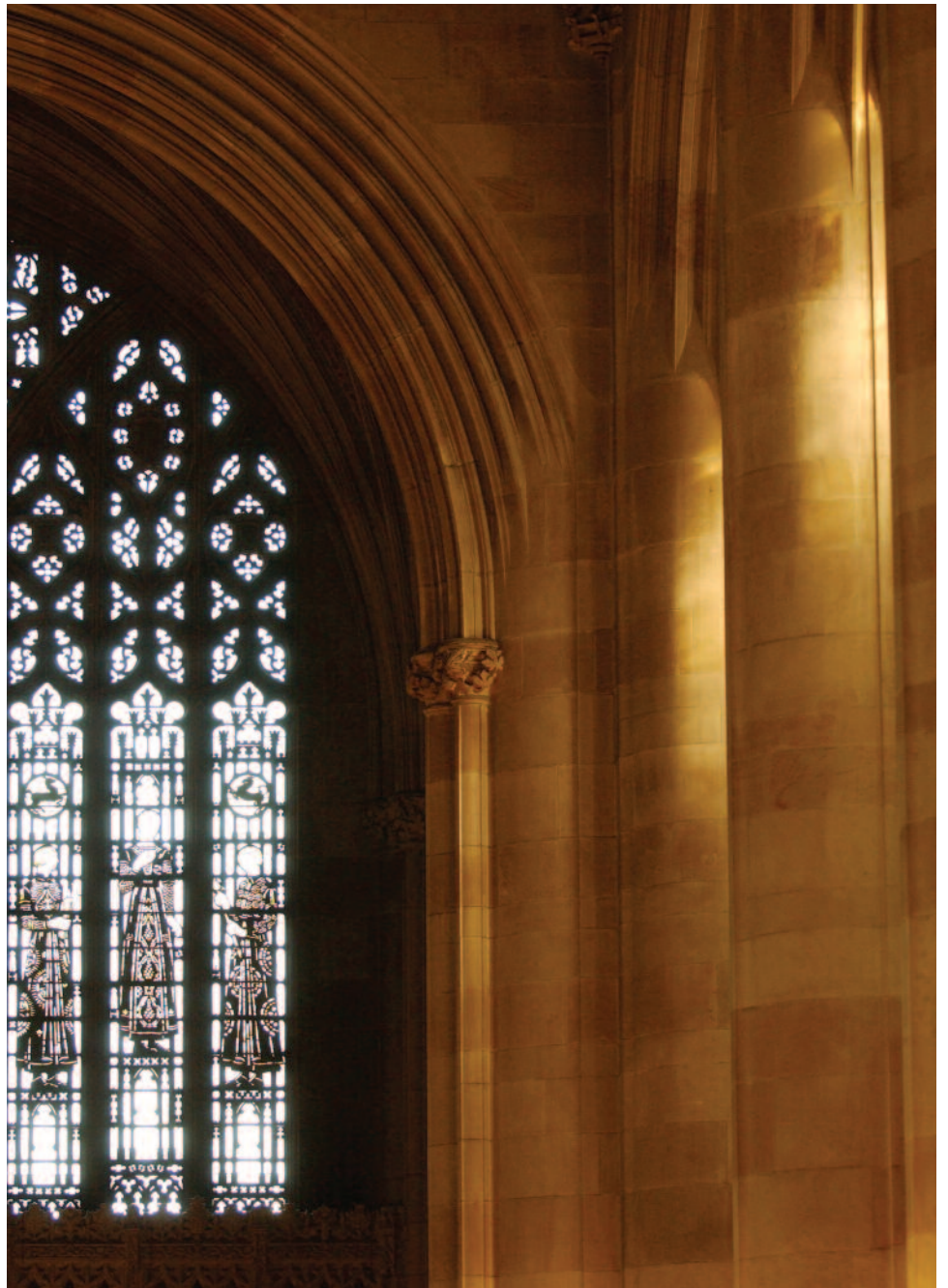


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Front cover:
Wall carving from west façade, Sterling
Memorial Library.

Right:
A window in Sterling Memorial Library.



Introduction

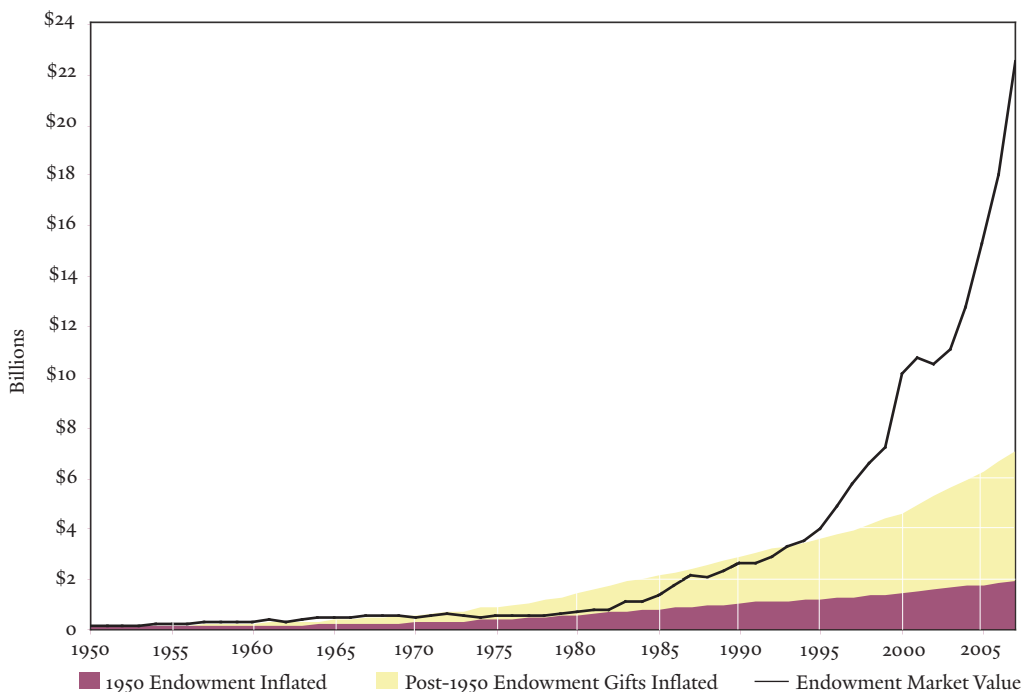
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Yale's Endowment generated extraordinarily strong results in fiscal year 2007, as investment returns of 28.0 percent produced record-setting investment gains of \$5.0 billion. For the third straight year, Yale enjoyed returns well in excess of 20 percent.

Over the past ten years, the Endowment grew from \$5.8 billion to \$22.5 billion. With annual net investment returns of 17.8 percent, the Endowment's performance exceeded its benchmark and outpaced institutional fund indices. The Yale Endowment's twenty-year record of 15.6 percent per annum produced a 2007 Endowment value of more than ten times that of 1987. Yale's superb long-term record resulted from disciplined and diversified asset allocation policies, superior active management results, and strong capital market returns.

Spending from Endowment grew during the last decade from \$191 million to \$684 million, an annual growth rate of approximately 14 percent. On a relative basis, Endowment contributions expanded from 18 percent of total revenues in fiscal 1997 to 33 percent in fiscal 2007. Next year, spending will amount to \$843 million, or 37 percent of projected revenues. Yale's spending and investment policies have provided handsome levels of cash flow to the operating budget for current scholars while preserving Endowment purchasing power for future generations.

Endowment Growth Outpaces Inflation 1950–2007



2

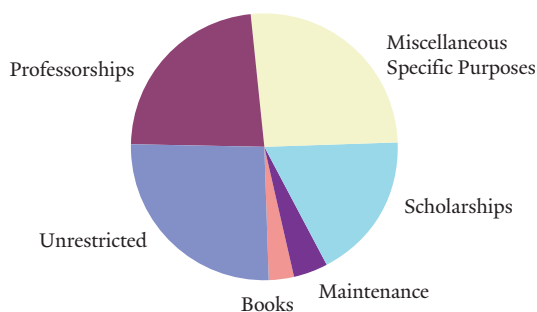
Totalling \$22.5 billion on June 30, 2007, the Yale Endowment contains thousands of funds with a variety of designated purposes and restrictions. Approximately four-fifths of funds constitute true endowment, gifts restricted by donors to provide long-term funding for designated purposes. The remaining one-fifth represent quasi-endowment, monies that the Yale Corporation chooses to invest and treat as endowment.

Donors frequently specify a particular purpose for gifts, creating endowments to fund professorships, teaching, and lectureships (23 percent), scholarships, fellowships, and prizes (18 percent), maintenance (4 percent), books (3 percent), and miscellaneous specific purposes (26 percent). Twenty-six percent of funds are unrestricted. Thirty-four percent of the Endowment benefits the overall University, with remaining funds focused on specific units, including the Faculty of Arts and Sciences (30 percent), the professional schools (23 percent), the library (7 percent), and other entities (6 percent).

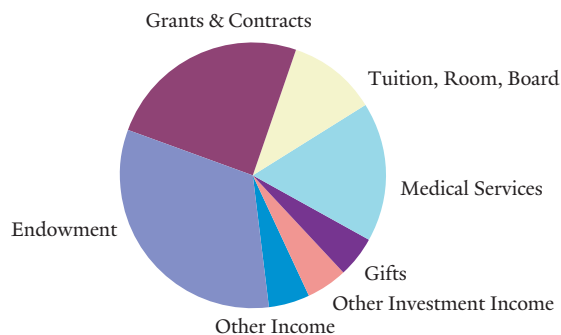
Although distinct in purpose or restriction, Endowment funds are commingled in an investment pool and tracked with unit accounting much like a large mutual fund. Endowment gifts of cash, securities, or property are valued and exchanged for units that represent a claim on a portion of the whole investment portfolio.

In fiscal 2007, the Endowment provided \$684 million, or 33 percent, of the University's \$2,075 million operating income. Other major sources of revenues were grants and contracts of \$526 million (25 percent), medical services of \$344 million (17 percent), net tuition, room, and board of \$237 million (11 percent), gifts of \$98 million (5 percent), other investment income of \$94 million (5 percent), and other income and transfers of \$92 million (4 percent).

Endowment Fund Allocation
Fiscal Year 2007



Operating Budget Revenue
Fiscal Year 2007



3

Yale's portfolio is structured using a combination of academic theory and informed market judgment. The theoretical framework relies on mean-variance analysis, an approach developed by Nobel laureates James Tobin and Harry Markowitz, both of whom conducted work on this important portfolio management tool at Yale's Cowles Foundation. Using statistical techniques to combine expected returns, variances, and covariances of investment assets, Yale employs mean-variance analysis to estimate expected risk and return profiles of various asset allocation alternatives and to test sensitivity of results to changes in input assumptions.

Because investment management involves as much art as science, qualitative considerations play an extremely important role in portfolio decisions. The definition of an asset class is quite subjective, requiring precise distinctions where none exist. Returns and correlations are difficult to forecast. Historical data provide a guide, but must be modified to recognize structural changes and compensate for anomalous periods. Quantitative measures have difficulty incorporating factors such as market liquidity or the influence of significant, low-probability events. In spite of the operational challenges, the rigor required in conducting mean-variance analysis brings an important perspective to the asset allocation process.

The combination of quantitative analysis and market judgment employed by Yale produces the following portfolio:

Asset Class	June 2007	Current Target
Absolute Return	23.3%	23.0%
Domestic Equity	11.0	11.0
Fixed Income	4.0	4.0
Foreign Equity	14.1	15.0
Private Equity	18.7	19.0
Real Assets	27.1	28.0
Cash	1.9	0.0

The target mix of assets produces an expected real (after inflation) long-term growth rate of 6.3 percent with a risk (standard deviation of returns) of 12.4 percent. Because of deviations in actual holdings from target levels, the actual allocation produces a portfolio expected to grow at 6.2 percent with a risk of 12.2 percent. The University's measure of inflation is based on a basket of goods and services specific to higher education that tends to exceed the Consumer Price Index by approximately one percentage point.

At its June 2007 meeting, Yale's Investment Committee adopted a number of changes in the University's policy portfolio allocations. Despite massive capital inflows to the alternatives arena, Yale's disciplined managers continue to find compelling opportunities. The Committee approved an increase in the private equity target from 17 percent to 19 percent due to the persistence of attractive bottom-up opportunities, even in this heated market. The University increased the real assets allocation from 27 percent to 28 percent, as Yale's managers demonstrate the ability to source off-market acquisitions at below-market prices. The increases in the illiquid asset classes were funded by a 2 percentage point decrease in the absolute return target allocation to 23 percent, and a 1 percentage point decrease in the domestic equity target allocation to 11 percent.

The need to provide resources for current operations as well as preserve purchasing power of assets dictates investing for high returns, causing the Endowment to be biased toward equity. In addition, the University's vulnerability to inflation further directs the Endowment away from fixed income and toward equity instruments. Hence, 96 percent of the Endowment is targeted for investment in assets expected to produce equity-like returns, through holdings of domestic and international securities, real assets, and private equity.

Over the past two decades, Yale reduced dramatically the Endowment's dependence on domestic marketable securities by reallocating assets to nontraditional asset classes. In 1987, nearly 80 percent of the Endowment was committed to U.S. stocks, bonds, and cash. Today, target allocations call for 15 percent in domestic marketable securities, while the diversifying assets of foreign equity, private equity, absolute return strategies, and real assets dominate the Endowment, representing 85 percent of the target portfolio.

The heavy allocation to nontraditional asset classes stems from their return potential and diversifying power. Today's actual and target portfolios have significantly higher expected returns and lower volatility than the 1987 portfolio. Alternative assets, by their very nature, tend to be less efficiently priced than traditional marketable securities, providing an opportunity to exploit market inefficiencies through active management. The Endowment's long time horizon is well suited to exploiting illiquid, less efficient markets such as venture capital, leveraged buyouts, oil and gas, timber, and real estate.

Asset Class Characteristics

Yale's six asset classes are defined by differences in their expected response to economic conditions, such as price inflation or changes in interest rates, and are weighted in the Endowment portfolio by considering risk-adjusted returns and correlations. The University combines these assets in such a way as to provide the highest expected return for a given level of risk.

Absolute Return

In July 1990, Yale became the first institutional investor to pursue absolute return strategies as a distinct asset class, beginning with a target allocation of 15 percent. Designed to provide significant diversification to the Endowment, absolute return investments seek to generate high long-term real returns by exploiting market inefficiencies. Approximately half of the portfolio is dedicated to event-driven strategies, which rely on a very specific corporate event, such as a merger, spin-off, or bankruptcy restructuring to achieve a target price. The other half of the portfolio contains value-driven strategies, which involve hedged positions in assets or securities that diverge from underlying economic value. Today, the absolute return portfolio is targeted to be 23.0 percent of the Endowment, above the average educational institution's allocation of 19.5 percent to such strategies. Absolute return strategies are expected to generate real returns of 6.0 percent with risk levels of 10.0 percent for event-driven strategies and 15.0 percent for value-driven strategies.

Unlike traditional marketable securities, absolute return investments provide returns largely independent of overall market moves. Over the past ten years, the portfolio exceeded expectations, returning 13.1 percent per year with essentially no correlation to domestic stock and bond markets.

An important attribute of Yale's investment strategy concerns the alignment of interests between investors and investment managers. To that end, absolute return accounts are structured with performance-related incentive fees, hurdle rates, and clawback provisions. In addition, managers invest a significant portion of their net worth alongside Yale, enabling the University to avoid many of the pitfalls of the principal-agent relationship.

Domestic Equity

Finance theory predicts that equity holdings will generate returns superior to those of less risky assets such as bonds and cash. The predominant asset class in most U.S. institutional portfolios, domestic equity represents a large, liquid, and heavily researched market. While the average educational institution invests 26.3 percent of assets in domestic equities, Yale's target allocation to this asset class is only 11.0 percent. The domestic equity portfolio has an expected real return of 6.0 percent with a standard deviation of 20.0 percent. The Wilshire 5000 Index serves as the portfolio benchmark.

Despite recognizing that the U.S. equity market is highly efficient, Yale elects to pursue active management strategies, aspiring to outperform the market index by a few percentage points annually. Because superior stock selection provides the most consistent and reliable opportunity for generating excess returns, the University favors managers with exceptional bottom-up fundamental research capabilities. Managers searching for out-of-favor securities often find stocks that are cheap in relation to current fundamental measures such as book value, earnings, or cash flow. Recognizing the difficulty of outperforming the market on a consistent basis, Yale searches for managers with high integrity, sound investment philosophies, strong track records, superior organizations, and sustainable competitive advantages.

Fixed Income

Fixed income assets generate stable flows of income, providing greater certainty of nominal cash flow than any other Endowment asset class. The bond portfolio exhibits a low covariance with other asset classes and serves as a hedge against financial accidents or periods of unanticipated deflation. While educational institutions maintain a substantial allocation to fixed income instruments and cash, averaging 12.7 percent, Yale's target allocation to fixed income constitutes only 4.0 percent of the Endowment. Bonds have an expected real return of 2.0 percent with risk of 10.0 percent. The Lehman Brothers U.S. Treasury Index serves as the portfolio benchmark.

Yale is not particularly attracted to fixed income assets, as they have the lowest historical and expected returns of the six asset classes that make up the Endowment. In addition, the government bond market is arguably the most efficiently priced asset class, offering few opportunities to add significant value through active management. Based on skepticism of active fixed income strategies and belief in the efficacy of a highly structured approach to bond portfolio management, the Investments Office chooses to manage Endowment bonds internally. In spite of an aversion to market timing strategies, credit risk, and call options, Yale manages to add value consistently in its management of the bond portfolio. Willingness to accept illiquidity leads to superior investment results without impairing the portfolio protection characteristics of high-quality fixed income.

Yung Wing and the Chinese Educational Mission



A portrait of Yung Wing (Rong Hong), 1828-1912, B.A. 1854, the first Chinese student to graduate from a North American university. The painting, by Judith Reeve, is based on a lithograph of Yung in his Yale class book. Commissioned by the Yale-China Association in 2000, the painting hangs in the Yale College Dean's Office.

A graduate of the Yale College class of 1854, Yung Wing (Rong Hong) was the first Chinese student to obtain a diploma from a North American university. Born in 1828 to a peasant family near Nanping, Guangdong Province, Yung Wing left home at the age of seven to attend missionary school. At age thirteen he entered the Morrison Education Society School, where he distinguished himself as an excellent student, earning the admiration of school principal Samuel Robbins Brown (B.A. 1832). In 1847, Brown brought Yung Wing to the United States, where he enrolled in Massachusetts' Monson Academy under the direction of Dr. Charles Hammond (B.A. 1839).

When Yung Wing arrived at Yale College in the fall of 1850, he was the only Chinese student in a class of ninety-eight young men. Yung Wing's "Bright College Years" were filled with both obstacles and triumphs. During his freshman year, he toiled over his studies deep into the night. He had almost no social life and took little exercise. Yung Wing was constantly plagued by self-doubt regarding his academic abilities. He had "an utter aversion to mathematics, especially to differential and integral calculus," which he "abhorred and detested."

Despite a rough start, Yung Wing was moved by his experience at Yale. In December 1850, he wrote to his mentor

Samuel Wells Williams (later a Yale College faculty member): "Old Yale is surrounded with an atmosphere of ambition... I never was subject to such excitement. I enjoy its influence very much." In spite of his troubles with calculus, Yung Wing gained the admiration of his peers by winning two first prizes in English composition. During his junior and senior years, he worked as a librarian for the Brothers in Unity debating society, allowing him to develop relationships with "members of the three classes above, and members of the three classes below" and thrusting Yung Wing into "the college world at large."

During his time in New Haven, Yung Wing's mind never veered far from the needs of his homeland. While on long walks, he and classmate Carrol Cutler (the future president of Case Western Reserve University) discussed the idea of an "educational mission," whereby Chinese students would be sent to the United States for the best liberal arts education this country offered. "I was determined that the rising generation of China should enjoy the same educational advantages that I had enjoyed," Yung Wing later wrote in his autobiography. "Towards such a goal, I directed all of my mental resources and energy."

The Chinese Educational Mission

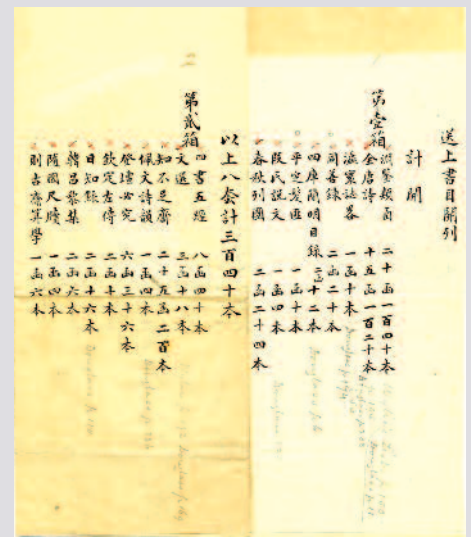
After graduation from Yale, Yung Wing spent ten years in the tea and silks business. He returned to a China wracked by violent internal rebellions and increasingly aggressive incursions from the West. In 1863, Yung Wing had the opportunity to present his plan for sending Chinese students abroad to Zeng Guofan, a liberal-minded Chinese official who was the driving force behind the "self-strengthening" movement, a progressive effort to stabilize and modernize an increasingly fractured China. In March 1872, the Qing government approved the Chinese Educational Mission (CEM), the formalization of the plan that Yung Wing hatched at Yale nearly two decades earlier.

The CEM called for 120 boys ranging from eleven to fifteen years old to study in the United States, in batches of thirty per year, for fifteen years. Yung Wing accompanied the first batch of boys back to the U.S., setting up headquarters in Hartford. In all, twenty-one Chinese students enrolled at Yale through the CEM. One student, Chung Mun Yew, B.A. 1883 (Zhong

Wenyao), Yale's first Chinese coxswain, made such a deep impression on the community that nearly thirty years after his departure from the University, the *Hartford Courant* recounted the following story:

"Famous in Yale annals as the coxswain of the Yale shell which distanced Harvard in the race of 1880, Chung was a favorite among his classmates. He was a bright student who never lost his temper and who was never known to swear, except on one occasion. That was during the race with Harvard in 1880. Toward the finish, the little coxswain broke out with 'Damn it boys, pull!': The boys did and Yale won the race."

Chung went on to join China's diplomatic service. Chung and fellow CEM students provided China with a generation of professional engineers, diplomats, and university presidents. Two Yale alumni went on to lead particularly illustrious careers: Jeme Tien Yau and Tong Koh-On. Jeme Tien Yau, Ph.B. 1881 (Zhan Tianyou), was admitted to Yale's civil engineering program in 1878. Jeme is the celebrated engineer of the Beijing-Zhangjiakou railroad line, the first in China to be built without direct foreign assistance. Although many were skeptical that Jeme could successfully navigate the mountainous northern terrain that separated Beijing from Zhangjiakou, he delivered the project under budget and two years ahead of schedule. Fondly remembered as the "father of the Chinese railroads," Jeme instituted a number of railroad standards that are still in force today.



Yung Wing's listing of the 1,237 volumes of Chinese texts that he contributed to Yale in 1877, following the University's agreement to establish a professorship in Chinese languages and literature.

Tong Koh-On (Tang Guo'an), the first president of China's prestigious Tsinghua University, enrolled at Yale in 1880. During Tong's freshman year, conservatives in the Qing government called into question the usefulness of the CEM. Despite the entreaties of Yung Wing, his personal friend Samuel T. Clemens (a.k.a. Mark Twain), Yale President Noah Porter, and Amherst College President Julius Seelye, the Chinese government discontinued the CEM program in 1881 and ordered the boys to sail home to China. Tong never obtained a Yale degree, but his compatriot, coxswain Chung, returned to Yale in 1904 for his twentieth reunion, when he was awarded his Bachelor of Arts in the Class of 1883.

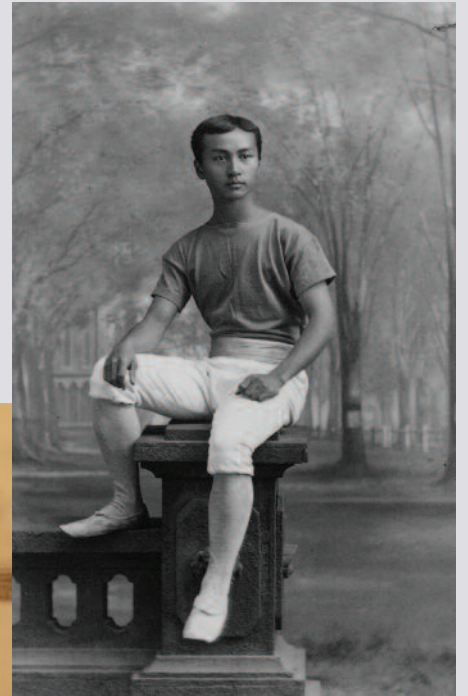
While Yung Wing was in the process of planning for and implementing the CEM, he also engaged in a range of other activities: he helped establish the China Merchant's Steamship Company, China's first domestically owned joint-stock corporation; he advocated for the rights of Chinese laborers in Peru, who were often mistreated by their employers; and he helped the Qing government purchase military equipment to modernize the Chinese armed forces. In 1876, in recognition of his many accomplishments, Yung Wing received an honorary degree from Yale Law School.

Contributions to Yale

As he carried out his efforts on behalf of China, Yung Wing reflected on ways to contribute to Yale. In 1877, Yung Wing offered to bestow a collection of 1,237 volumes of Chinese texts on Yale if the Corporation established a professorship in Chinese languages and literature. Gently urging the Yale Corporation to adopt his plan, Yung Wing wrote, "I hope Yale will not delay this matter long lest Harvard anticipate us." Yale agreed, laying the foundation for the University's East Asian Studies program at a time when few American colleges offered such instruction. Yung Wing's former mentor, Samuel Wells Williams, became Yale's first professor of Chinese language and literature. In one of his last acts, Williams left a bequest to Yale earmarked to fund the teaching of the Chinese language or "to assist worthy Chinese students in the College who may be in need." The Williams fund, created in 1903, is the University's earliest China-related endowment.

Although profoundly disappointed by the CEM's termination, Yung Wing continued to promote cross-cultural understanding and to pursue the betterment of China well into his old age. He grew from a self-doubting Yale freshman into one of the most influential Chinese figures of his time. Yung Wing's influence is still felt at

Yale today, over 150 years after his graduation. Two endowed funds, the Yung Wing Memorial Scholarship and the Yung Wing Memorial Fund for International Students, were created in his honor to support international students and students of Chinese descent. More students and scholars come to Yale from China than from any other country, with current totals of over 300 Chinese students and more than 330 Chinese scholars. Yale students have the opportunity to study Chinese language and Chinese society not only through numerous course offerings in New Haven, but also through programs based in China conducted jointly with Chinese universities. Nearly every Yale department supports ventures that allow University researchers to work with their colleagues in China. Yale's efforts to cooperate with China mark the legacy of a young man who planned and dreamed under the elms of Old Brick Row so long ago.



Chung Mun Yew (Zhong Wenyaoy), B.A. 1883, Yale's first Chinese coxswain, was brought to the United States through the Chinese Educational Mission, a program that sponsored Chinese students in this country, founded through the efforts of Yung Wing.

Foreign Equity

Investments in overseas markets give the Endowment exposure to the global economy, providing substantial diversification along with opportunities to earn above-market returns through active management. Emerging markets, with their rapidly growing economies, are particularly intriguing, causing Yale to target 6.0 percent of its portfolio to such opportunities, equal to the 6.0 percent allocated to foreign developed equities. In June 2007, Yale articulated a target of 3.0 percent of the portfolio to opportunistic foreign positions, with the expectation that holdings will be concentrated in emerging markets, particularly China and India. Yale's foreign equity target allocation of 15.0 percent stands materially below the average endowment's allocation of 22.1 percent. Expected real returns for emerging equities are 8.0 percent with a risk level of 25.0 percent, while developed equities are expected to return 6.0 percent with risk of 20.0 percent. The portfolio is measured against a composite benchmark of 40 percent developed markets, measured by the Morgan Stanley Capital International (MSCI) Europe, Australasia, and Far East Index, 40 percent emerging markets, measured by the MSCI Emerging Markets Index, and 20 percent opportunistic, measured by the Higher Education Price Index plus 8 percent.

Yale's investment approach to foreign equities emphasizes active management designed to uncover attractive opportunities and exploit market inefficiencies. As in the domestic equity portfolio, Yale favors managers with strong bottom-up fundamental research capabilities. Capital allocation to individual managers takes into consideration the country allocation of the foreign equity portfolio, the degree of confidence Yale possesses in a manager, and the appropriate asset size for a particular strategy. In addition, Yale attempts to exploit compelling undervaluations in countries, sectors, and styles by allocating additional capital and, perhaps, by hiring new managers to take advantage of the opportunities.



The Women's Table (by Maya Lin, B.A. 1981, M.A.R.C.H. 1986, D.F.A. 1987) reflecting Berkeley College and William L. Harkness Hall.

Private Equity

Private equity offers extremely attractive long-term risk-adjusted return characteristics, stemming from the University's strong stable of value-added managers that exploit market inefficiencies. Yale's private equity investments include participations in venture capital and leveraged buy-out partnerships. The University's target allocation to private equity of 19.0 percent far exceeds the 7.0 percent actual allocation of the average educational institution. In aggregate, the private equity portfolio is expected to generate real returns of 11.2 percent with risk of 27.7 percent. Yale's private equity program, one of the first of its kind, is regarded as among the best in the institutional investment community. The University is frequently cited as a role model by other investors pursuing this asset class. Since inception, private equity investments have generated a 31.4 percent annualized return to the University. The success of Yale's program led to a 1995 Harvard Business School case study – "Yale University Investments Office" – by Professors Josh Lerner and Jay Light. The popular case study was updated in 1997, 2000, 2003, and again in 2006.

Yale's private equity assets concentrate on partnerships with firms that emphasize a value-added approach to investing. Such firms work closely with portfolio companies to create fundamentally more valuable entities, relying only secondarily on financial engineering to generate returns. Investments are made with an eye toward long-term relationships – generally, a commitment is expected to be the first of several – and toward the close alignment of the interests of general and limited partners. Yale avoids funds sponsored by financial institutions due to the conflicts of interest and staff instability inherent in such situations.



View through Phelps Gate, on Old Campus, toward the New Haven Green.

The Yale-China Association

The Yale-China Association was founded in 1901 by a group of Yale University alumni and faculty members, motivated in part to honor the memory of Horace Tracy Pitkin (B.A. 1892), a Yale graduate who was killed during the Boxer Rebellion of 1900 while carrying out missionary work in China. Originally established as a non-denominational missionary society based in Changsha, Hunan, Yale-China was reincorporated in 1934 as a secular organization with education as its principal objective.

Medical education and care became a primary focus of Yale-China's work in 1905 with the arrival in Changsha of Edward H. Hume (B.A. 1897), who directed Yale-China's medical work for two decades. Dr. Hume's medical clinic was eventually transformed into an educational compound that included a number of institutions founded by Yale-China, including the Yali Middle School, Xiangya Medical College, Xiangya Nursing School, and Xiangya Hospital, an advanced teaching hospital built in 1916 with financial support from Edward S. Harkness (B.A. 1897), a generous Yale University benefactor.

The Yale-China Association made a dedicated effort early on to bring as many Chinese faculty and administrators into



The "Yali Middle School" campus photographed from the roof of the Xiangya Hospital in the 1930s. Yale-China founded the school in 1909 and continues to send Teaching Fellows to it today.

leadership positions as possible, making Yale-China a true joint Sino-American enterprise. Hume's endeavors in Changsha were assisted by Dr. Fuqing Yan, a 1909 graduate of the Yale School of Medicine. From 1910 to 1926, Yan provided a critical link between Chinese officials and the Western community, and went on to serve as China's Minister of Health in the 1930s.

Japan's invasion of China in 1937 placed severe strains on Yale-China's programs, especially the Xiangya Hospital, which cared for large numbers of casualties and war refugees. As the Chinese army retreated to the southwest, the Yale-China institutions also evacuated to regions free of Japanese occupation. Invading Japanese troops damaged many of the Changsha

facilities. In 1945, Yale-China staff returned to the Changsha campus, but political instability and a growing ambivalence toward foreigners made the future of the association uncertain. In 1951 the newly formed Communist government took over Yale-China's properties in Changsha, breaking the association's ties with mainland China.

From 1951 to 1979 the Yale-China Association directed its attention toward Hong Kong. The association formed a partnership with New Asia College and, with the support of the Ford Foundation and several other U.S. non-profit organizations, resumed the practice of sending new Yale College graduates to Asia to teach English, a program that remains in place. Yale-China assisted with the formation of the Chinese University of Hong Kong, securing funding for several new campus buildings and establishing the New Asia/Yale-in-China Chinese Language Centre and the International Asian Studies Program. The relationship between the Yale-China Association and the Chinese University of Hong Kong remains strong to this day.

After the resumption of normal diplomatic relations with China in the 1970s, Yale-China explored the possibility of academic exchanges with a number of Chinese universities. In the fall of 1980, the association resumed its program of sending recent Yale College graduates to teach in mainland China and inaugurated a program of scholarly exchanges between faculty of the Yale School of Medicine and Xiangya.



Yale-China Teaching Fellow Max Gladstone (B.A. 2006) meets with students after class at Xiuning Middle School in rural Anhui province. Max is one of twenty Teaching Fellows that Yale-China placed in China in 2007.



Japan's invasion of China in 1937 and the ensuing war placed severe strains on the Yale-China Association's ability to operate. Surgeon Phillips Green is seen placing a U.S. flag on the roof of the Xiangya Hospital, 1937. Until the bombing of Pearl Harbor in 1941, Japanese bombers generally avoided targeting American property.

In the nearly three decades since the Yale-China Association resumed its programs in mainland China, the association's activities have expanded to include a host of new initiatives in new locations. Ventures between the association and China include programs in legal education, American Studies, HIV/AIDS education and prevention, community health education, health care for the underserved, and educational and cultural exchange for Yale students and their Chinese counterparts. Yale-China draws support from numerous generous benefactors, including Mrs. Katharine R. Lyman, the widow of Richard S. Lyman (B.A. 1913), whose 1994 gift to Yale University directed a portion of the bequest to the Yale-China Association.

Yale-China's work reaches dozens of members of the Yale community and thousands of people in China each year. Yale-China currently sponsors twenty Yale graduates serving as Yale-China Teaching Fellows, and in the summer of 2007 sent eleven Yale undergraduates to China to intern at non-profit organizations. In addition, more than fifteen faculty members from the Yale Schools of Nursing, Medicine, Public Health, and Law, as well as the Yale Teacher Preparation Program, will participate in Yale-China programs this year. True to its roots, the Yale-China Association continues to serve as a bridge for students and educators in the Yale community and their colleagues in China.



Hongping Tian, director of health programs in the Yale-China Association, receives a gift of paintings from a Chinese student whose school participates in a nutrition education program organized by the association.



The founders of medical operations of the Yale-China Association, Drs. F.C. Yen and Edward Hume (first and second from right) are seen with officials of the Hunan government soon after the association was created in 1901. Attempts were made from the start to bring as many Chinese faculty and administrators on board as possible.

Real Assets

Real estate, oil and gas, and timberland share common characteristics: sensitivity to inflationary forces, high and visible current cash flow, and opportunity to exploit inefficiencies. Real asset investments provide attractive return prospects, excellent portfolio diversification, and a hedge against unanticipated inflation. Yale's 28.0 percent long-term policy allocation significantly exceeds the average endowment's commitment of 10.1 percent. Expected real returns are 6.0 percent with risk of 13.6 percent.

The real assets portfolio plays a meaningful role in the Endowment as a powerful diversifying tool and a generator of strong returns. Real assets provide relative stability to the Endowment during periods of public market turmoil. Pricing inefficiencies in the asset class and opportunities to add value allow superior managers to generate excess returns over a market cycle. Since inception in 1978 the portfolio has returned 17.8 percent per annum.

The illiquid nature of real assets combined with the expensive and time-consuming process of completing transactions create a high hurdle for casual investors. Real assets provide talented investment groups with the opportunity to generate strong returns through savvy acquisitions and managerial expertise. A critical component of Yale's investment strategy is to create strong, long-term partnerships between the Investments Office and its investment managers. In the last decade Yale played a critical role in the development and growth of more than a dozen organizations involved in the management of real assets.

Asset Allocations

	Yale University	Educational Institution Mean
Absolute Return	23.3%	19.5%
Domestic Equity	11.0	26.3
Fixed Income	4.0	12.7
Foreign Equity	14.1	22.1
Private Equity	18.7	7.0
Real Assets	27.1	10.1
Cash	1.9	2.3

Data as of June 30, 2007

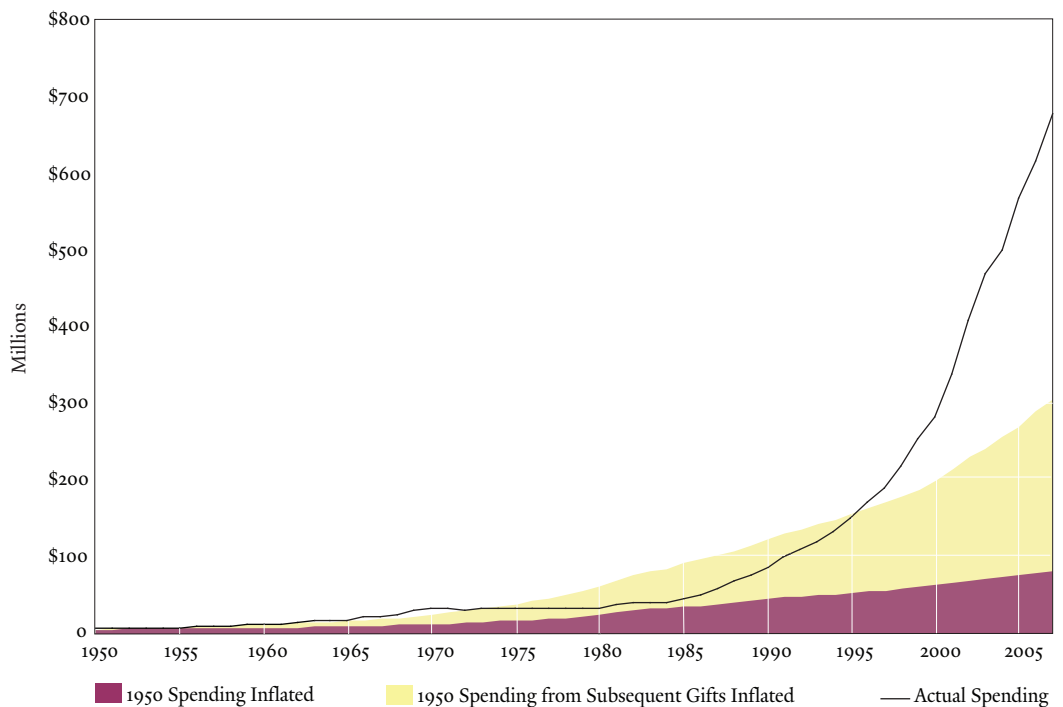
4

The spending rule is at the heart of fiscal discipline for an endowed institution. Spending policies define an institution's compromise between the conflicting goals of providing substantial support for current operations and preserving purchasing power of Endowment assets. The spending rule must be clearly defined and consistently applied for the concept of budget balance to have meaning.

Yale's policy is designed to meet two competing objectives. The first goal is to release substantial current income to the operating budget in a stable stream, since large fluctuations in revenues are difficult to accommodate through changes in University activities or programs. The second goal is to protect the value of Endowment assets against inflation, allowing programs to be supported at today's level far into the future.

Yale's spending rule attempts to achieve these two objectives by using a long-term spending rate of 5.25 percent combined with a smoothing rule that adjusts spending gradually to changes in Endowment market value. The amount released under the spending rule is based on a weighted average of prior spending adjusted for inflation (80 percent weight) and an amount determined by applying the target rate to the current Endowment market value (20 percent weight) with an adjustment factor based on inflation and the expected growth of the Endowment net of spending.

Spending Growth Surpasses Inflation 1950–2007



Endowed Support for Yale-China Exchanges

Yale University's interaction with China covers a range of activities involving students, faculty, courses of study, and centers for teaching and research. Since China and the United States re-established diplomatic ties nearly thirty years ago, Yale has stood at the forefront of American universities making commitments to work with their Chinese counterparts. Although Yale receives a range of funding to establish and operate programs with China, endowed funds provide one of the most important sources of support for these activities.

Support for Chinese Studies

Until the improved diplomatic relations between the People's Republic of China and the United States in the 1970s, Yale's endowed funding of Chinese studies remained modest. Older endowed funds concentrated on support for students of Chinese ancestry, the teaching of Chinese language and history, academic prizes, and book acquisitions. The focus of endowed funding changed in 1977, when an endowment from the Andrew W. Mellon Foundation helped to create a program in East Asian studies with an emphasis on China, specifically in the humanities and social sciences. The Mellon Foundation went on to contribute a larger fund for the same purpose in 1986.

Yale's programs in Chinese studies attract international attention and support. In 1991, the Development of Chinese Studies Fund provided a total of \$6 million from the Cheng Yu-tun Foundation and the Lee Shau-kee Foundation, the philanthropic efforts of two well-known Hong Kong businessmen, to endow Chinese studies in various forms: exchanges with the Chinese University of Hong Kong, fellowships, faculty research, library acquisitions, conferences, and financial support for Yale's Council on East Asian Studies. Founded in 1961, the council is just one of several programs that coordinate Chinese studies and programs related to China.

Support for Chinese Students

A number of endowed funds have been established to bring international students and scholars to Yale. The Fan Family Fellowship Endowment (established in 1999 through gifts from Henry H.L. Fan), one of the most extensive programs of this kind, enables several Chinese students each year to complete doctoral, master's, or undergraduate degrees at Yale. The Kenneth and Mary Wang Graduate



S. Wells Williams, who had been a professor of Chinese language and literature at Yale from 1877 to 1884, created the University's first endowed teaching fund for Chinese studies through a bequest in 1903.

Fellowship Fund (1992) makes grants to students from China "who intend to return to their homeland upon completion of their degree." Similar endowed funds include the Kwok Family Scholarship Fund (2000) for both graduate and undergraduate students, the Undergraduate Scholarship Fund for Chinese and Singaporean Students (1999, the gift of Yale College parent Robert C. Ng), the Yale College Dean's Discretionary Fund for Asian and International Students (2003),

and the Sally and Bob Gries Scholarship Fund (2005) for undergraduates (created in 2005 by Robert D. Gries, B.A. 1951).

Donors have created endowments specifically earmarked for Chinese students in professional schools at Yale. A bequest from Ping The Sie (B.D. 1952) established a scholarship in the Divinity School for a Chinese student in 1988. Young artists from China can seek support at the Yale School of Art from the Andrea Frank Foundation Sanyu Scholarship Fund, established by the Frank Foundation in 1998 in honor of Chinese artist Sanyu (1900 -1966). The Laura Cha (Shi Mei Lun) Scholarship at the Yale School of Management (2005) awards merit-based financial aid to one M.B.A. student from mainland China every other year. Other Yale School of Management scholarships include the Kevin Y. Zhang Scholarship Fund (2006), created by Mr. Zhang, M.B.A. 1994, who came to SOM from China. His fund is intended to increase the international diversity of the student body by providing half-tuition for a student from mainland China.

Support for Student Travel and Exchanges

Today, Yale undergraduates and graduate students can apply for a number of fellowships for study, research, or employment in China for durations that range from a few weeks to more than a year. Mrs. Richard S. (B.A. 1913) Lyman set up the Yale-China Fund (1994) to support students who go to



Yale's longstanding ties to China, and continuing financial support for the Yale-China Association, helped the University to step up activity promptly following the thaw in U.S.-China relations in the 1970s. Yale Professor of Surgery Bernard Lytton is seen lecturing at Hunan Medical College in 1983.

The spending rule has two implications. First, by incorporating the previous year's spending, the rule eliminates large fluctuations, enabling the University to plan for its operating budget needs. Over the last twenty years, annual changes in spending have been a third as volatile as annual changes in Endowment value. Second, by adjusting spending toward the long-term target spending level, the rule ensures that spending will be sensitive to fluctuating Endowment market values, providing stability in long-term purchasing power.

Despite the conservative nature of Yale's spending policy, distributions to the operating budget rose from \$191 million in fiscal 1997 to \$684 million in fiscal 2007. The University projects spending of \$843 million from the Endowment in fiscal 2008, representing 37 percent of revenues.

China to study or teach through programs of the Yale-China Association. The Raymond (B.A. 1975) and Nora Wong Summer Travel Fellowship Fund (2005) provides funding for students to study, work, travel, or conduct research in China. A separate endowment, the Light Fellowship, founded in 1997 by Dr. Richard Upjohn Light (B.A. 1924), has sent hundreds of Yale students to China for language studies.

The Schoen Foreign Study Fund, endowed through a gift from Scott A. Schoen (B.A. 1980) and Laurie G. Schoen, provides support for the Peking-Yale Joint Undergraduate Program, which also receives funding from individual contributions of Yale alumni and parents. Founded in 2005, the program enables Yale College students and their counterparts at Peking University to study and live together in Beijing. Yale College students selected for the program take a full course load taught in English by Yale and Peking University faculty and receive full Yale credit toward their degrees.

University benefactors have provided a wealth of support for a broad range of student exchanges. The Pao-Watari Fund for East Asian Studies (2005) supports internships for Yale students in non-profit educational and public policy organizations in China as well as Chinese and East Asian students who wish to come to New Haven for a period of study. This fund was established in 2005 through a gift from Ms. Cissy Pao and Mr. Shinichiro Watari, parents of Yale College students (2001 and 2005). For graduate study, Shanghai's Fudan University participates in a yearlong

international exchange under Yale's Fox Fellowship Program (established in 1988 by Joseph Carrère Fox, B.A. 1938), which sends Yale graduate students to China and brings Chinese students to Yale. The Fox program is an important vehicle for the University's projects with China and has continued to expand in recent years thanks to new endowment funding from Mr. Fox and other contributors.

Demand from the Yale community for access to Chinese studies and exchanges with China has increased dramatically over the last decade. The University continues to seek endowed funding to maintain and expand its vital work with China. For Yale – and for its generous benefactors – these funds provide an opportunity to make a profound impact on the future of United States, China, and the world.



Alexander Millman (B.A. 2006) interviews a Chinese resident of Yunnan province as a part of the Yale-China Service Internship Program. The program receives support from the Pao-Watari Fund, which was established in 2005 by a gift from Ms. Cissy Pao and Mr. Shinichiro Watari, parents of Yale College students (2001 and 2005).

Chinese Art at Yale

The Chinese Collection at the Yale University Art Gallery was initiated in 1837 with a painting of David Wooster by an unknown Chinese artist. Building on this humble beginning, the Chinese collection grew steadily over the next 170 years through the gifts of alumni collectors, such as Frederick Wells Williams (B.A. 1879), one of the founders of the Yale-China Association.

The Yale-China Association indirectly facilitated the establishment of one of Yale's most extraordinary collections of Chinese art, a collection of ceramics from the Changsha region of south central China. In the mid 1930s, while spending two years teaching English on the Yale-China Association campus in Changsha, John Hadley Cox (B.A. 1935) witnessed the leveling and excavation of a large area just outside the city. The excavation uncovered numerous tombs and artifacts. Although Cox had no formal training in art or archaeology, he recognized the significance of the findings and began to amass an extensive collection.

Toward the end of his tenure in Changsha, Mr. Cox proposed a gift of forty ceramics to Yale in the hopes of stimulating an interest in "things Chinese" at the University. Yale enthusiastically accepted. Over the next several decades, Yale's Changsha ceramics collection grew to more than 200 pieces through the continued generosity of Mr. Cox and the financial support of Ada Small Moore (also known as Mrs. William H. Moore).

The Changsha ceramics collection documents the evolution of Chinese ceramics in the Changsha region from the third century B.C.E. to the fourteenth century C.E.. One of the most notable pieces in the collection is a ceramic model of a Chinese



Ceramic model of a Chinese dwelling, which dates to the Eastern Han dynasty (first to second century C.E.). The single-storied, L-shaped house is an example of a Han mortuary object. Changsha ceramics collection.

dwelling, which dates back to the Eastern Han dynasty (first to second century C.E.). The single-storied, L-shaped house is an example of a Han mortuary object, which is meant to facilitate the deceased's transition to the afterlife. The house provides Yale scholars and their colleagues with important information about the construction of dwellings during the Eastern Han period, as well as clues about attitudes

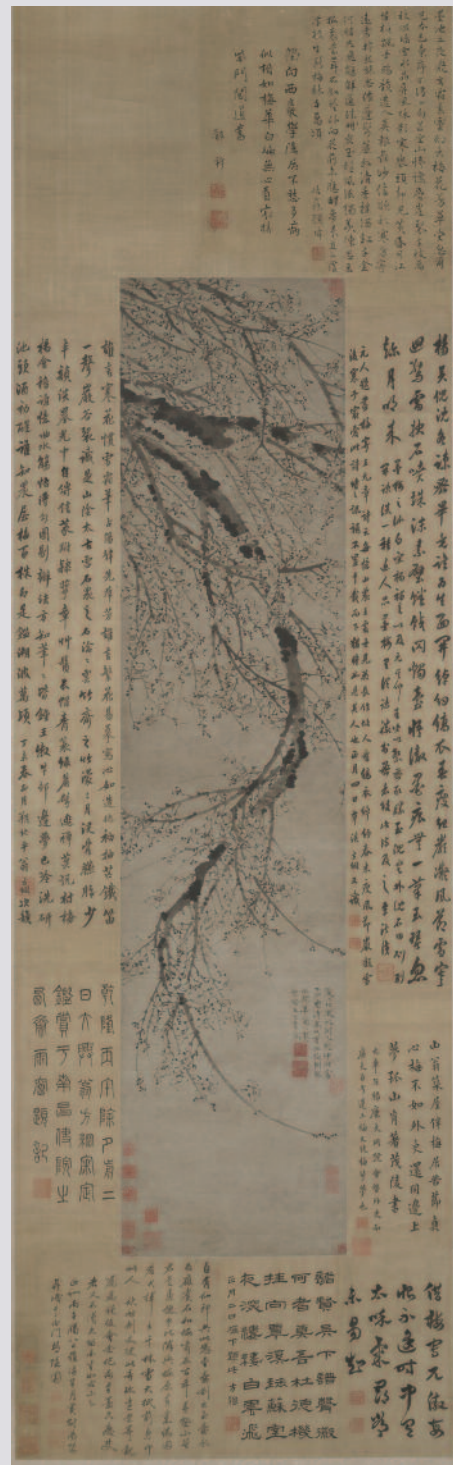


Finial or pole top (ca. 1300–1050 B.C.E., Shang dynasty, YinXu period, thirteenth to eleventh century B.C.E.), bronze. Hobart and Edward Small Moore Memorial Collection, gift of Mrs. William H. Moore. Two heads, one human and one animal, are joined back-to-back to constitute the upper half of this finial.

toward death, which, as the Han dynasty progressed, shifted from the pursuit of transcendent immortality toward a more materialistic approach that emphasized the continuation of the comforts of worldly life.

In addition to supporting Yale's efforts to enlarge its collection of Changsha ceramics through monetary donations, Ada Small Moore made generous gifts to the Art Gallery from her extensive collection of Chinese art. Traveling frequently to East Asia with only her Irish maid in tow, Mrs. Moore was an intrepid woman. In 1937 she donated her collection of Chinese textiles to the University in memory of her son, Hobart Moore (B.A. 1900). Over the next eighteen years until her death in 1955, Mrs. Moore continued to give works from her collection. In 1953 the name of the collection changed to include Edward Small Moore (Yale 1900-1903), her second son.

The gifts of Ada Small Moore and her family are central to Yale's collection of Chinese art and include a number of



Wang Mian (Chinese, died 1359), *Ink Plum* (undated; ca. 1350s), hanging scroll, ink on paper. From the Hobart and Edward Small Moore Memorial Collection, a gift of Mrs. William H. Moore. Paintings of plum executed in ink developed as a genre of painting particularly associated with scholars during the late Northern Song period at the end of the eleventh and the beginning of the twelfth century.



Portrait of Du Yan, one of the Five Old Men of Suizhang (before 1056, Northern Song dynasty, 960–1126), ink and color on silk. From the Hobart and Edward Small Moore Memorial Collection, a gift of Mrs. William H. Moore. The colophons range from 1056 to 1898, making this one of the most extensively documented paintings in the history of art.

notable pieces that span many dynasties. One of the oldest pieces in the Hobart and Edward Small Moore Memorial Collection is a finial/pole top dating back to the Shang dynasty (sixteenth to eleventh century B.C.E.) of China's Bronze Age. Two heads, one of a man and one of a tiger, are fused back to back to form a striking ornament. The collection also includes a number of important paintings, of which one of the most significant is Wang Mian's *Ink Plum*, a hanging scroll dating to the 1350s. The artist's images of plum blossoms cascading in S-curves painted in ink combined with poems gave definitive shape to the genre of ink plum blossom painting. Wang Mian's poetry and paintings expressed deep

resentment toward the conquering Mongols of the Yuan dynasty, a sentiment that was common among Chinese scholars of that era.

Over the last several decades, gifts have added substantially to the Art Gallery's holdings of Chinese art. In 1982 the support of alumni and anonymous benefactors helped Yale acquire *Reminiscence of the Jian River*, a hanging executed in ink and color on paper by Dong Qichang, one of the most important painters and theorists in the history of later Chinese painting.

The Chinese collection at Yale currently contains roughly 2,500 pieces, many of which were given or financed by alumni, foundations, and the Art Gallery's other

generous benefactors. Yale's Asian art collection is administered by two dedicated curators, one supported by a gift from Ruth and Bruce Dayton (B.A. 1940) and the other by The Japan Foundation Endowment through the Council on East Asian Studies. The collection not only serves as an important teaching tool for the University, but also draws acclaim and appreciation from the public and will undoubtedly continue to inspire generations of students as well as Chinese art enthusiasts, collectors, and researchers.



Dong Qichang (1555–1636), *Reminiscence of Jian River* (ca. 1621), hanging scroll, ink, and color on paper. Gift of Leonard C. Hanna, Jr. (B.A. 1913), and Mrs. Paul Moore, and the Anonymous Oriental Purchase Fund. Dong Qichang was the most important painter and theorist in the history of later Chinese painting.

Investment Performance

5

Performance by Asset Class

Yale has produced excellent investment returns. Over the ten-year period ending June 30, 2007, the Endowment earned an annualized 17.8 percent return, net of fees, placing it in the top one percent of large institutional investors. Endowment outperformance stems from sound asset allocation policy and superior active management.

Yale's long-term superior performance relative to its peers and benchmarks has created substantial wealth for the University. Over the ten years ending June 30, 2007, Yale added \$11.0 billion relative to its composite benchmark and \$11.9 billion relative to the average return of a broad universe of college and university endowments.

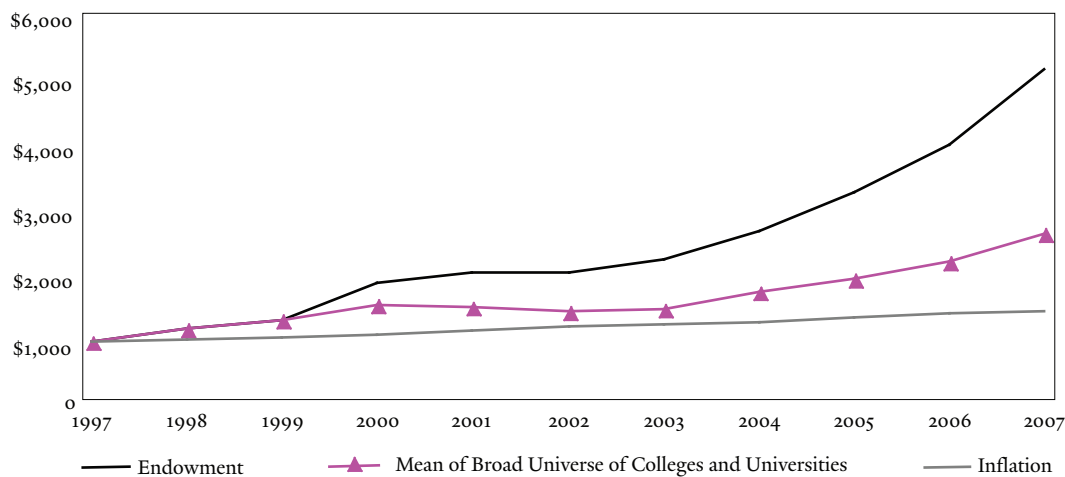
Yale's long-term asset class performance continues to be outstanding. In the past ten years every asset class posted superior returns, significantly outperforming benchmark levels.

Over the past decade, the absolute return portfolio produced an annualized 13.1 percent, exceeding the passive benchmark of the One-Year Constant Maturity Treasury plus 6 percent by 2.5 percent per year and besting its active benchmark of hedge fund manager returns by 1.5 percent per year. For the ten-year period, absolute return results exhibited essentially no correlation to traditional marketable securities.

For the decade ending June 30, 2007, the domestic equity portfolio returned an annualized 13.5 percent, outperforming the Wilshire 5000 by 5.8 percent per year and the Russell Median Manager return by 5.4 percent per year. Yale's active managers have added value to benchmark returns primarily through stock selection.

Yale's internally managed fixed income portfolio earned an annualized 6.4 percent over the past decade, exceeding the Lehman Brothers Treasury Index by 0.6 percent per year and the Russell Median Manager return by 0.5 percent per year. By making astute security selection decisions and accepting illiquidity, the Endowment benefited from excess returns without incurring material credit or option risk.

Yale's Performance Exceeds Peer Results
1997 to 2007, 1997 = \$1,000

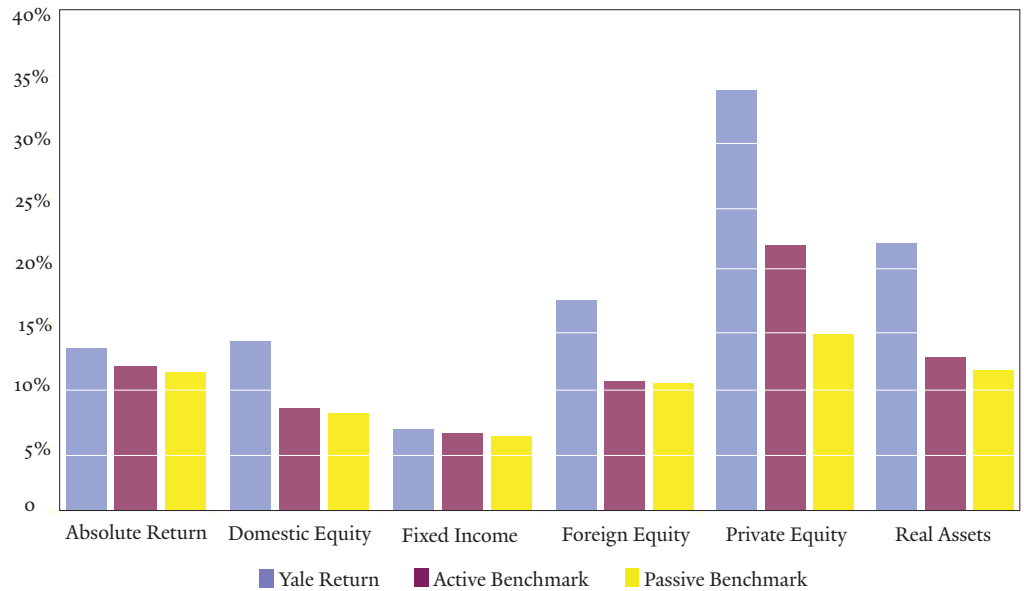


The foreign equity portfolio generated an annual return of 16.9 percent over the ten-year period, outperforming its composite benchmark by 6.8 percent per year and the Russell Median Manager return by 6.2 percent per year. The portfolio's excess return is due to effective security selection and country allocation by active managers.

Results from Yale's non-marketable assets demonstrate the value of superior active management. Private equity earned 33.9 percent annually over the last ten years, outperforming the passive benchmark of University inflation plus 10 percent by 19.2 percent per year and the return of a pool of private equity managers compiled by Cambridge Associates by 12.8 percent per year. Since inception in 1973, the private equity program has earned an astounding 31.4 percent per annum.

Real assets generated a 21.5 percent annualized return over the ten-year period, outperforming the passive benchmark of University inflation plus 6 percent by 11.5 percent per year and an active benchmark of real assets manager returns by 7.6 percent per year. Yale's outperformance is due to the successful exploitation of market inefficiencies and timely pursuit of contrarian investment strategies.

Yale Asset Class Results Trounce Benchmarks 1997 – 2007



Active Benchmarks

Absolute Return: CSFB Composite
Domestic Equity: Frank Russell Median Manager, U.S. Equity
Fixed Income: Frank Russell Median Manager, Fixed Income
Foreign Equity: Frank Russell Median Manager Composite, Foreign Equity
Private Equity: Cambridge Associates Composite
Real Assets: NCREIF and Cambridge Associates Composite

Passive Benchmarks

Absolute Return: 1-year Constant Maturity Treasury + 6%
Domestic Equity: Wilshire 5000
Fixed Income: Lehman Brothers Treasury Index
Foreign Equity: MSCI EAFE Index and MSCI EM Index Composite
Private Equity: University Inflation + 10%
Real Assets: University Inflation + 6%

President Hu Jintao and the Yale 100 Delegation

In April 2006, Chinese President Hu Jintao paid Yale University an historic visit. Citing China's relationship with Yale as evidence of a long-standing mutual admiration between China and the United States, President Hu stressed that Yale, by serving as an academic, cultural, and social link between the two countries, was in a unique position to foster amicable ties between the American and Chinese peoples.

In the spirit of advancing "mutual understanding between our two countries and especially between our young people," President Hu concluded his speech by inviting one hundred Yale students, faculty, and administrators to visit China. Enthusiastically accepting this unprecedented invitation, the University spent a full year preparing for the trip. The Yale 100 set off for China in May 2007.

Intended to provide a multi-faceted introduction to China, the ten-day trip blended official meetings with informal interactions and featured visits to multiple cities. President Hu welcomed his guests on their arrival with a formal banquet at the Great Hall of the People in Beijing. Following the reception, the Yale delegation visited Peking and Tsinghua Universities to discuss education policy with administrators and students. The Yale 100 visited the Forbidden City and the Olympic Stadium, followed by a feast of Peking duck and a performance of Beijing opera. On their last day in Beijing, the delegates toured a museum dedicated to Zhan Tianyou (P.H.B. 1881), the "father of the Chinese railroads." There, the Yale 100 found plenty to remind them of home, from Zhan's 1881 senior essay to nineteenth-century images of the familiar stained glass window in Linsley-Chittenden 102.

The Yale delegation's Chinese hosts arranged for an extended trip outside the capital city. First on the stop was Xi'an, where Yale students got a glimpse of a typical Chinese household. After a visit to see the terracotta warriors and a day in the rural outskirts of the city, the Yale 100 proceeded to Shanghai, where delegation members marveled at the scale of construction and the energy of the city's stock exchange.

President Levin described the experience as an "extraordinary journey" and encouraged members of the Yale delegation to consider returning to China for work or scholarship. Without a doubt, the Yale 100 will not soon forget their exceptional introduction to China.



President Hu Jintao visited Yale on April 21, 2006, to give an address in Sprague Memorial Hall to students and faculty. President Hu also met with Yale President Richard C. Levin, who during one of his six visits to China in recent years invited President Hu to visit Yale. Addressing a crowd of Yale College students, President Hu said, "If time could go back several decades, I would really like to be a student of Yale just like you." The Chinese President's historic visit continued the close interactions between Yale and China going back many years.



Wendy Sharp, Director of Chamber Music at the Yale School of Music, and Jody L. Sindelar, Professor of Epidemiology and Public Health, during the Yale 100 tour.



In Beijing, a waiter serves tea to President Richard Levin, center, and Senior Lecturer Jane Levin in dramatic fashion.



A delegation of 100 Yale students, faculty members, and administrators made a ten-day trip to China in May 2007, responding to the official invitation of President Hu Jintao in the conclusion to his address at Yale the year before. The trip was intended, said President Hu, to advance "mutual understanding between our two countries and especially between our young people."

Management and Oversight

6

Since 1975, the Yale Corporation Investment Committee has been responsible for oversight of the Endowment, providing senior-level governance over investment management activities. The Investment Committee consists of at least three Fellows of the Corporation and other persons who have particular investment expertise. The Committee meets quarterly, at which time members review asset allocation policies, Endowment performance, and strategies proposed by Investments Office staff. The Committee approves guidelines for investment of the Endowment portfolio, specifying investment objectives, spending policy, and approaches for the investment of each asset category. Twelve individuals currently sit on the Committee.

Investment Committee

Charles D. Ellis '59, Chairman
*Former Managing Partner
Greenwich Associates*

Henry F. McCance '64
*Chairman
Greylock Management*

G. Leonard Baker '64
*Managing Director
Sutter Hill Ventures*

Jane L. Mendillo '80, '84 MBA
*Chief Investment Officer
Wellesley College*

Joshua Bekenstein '80
*Managing Director
Bain Capital*

William I. Miller '78
*Chairman
Irwin Financial Corporation*

Shauna King
*Vice President Finance & Administration
Yale University*

Honorable Barrington Parker
'66, '69 LL.B.
*Judge
United States Court of Appeals
for the Second Circuit*

James Leitner '75
*President
Falcon Investment Management*

Douglas A. Warner, III '68
*Former Chairman of the Board
J.P. Morgan Chase & Co.*

Richard C. Levin '74 PH.D.
*President
Yale University*

Fareed Zakaria '86
*Editor
Newsweek International*

The Investments Office manages the Endowment and other University financial assets, and defines and implements the University's borrowing strategies. Headed by the Chief Investment Officer, the Office currently consists of nineteen professionals.

Investments Office

David F. Swensen '80 PH.D.
Chief Investment Officer

Anne Martin
Associate Director

Dean J. Takahashi '80, '83 MPPM
Senior Director

Suzanne K. Wirtz
Associate Director

Alexander C. Banker
Director

David B. Slifka '01
Senior Associate

Alan S. Forman
Director

Celeste P. Benson
Senior Portfolio Manager

Timothy R. Sullivan '86
Director

Carrie A. Abildgaard
Senior Financial Analyst

Deborah S. Chung
Associate General Counsel

Nicholas T. Shalek '05
Senior Financial Analyst

Kenneth R. Miller '71
Associate General Counsel

Xiaoning Wu '04
Senior Financial Analyst

Peter H. Ammon '05 MBA, '05 MA
Associate Director

R. Alexander Hetherington '06
Financial Analyst

Michael E. Finnerty
Associate Director

Matthew S. T. Mendelsohn '07
Financial Analyst

Randy Kim '98, '04 MBA
Associate Director



Autumn on the Old Campus, with the statue of Rector Abraham Pierson (1641/5-1707), Yale College's first rector, who served from 1701 to 1707.

The Qualified Foreign Institutional Investor Program

For over a decade after its establishment in December 1990, the Chinese public equity market was essentially closed to foreign investors. In late 2002 the Chinese government initiated the Qualified Foreign Institutional Investor (QFII) program, allowing a limited group of non-Chinese institutions to own domestically listed companies, also known as A-shares.

The China Securities Regulatory Commission and the State Administration of Foreign Exchange (SAFE), two bodies that govern financial markets and currency flows, set an initial quota of \$4 billion to be divided among approved QFII participants. Interest in the QFII was high; foreign investors soon consumed the existing quota and in 2005, in recognition of the heavy investor demand for access to A-shares, the Chinese government approved an expansion of the QFII quota to \$10 billion.

Yale's application for \$50 million in A-share quota was approved on April 14, 2006, making the University the first foreign educational institution to receive a QFII license. As of August 2007, Chinese authorities have approved 51 QFII participants with quotas that aggregate to the maximum allowable of \$10 billion.

A strong market environment and superior active management led the Endowment's A-share investments to appreciate significantly. In fiscal 2007, Yale's A-share portfolio outperformed the market by a healthy margin, no easy feat in a year when the Morgan Stanley Capital International A-share Index returned a jaw-dropping 196%. With approximately 1,400 listed companies, many of which are unknown to foreign investors, the A-share market is particularly well suited to Yale's approach of pursuing research-intensive active management of publicly traded equities.

Yale holds a concentrated portfolio of A-share companies run by exemplary management teams that are uniquely positioned to benefit from China's economic growth. Two such holdings are department store operator Guangzhou Friendship Company and construction machinery manufacturer Changsha Zoomlion. Guangzhou Friendship Company is a premier shopping destination for luxury goods, a market that has grown tremendously in the past decade. Friendship's department stores benefit from occupying prime locations in the city, providing the company with a key advantage over competitors.



Cubicles for traders at the Shanghai Stock Exchange. The Yale 100 tour in May 2007 (discussed on page 22) included a visit to the exchange.

Located in the Hunanese city where the Yale-China Association* established its headquarters, Changsha Zoomlion was founded by Dr. Zhan Chunxin in 1992 as a small division of the Changsha Construction Machinery Research Institute. Buoyed by China's infrastructure boom, Zoomlion has seen demand for its products soar. The company is headed by a savvy management team that has built strong sales channels and fostered an environment that encourages technology research and development. Zoomlion's focus on innovation and efficiency have led to impressive earnings growth.

Market volatility will undoubtedly occur (and oftentimes quite violently) in emerging markets like China. Yale's long-term

investment perspective enables the University to take a contrarian view, with the recognition that market fluctuations do not affect the fundamental strengths of good businesses. In addition to maintaining a disciplined, long-term focus, Yale emphasizes fundamental research, which is imperative to understanding and navigating largely unexplored emerging markets. Yale expects to maintain a long-term commitment to Chinese equities.

* Founded in 1901, the Yale-China Association is a private, non-profit organization dedicated to promoting education in China and fostering cooperation between Chinese and American students, academics and professionals. For information about the organization, please see "The Yale-China Association" article in this publication.



On April 14, 2006, Yale became the first foreign educational institution authorized to own domestically listed Chinese companies, also known as A-shares, as attested by this certificate from the China Securities Regulatory Commission and the State Administration of Foreign Exchange (SAFE), two bodies that govern financial markets and currency flows. Yale's portfolio of Chinese shares performed favorably in 2007.

Yale and China Joint Programs

Yale currently maintains more than eighty joint ventures with Chinese universities, facilitating a lively and mutually beneficial series of exchanges in the classroom, laboratory, and studio. The joint ventures provide a platform for innovative research and collaboration across a wide range of academic disciplines. The following programs represent only a handful of Yale's many joint projects with China.

The China Law Center at Yale

Yale Law School spearheaded one of the University's first long-term joint ventures in China. Paul Gewirtz, the Potter Stewart Professor of Constitutional Law at Yale, founded the China Law Center in 1999 to assist China's efforts at judicial reform and increase knowledge of the country's legal system. Led by members of the Law School staff, projects of the China Law Center have focused on efforts by legislatures, scholars, lawyers, and advocates to promote reforms to improve fairness, effectiveness, and rights-protection in China's criminal justice system. The center has worked to encourage positive steps in recent years by China's Supreme People's Court to increase the transparency of court proceedings, strengthen the authority of trial judges, and encourage more active participation by litigants and their lawyers. In addition to the China-based activity, the joint venture created opportunities for Yale students in New Haven: the Workshop on Chinese Legal Reform, a course offered at Yale Law School each fall in conjunction with the China Law Center, provides Yale students and faculty an opportunity to learn about the Chinese legal system.

In 2007, in recognition of the work of the China Law Center of Yale Law School, the William and Flora Hewlett Foundation announced a grant of \$10 million to support the center's operations for five years. The 2007 Hewlett Foundation grant recognizes the Law Center's strong record of accomplishment in designing and carrying out cooperative projects between U.S. and Chinese experts on key issues of Chinese law and policy reform. Yale Law School's China Law Center recently hosted a major academic conference, which focused on sexual orientation and related policy issues. The conference was called "Diversity, Equality and Harmony: International Workshop on Sexuality, Policy and Law" and was held in conjunction with Fudan University in Shanghai in January, 2006.



Yale's China Law Center was established in 1999 by Professor Paul Gewirtz to foster cooperative projects with leading Chinese legal experts in the areas of judicial reform, criminal law, administrative law, regulatory reform, and legal education. Professor Gewirtz, the Potter Stewart Professor of Constitutional Law at Yale, is shown with Zeng Xianyi, then Dean of the Renmin University Law School, during a lecture series in Beijing in 2003 sponsored by the Yale China Law Center.



The China-Yale Advanced University Leadership Program (CYAULP) was initiated in 2004 for presidents and vice-presidents from China's leading universities. It is the most senior group of Chinese university leaders ever to participate in an executive education program outside of China. In collaboration with China's Ministry of Education, the CYAULP was developed in response to the aspiration expressed in 1998 by China's President Jiang Zemin to transform a small number of Chinese institutions into "world-class universities." Participants from China are shown during sessions at Yale in August 2004.

The Fudan-Yale Biomedical Research Center

University President Richard Levin officiated at the opening of The Fudan-Yale Biomedical Research Center on the Fudan University Shanghai campus in November 2003. Under the direction of Professor Tian Xu of the Yale School of Medicine's Genetics Department, this joint initiative of Yale and Fudan University uses model organisms to study developmental biology and human diseases while pursuing three main goals: to perform cutting-edge research and training; to serve as a model for academic reform; and to promote international exchange and cooperation. The center has produced exceptional research, including a project that was featured on the cover of the August 12, 2005 issue of *Cell*, a prominent scientific journal.

The Center has three professors, three associate professors, and approximately twenty postgraduate fellows and doctoral students. Fudan University recently added 10,000 square meters of laboratory space and will provide an auditorium and facilities for the conduct of videoconferences and televisual seminars. The Center's seminar series has hosted sessions with more than forty internationally renowned scholars, including four Nobel laureates in the genetics field.

The Advanced University Leadership Program

In August 2004, Yale welcomed senior administrators from seven of China's top universities for the China-Yale Advanced University Leadership Program. In the first event of its kind outside of China, Yale and the Chinese Ministry of Education sponsored a two-week training program for Chinese university administrators on a broad range of topics, including faculty recruitment, department structure, and endowment management. In 2005, the program was again held at Yale and in 2006, the program continued for a third year in China. The Advanced University Leadership Program reinforced long-standing ties between Yale and China, providing further evidence of Yale's commitment to work hand-in-hand with the Chinese university community.

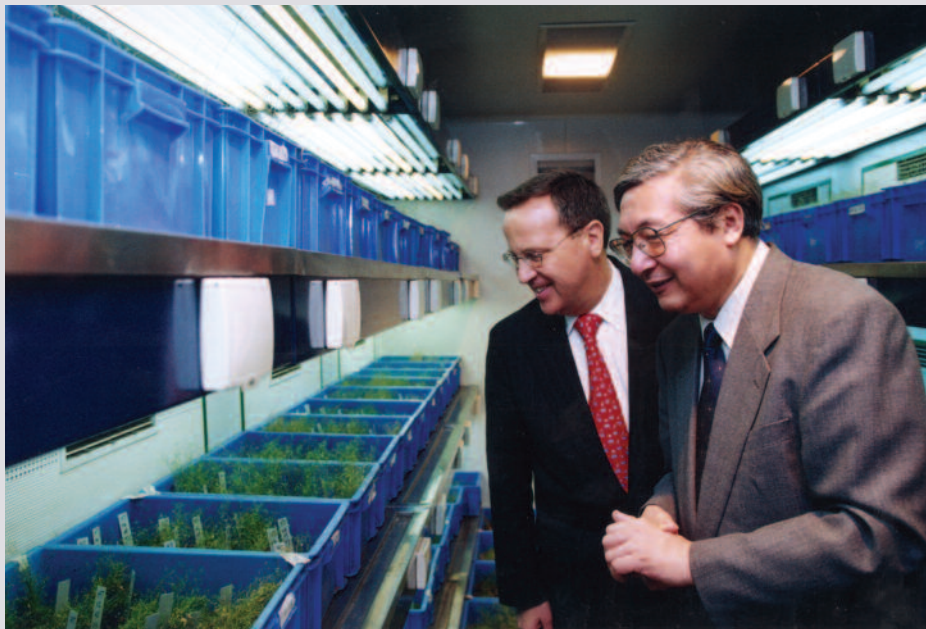
The Peking-Yale Joint Center for Microelectronics and Nanotechnology

In fall 2005, Yale and Peking University launched a joint research center in microelectronics and nanotechnology. Combining the expertise of faculty members from both universities with the facilities and human resources of Peking University, the Peking-Yale Joint Center for Microelectronics and Nanotechnology supports a multidisciplinary research program in which independent research groups work within a common facility, sharing resources and expertise. The center engages in the synthesis, manipulation, measurement, analysis, and modeling of electronic materials and devices on a molecular scale. Funding comes from the two sponsoring universities and the local municipality in which it operates. Efforts are under way to procure additional support from industrial sponsors as well as individual donors.

Yale is committed to building lasting partnerships with Chinese universities. Yale's joint programs with Chinese universities facilitate robust intellectual exchange, allowing students, researchers, and professors from the United States and China to explore new frontiers in the sciences and humanities.

The Yale School of Management and China

A number of professors from the Yale School of Management (SOM) conduct research on topics in Chinese finance, including: William Goetzmann, who researches the development of corporations in pre-revolutionary China; Chen Zhiwu, who collaborates with colleagues from several Chinese universities and institutions to study market efficiency and the history of capital markets in Greater China; and Lode Li, who analyzes supply-chain management issues in Hong Kong and other East Asian countries. SOM provides students an opportunity to study the Chinese business environment first-hand through the International Experience China Trip. Established in 2006, the trip allows approximately twenty students, led by Professor Zhiwu Chen, to meet with business and government leaders in Beijing and Shanghai for a period of ten days. In 2008, Yale SOM will present an educational program for senior executives set to take place against the historical backdrop of the Beijing Olympics. The program will feature some of Yale's leading professors on China business issues, leadership, globalization, economics, and competitive strategy, as well as several of the world's most prominent CEOs.



Since 2001, Yale has established four joint centers for cooperative teaching and research in the biological sciences with Peking University and with Fudan University in Shanghai. Here President Levin is shown touring the Peking-Yale Joint Center for Plant Molecular Genetics and Agro-Biotechnology, in Beijing, with its director, Professor Xing-Wang Deng, the Daniel C. Eaton Professor of Plant Biology at Yale.

Sources

Financial and Investment Information

Much of the material in this publication is drawn from memoranda produced by the Investments Office for the Yale Corporation Investment Committee. Other material comes from Yale's financial records, Reports of the Treasurer, and Reports of the President.

Pages 6-7, 10-11, 14

Educational institution asset allocations and returns from Cambridge Associates.

Page 20

The Endowment's annual return for the ten years ending June 30, 2007 ranks in the top one percent of institutional funds as measured by the SEI Large Plan Universe.

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Information from Yale Development Office.

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President Hu Jintao and the Yale 100 Delegation

Yale Office of International Affairs
Yale 100 Delegation
Yale Office of Public Affairs

Yale and China Joint Programs

Information from each of the Centers included in the report
Yale School of Management
Yale Office of International Affairs

Individuals

The Yale Investments Office expresses appreciation to the following individuals who provided helpful information:

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Yale University Art Gallery

Pages 1, 10, 11, 22 (top and middle), 24, 26 (bottom), inside back cover
Michael Marsland, Office of Public Affairs

Pages 8 (top, painting of Yung Wing by Judith Reeve), 12-13, 16 (bottom), 17
Yale-China Association

Page 8 (bottom), 9, 16 (top)
Sterling Memorial Library Manuscripts and Archives

Pages 18-19
Yale University Art Gallery

Pages 22 (middle, bottom), 25 (top)
Yale 100 Delegation,
Michael Blank, photographer

Page 25 (bottom)
China Securities Regulatory Commission and the State Administration of Foreign Exchange

Page 26 (top)
Yale China Law Center

Page 27
Office of International Affairs

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Strong Cohen/DJP

Opposite page:
Stained-glass windows in Yale Law School.

Back cover:
Bodhisattva Guanyin (1168, Jin dynasty, 1115-1234), polychromed wood with gilt. Gift of Winston F. C. Guest (B.A. 1927). *Guanyin*, Sound Observer, or *Guanshiyin*, the One Who Observes the Sounds of the World, is the Chinese name for Avalokitesvara, the compassionate bodhisattva who has been worshiped throughout the Buddhist world and later became a god of mercy although Guanyin often takes the female form. Guanyin's identifying attribute is the small image of the Buddha Amitabha seen in his crown.



