Performance

	Qtr	CYTD	3-Year	5-Year
USMF Endowment [1]	5.4%	8.9%	(2.0%)	4.5%
80%/20% Portfolio [2]	13.2%	16.8%	(2.8%)	2.1%
60%/40% Portfolio [2]	10.9%	14.2%	(0.2%)	3.1%
S&P 500 Index	15.6%	19.3%	(5.4%)	1.0%

Asset Allocation

	% of Total	Target Range
Global Equities	37%	30% - 60%
Multi-Strategy & Opportunistic	28%	20% - 40%
Real Assets	25%	20% - 30%
Bonds & Cash	9%	5% - 10%

Account Information

USMF Endowment

In $000s	Qtr	FYTD
Beginning MV [3]	$615,627	$615,627
Additions	$10,197	$10,197
Withdrawals	($3,609)	($3,609)
USMF Mgmt Fee	--	--
Other Fees	($1,015)	($1,015)
Investment Gains/Loss	$41,582	$41,582
Ending MV [3]	$662,783	$662,783

Market Review

The explosive rally in global equity markets continued during the third quarter, with all major indices posting double digit gains. Since the March 9th lows, the U.S. market has gained almost 60% while other developed markets are up 75% and emerging markets have rallied 90%. For the 2009 calendar-year-to-date, domestic stocks are now up 20% but remain well under their 2007 highs. The trailing operating P/E on the S&P 500 is around 27x, a huge expansion from March lows and far higher than the typical multiple when the economy enters a recovery phase. This has been the fastest and third largest PE multiple expansion in history. Equities once again appear over-valued and it is unlikely the stock market continues to climb at this pace for very long. On the other hand, we know markets are prone to overshooting and it is possible for a further 'melt-up', especially if one considers the low yields offered in cash and government bonds. Investors may start to reach for returns once again, an all too familiar scenario.

Credit markets have recovered from the crisis environment, as investment grade bonds returned 17% for the year through September, almost matching the yearly gain of U.S. equities but with far less risk. High grade corporate bonds were up 11% for the quarter, bringing the year-to-date return back into positive territory at 5%. Most impressive were the gains of high yield bonds, up 14% for the quarter and 48% for the year. Credit spreads in many areas are now back to pre-crisis levels.

The latest signs of economic recovery are encouraging but not yet cause for unbridled optimism as significant headwinds remain. Third quarter GDP gains were largely due to the stimulus and inventory re-stocking. The consumer remains over-levered and access to credit has been reduced. The Fed faces a difficult challenge in the timing and withdrawal of quantitative easing. It seems plausible consumer borrowing costs will rise when the Fed completes its mortgage purchase plan early next year.

These factors, combined with the consumer's renewed desire to save, act as a drag on growth. The fullest measure of unemployment, the U6 measure that includes all forms of unemployed and underemployed, is now over 17%. This is a record spread to the official rate, which recently topped 10%. If and when employers decide to increase their labor force, before they actually create new jobs they can increase the hours of those who have been furloughed and endured shortened work-weeks. A jobless recovery remains in the cards, adding yet another hurdle for the domestic economy. Amidst such uncertainty, we believe it is prudent to not increase our risk profile significantly at this stage. We remain at the lower end of our range for market exposure and have already realized profits from many of the compelling opportunities that arose earlier in the year.

Portfolio Review

For the quarter ending September 30, the USMF Endowment appreciated 5.4% vs. the 13.2% gain of an 80/20 stocks/bonds portfolio. The Endowment returned 9% so far this year, a strong showing given our lower risk profile and 30% allocation to illiquid long-term investments. We do not expect our strategy to always keep pace with stock markets over a short period, especially during huge rallies such as the one this year. Over a longer period, we aim to provide superior risk-adjusted returns compared to the markets and traditional asset allocation models. We continue to meet this objective, as evidenced by our five year annualized return of 4.5% vs. 1.0% for the S&P 500 and 2.1% for the 80/20 model. During that period of time, the portfolio's volatility was about 2/3rds that of the stock market. We are cognizant that some people will focus on the short-term, despite our annoying insistence that this is not the right time horizon to evaluate our strategy. In order to clarify why we have *not* participated in this rally, here are a few key points regarding our positioning and performance for the year.

In both the public equities and multi-strategy portfolios, the majority of our managers have the ability to increase or decrease their risk profile by adjusting their net market exposure. Many of these managers entered the year with lower gross and net equity exposure compared to prior years. Their short equity positions have significantly detracted from performance as many of our funds tend to short lower quality companies, which have rallied far more than the high quality companies they tend to be long. Earlier in the year, a number of our multi-strategy funds shifted out of equities and into various credit-related investments. At the time, credit investments offered attractive yields and superior downside protection compared to equities. These investments are up substantially since March but lag the rally in stocks. As a result of these moves, the total endowment was at the lower end of its historical exposure to public stocks, but still well within the policy range. Looking back with perfect hindsight, the portfolio could have benefitted from higher equity exposure but we chose to limit risk rather than make a market call.

In addition to a low equities exposure, illiquid investments, particularly in real estate, have been a drag on the near-term results. We are just now receiving the Q3 valuations for our non-marketable funds. These valuations have not been included in the overall performance, but early indications point to a slight increase in market value. Although they were quick to write-down investments, our private equity managers have been slow to mark up their holdings during the recovery, a conservative practice we approve of even though it dampens our short-term performance numbers. Private energy & resources managers are enjoying the upswing of commodity prices in terms of increased cash flow to their companies, but again, they have been slow to mark up these holdings. Unfortunately, real estate is a different story and our managers are coming under increasing pressure from reduced rental income due to higher vacancy and greater leasing concessions.

Finally, we have elected to keep our cash and bonds allocation at the high end of the policy range in order to provide liquidity and flexibility for new opportunities. With short-term yields near 0%, our cash allocation has been a drag on overall performance.

Some of our funds are realizing substantial gains from investments made earlier in the year. Our equity funds are harvesting some profits on the long side and adhering to a disciplined covering process to limit losses on the short side. Within the multi-strategy portfolio we have begun to see a number of profitable exits from high yield, bank debt, and other credit related investments that were bought at distressed prices several months ago. These once-in-a-lifetime opportunities arose during the height of the crisis when panicked investors sold securities at irrational prices. Almost all of these technical pricing gaps have closed. We are now seeing a rotation into securities of distressed companies, which requires a greater degree of skill to assess the risks and potential returns possible in a bankruptcy and restructuring process. There has been a serious reduction in the number of players and capital available to pursue these opportunities, especially outside the U.S., offering an attractive playing field for our experienced managers. Other traditional event-driven strategies, such as merger arbitrage, are also more attractive today and growing as a percentage of the portfolio. We remain focused on public markets and are spending little time looking at private investments.

The investment environment remains highly uncertain. We continue to believe our strategy is the right one for the long-term. We have spent a fair amount of time this year searching for ‘upgrades’ to our current manager roster as well as researching markets that appear to be undervalued and left behind the global rally. Thank you for your support and as always, please feel free to contact the investment office if you have questions, comments, or advice.

Performance by Asset Class

	Qtr	CYTD	3-Year	5-Year
Global Equities	10.6%	12.4%	(2.8%)	3.3%
MSCI World Index	*17.5%*	*24.9%*	*(4.4%)*	*3.5%*
Multi-Strategy & Opportunistic	6.5%	18.3%	2.9%	5.7%
HFR Fund of Funds Index	*4.4%*	*9.8%*	*0.1%*	*3.4%*
Real Assets	14.6%	12.6%	0.7%	15.1%
GSCI Commodities Index	*(1.8%)*	*4.7%*	*(10.8%)*	*(6.7%)*
Bonds & Cash	0.8%	2.6%	3.9%	3.6%
Barclays Aggregate Index	*3.7%*	*5.7%*	*6.4%*	*5.1%*
Total Endowment	5.4%	8.9%	(2.0%)	4.5%
80%/20% Portfolio	*13.2%*	*16.8%*	*(2.8%)*	*2.1%*

Exposures by Security Type [4]

	% of Endowment			
	Long	Short	Gross	Net
Public Equity	41.3%	(15.5%)	56.8%	25.8%
U.S. & Canada	*22.2%*	*(9.5%)*	*31.7%*	*12.7%*
Europe	*8.0%*	*(3.5%)*	*11.5%*	*4.5%*
Japan	*1.4%*	*(0.7%)*	*2.1%*	*0.7%*
Asia Ex Japan	*5.7%*	*(0.8%)*	*6.5%*	*4.9%*
Other Markets	*4.0%*	*(1.0%)*	*5.0%*	*3.0%*
Private Equity	15.4%	---	15.4%	15.4%
Buyouts & Turnarounds	*8.5%*	---	*8.5%*	*8.5%*
Venture & Growth Equity	*2.4%*	---	*2.4%*	*2.4%*
Mezzanine	*1.0%*	---	*1.0%*	*1.0%*
Hedge Fund Side Pockets	*3.5%*	---	*3.5%*	*3.5%*
Real Assets	19.4%	---	19.4%	19.4%
Resources & Infrastructure	*10.5%*	---	*10.5%*	*10.5%*
Real Estate	*8.9%*	---	*8.9%*	*8.9%*
Fixed Income	11.7%	(2.4%)	14.1%	9.3%
Government & Agencies	*1.2%*	---	*1.2%*	*1.2%*
Investment Grade Corporates	*0.8%*	---	*0.8%*	*0.8%*
High Yield	*0.1%*	---	*0.1%*	*0.1%*
Distressed	*5.2%*	*(0.4%)*	*5.6%*	*4.8%*
Structured Products	*2.1%*	---	*2.1%*	*2.1%*
Other	*2.3%*	*(2.0%)*	*4.3%*	*0.3%*
Other	0.6%	(0.3%)	0.9%	0.3%
Total Endowment	88.4%	(18.2%)	106.6%	70.2%
Net Cash [5]	11.6%	---	---	---

Endnotes

1: Private investments market values are as of 6/30/2009 plus contributions and less distributions through 9/30/2009.

2: Benchmark consists of the S&P 500 Index and the 20% Barclays Aggregate Bond, weighted as defined.

3: Accounting values do not match investment performance due to the nature of when the custodian closes records for a period. This typically occurs before all market values have been received.

4: Exposures by Security Type is aggregated data from all managers in the portfolio on a look-through basis.

5: Net Cash represents cash held by individual managers in addition to cash held directly by the Endowment.