

Stanford Management Company

2014 Annual Report

The Stanford Management Company (SMC) was established in 1991 to manage Stanford's financial assets. SMC is a division of the University with oversight by a Board of Directors appointed by the University Board of Trustees. The SMC Board consists of investment professionals, the University president, the University chief financial officer, members of the Board of Trustees, and the SMC chief executive officer. The Board approves SMC asset allocation targets, oversees the hiring of external asset managers, evaluates the performance of SMC investments and professionals, and oversees management of significant portions of endowment, trust assets and expendable funds for the University and the Hospitals.

The majority of the University's endowment assets are invested through the Merged Pool (MP), which is a diversified portfolio of actively managed financial assets valued at approximately \$25.0 billion as of June 30, 2014. To facilitate the comparison of returns with other endowments and foundations, MP performance measurements were calculated on the 12 months ending June 30, 2014. The following discussion of endowment performance relates solely to investments in the MP. The MP realized a 16.8% investment gain for the 12 months ending June 30, 2014. Over the past 10 years, the MP achieved an annualized rate of return of 9.9%, growing from \$10 billion to \$25 billion.

The MP portfolio is constructed on a foundation of modern portfolio theory and strategic asset allocation. The portfolio is designed to optimize long-term returns, create consistent annual payouts to the University's operating budget and preserve purchasing power for future generations of Stanford faculty and students.

SMC, with assistance from its Board of Directors, actively manages the MP, primarily through selecting third-party managers to deploy the MP's capital. Stanford University's brand and SMC's reputation as a stable long-term source of capital enable SMC to gain access to the best third-party managers in the world. Within each business unit, we endeavor to place capital with a diversified set of managers across geographies and investment strategies. SMC also seeks to add value through effective risk management, tactical portfolio rebalancing and opportunistic investment tilts.

STANFORD MP ASSET ALLOCATION

Given the perpetual nature of the University, SMC's investment horizon is long-term. Our objective is to generate maximum total returns for an appropriate level of risk. SMC and the Board regularly reevaluate portfolio asset allocation targets, as well as expected risks, returns and correlations across business units. In addition, SMC reviews positioning relative to long-term policy targets on an ongoing basis and adjusts the portfolio in the context of current market conditions and relative opportunities. The strategic asset allocation targets for the MP as of June 30, 2014 are listed below:

LONG-TERM POLICY TARGETS

Business Unit	Long-Term Policy Target
Public Equity	25%
Private Equity	23%
Absolute Return	22%
Natural Resources	12%
Real Estate	8%
Fixed Income	10%

STANFORD MP PERFORMANCE COMPARED TO INFLATION

The table below outlines annualized returns for various periods ending June 30, 2014.

Business Unit	One-Year	Three-Year	Five-Year	Ten-Year
Nominal Endowment Return	16.8%	9.8%	13.1%	9.9%
GDP Deflator	1.6%	1.6%	1.6%	2.0%
Real Endowment Return	15.2%	8.2%	11.5%	7.9%

STANFORD MP PERFORMANCE COMPARED TO BENCHMARKS

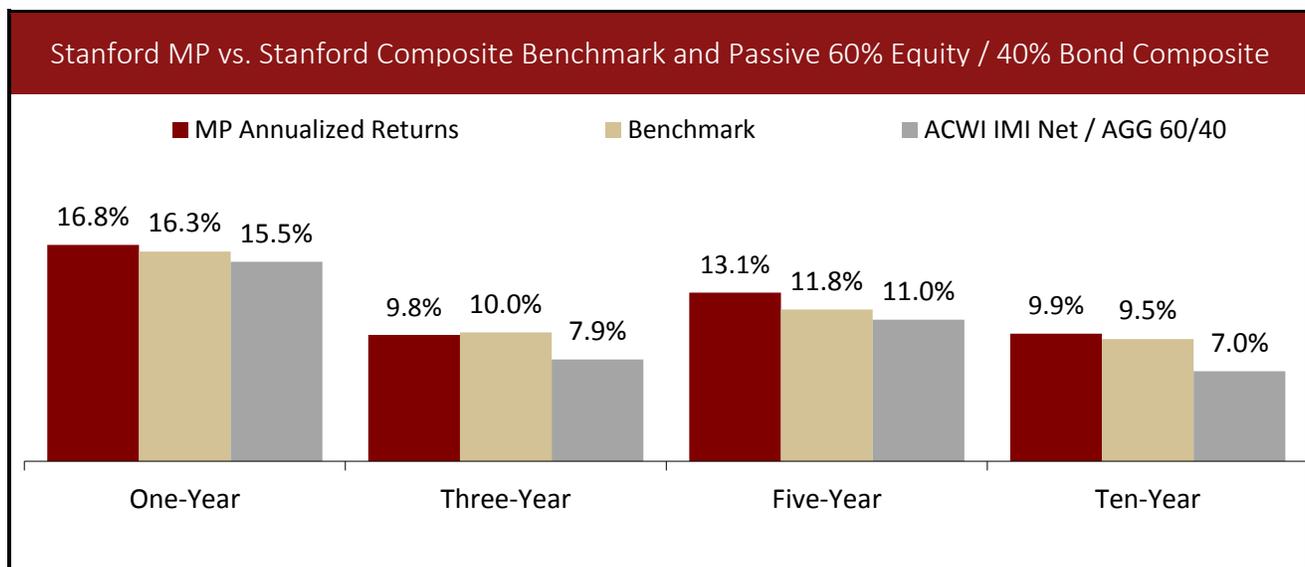
SMC reviews overall MP performance against the composite benchmark return, which represents a blend of the benchmark returns for each business unit weighted by the strategic allocations above. The relative one-year performance of the MP versus the benchmark was 0.5%.

In the 12 months ending June 30, 2014, the Merged Pool (MP) gained 16.8%, continuing a strong recovery since the market bottom in 2009. During the same period, the MSCI ACWI IMI Net Index returned 23.4%, the Barclays Aggregate returned 4.4%, and a 60/40 equity/fixed income mix would have returned 15.5%. Our performance was consistent with our long-term strategic asset allocation which gives us significant exposure to rising markets, while maintaining flexibility and optionality in the case of market volatility.

Diverging global macroeconomic conditions and policy responses have driven returns across the portfolio over the past year. The US economic recovery continues and the S&P 500 returned 24.6% over the year ending June 30, 2014. Economic growth has been weaker in Europe and Japan, but expectations of further stimulus have supported equity markets. Sovereign bond yields across Developed Markets remain low and credit spreads tight. US rates are expected to gradually increase, but how and when the Fed exits this period of unconventional monetary policy is a key question facing the economy and markets.

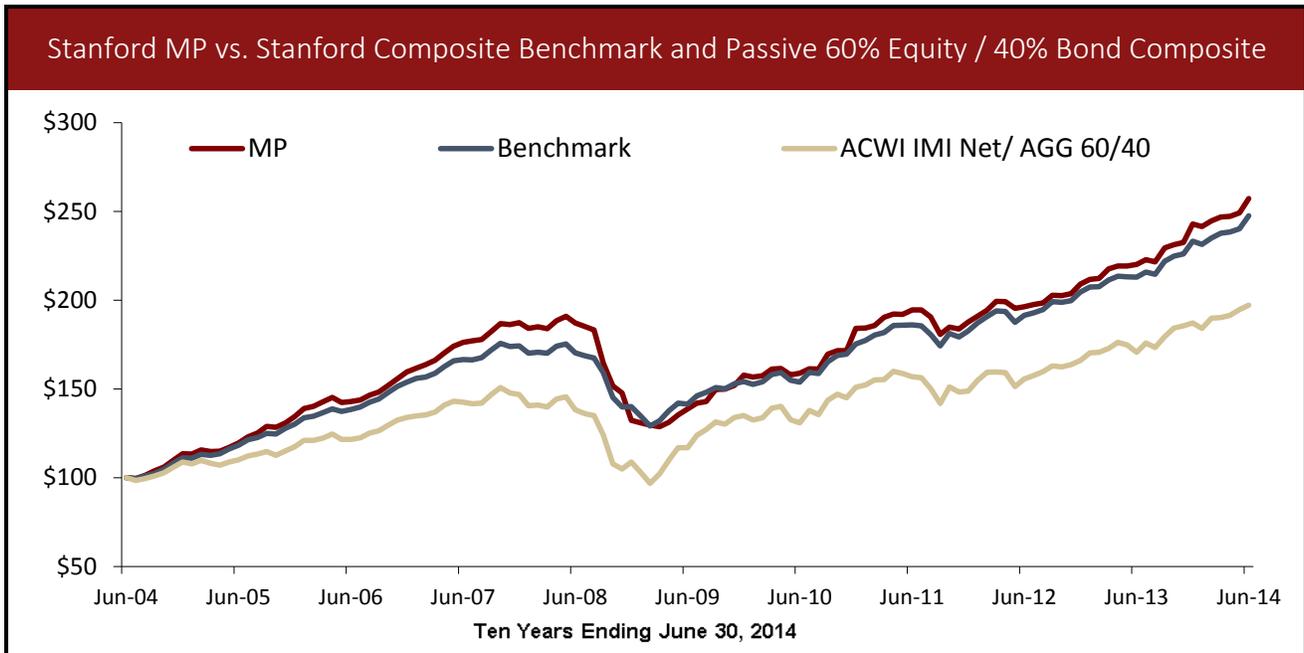
The MP is fully invested across a range of diversified assets and positioned close to policy allocation. The majority of our exposure is through external managers and complemented by direct positions to express more intentional global asset tilts and idiosyncratic opportunities. Within our asset allocation, we are actively positioning to drive alpha and maximize absolute and relative returns over the market cycle. In the table below, actual performance, net of management fees, is compared to the composite benchmark along with a 60% equity / 40% bond portfolio for periods ended June 30, 2014.

STANFORD MP VS. STANFORD COMPOSITE BENCHMARK



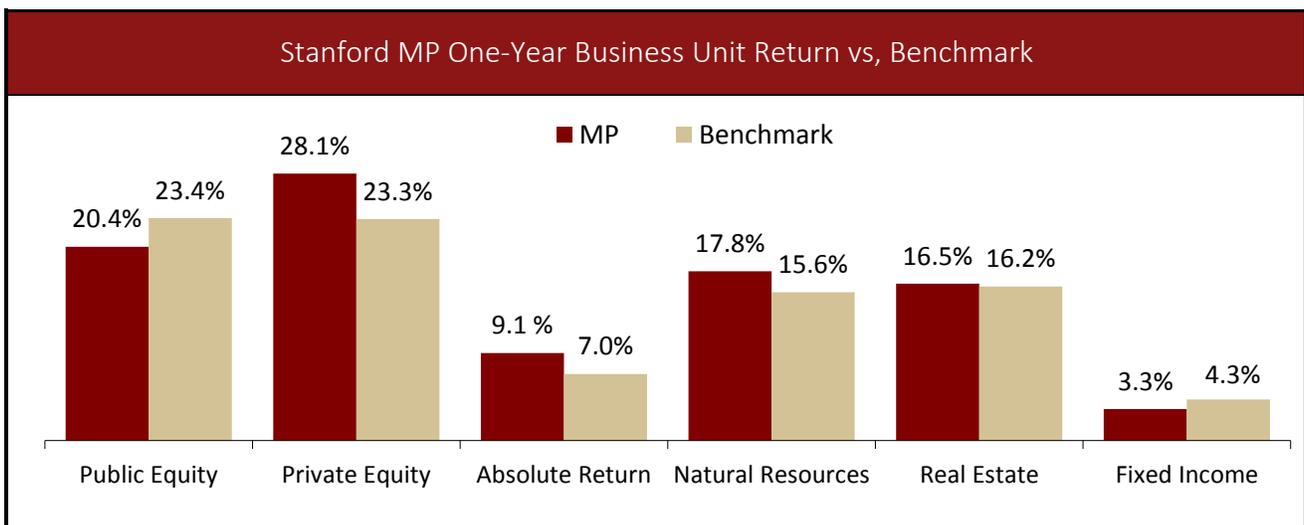
STANFORD MP VS. STANFORD COMPOSITE BENCHMARK AND PASSIVE 60% EQUITY / 40% BOND COMPOSITE

SMC's effectiveness in implementing its investment strategies through top-level manager selection has resulted in consistent and long-term outperformance versus relevant benchmarks. The cumulative return chart below compares the growth of \$100 in Stanford's MP, a composite benchmark portfolio, and a 60% equity / 40% bond portfolio over the past 10 years:

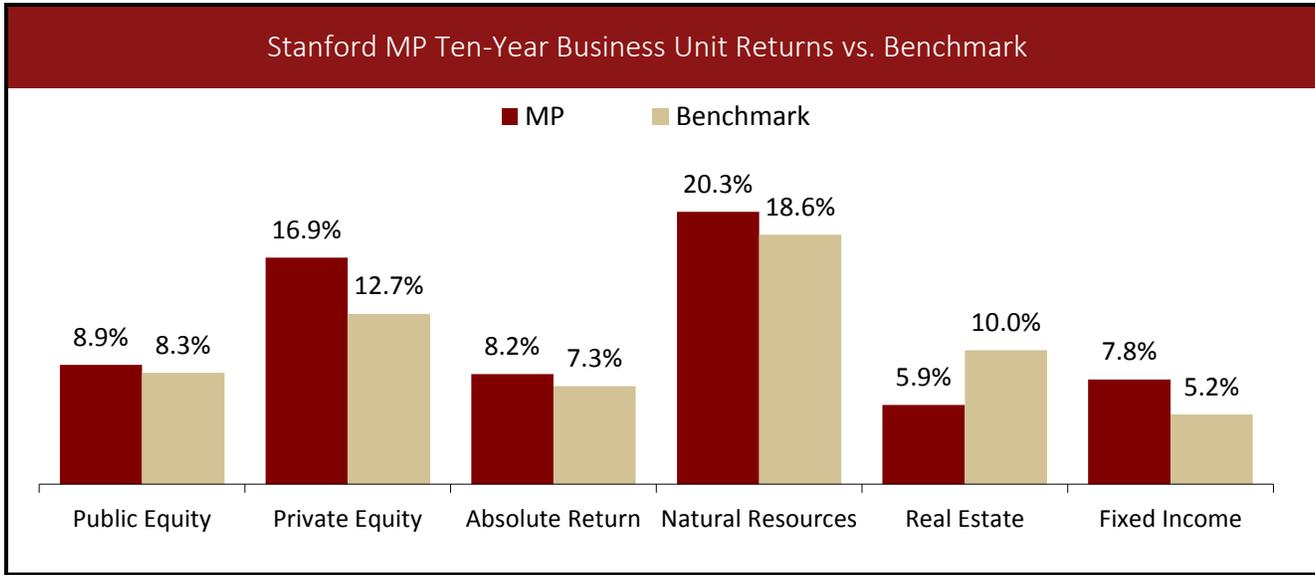


INDIVIDUAL BUSINESS UNIT PERFORMANCE

SMC evaluates investment manager performance by comparing manager returns to respective SMC Board approved benchmarks. The performance of individual business units for the 12 months ended June 30, 2014, relative to each business unit benchmark, is illustrated in the graph below:



STANFORD MP TEN-YEAR BUSINESS UNIT RETURNS VS. BENCHMARK



The endowment provides valuable resources to support the University's mission through funding financial aid, faculty research, and innovative programs. Over the past ten years, the MP has grown from \$10 billion to \$25 billion through strong investment returns and the generous support of alumni and friends. SMC is committed to building on past success to further improve our investment performance and enhance the University's mission of educating current students and future generations.

Finally, I have announced that I will leave my post in 2015. It has been a privilege and an honor to support this great university with its missions of teaching, research and service. I have decided that it is time to take my enthusiasm for business-building and find a new challenge, but I am mindful of the responsibility that comes with service to Stanford. Thus I want to provide ample time for a search to be conducted for a successor to lead the SMC team, of which I am very proud. I plan to remain CEO until my replacement can be appointed.

JOHN F. POWERS
President and Chief Executive Officer
Stanford Management Company