

**THE UNIVERSITY OF TEXAS SYSTEM
GENERAL ENDOWMENT FUND**

FINANCIAL STATEMENTS

Year Ended August 31, 2003 and 2002

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

Our discussion and analysis of The University of Texas System General Endowment Fund's (Fund) financial performance provides an overview of its activities for the fiscal year ended August 31, 2003. This discussion was prepared by The University of Texas Investment Management Company "UTIMCO" and should be read in conjunction with the Fund's financial statements and notes. The Fund is an internal UT System mutual fund for the pooled investment of the Permanent Health Fund (PHF) and The University of Texas System Long Term Fund (LTF). The Fund was created to allow the PHF and LTF to benefit from their identical investment objectives by providing greater efficiencies and cost savings than was possible when the investments of the PHF and LTF were managed separately. The Texas Constitution and various state statutes designate The University of Texas System Board of Regents (UT Board) as the fiduciary for the management of certain public endowment and operating funds. The UT Board has entered into an Investment Management Services Agreement delegating investment management responsibility for all investments to UTIMCO.

The purpose of the MD&A is to provide an objective and easily readable analysis of the Fund's financial statements based upon currently known facts, decisions or conditions.

Financial Highlights

- The Fund's net asset value, after contributions and withdrawals, increased by \$291.6 from \$3,293.2 million to \$3,584.8 million or approximately 8.9% during the year.
- The PHF and LTF redeemed and purchased Fund units resulting in a net reduction in contributions of \$126.1 million during the year.
- The Fund posted a net investment return of 12.81% for the fiscal year ended August 31, 2003, compared to a net investment return of negative 6.96% for the prior fiscal year.
- The Fund allocated \$71.4 million of net investment income and \$24.3 million of realized losses to the LTF and PHF during the fiscal year ended August 31, 2003. The Fund allocates its net investment income and its realized gain or loss to the PHF and LTF monthly based on their ownership of Fund units at month end. The distributed net investment income and realized gain amounts are considered reinvested as contributions to the Fund. Any distributed realized losses reduce the cost basis of the units in the Fund. Since the distribution is proportional to the percentage ownership by the PHF and LTF, no additional units are purchased.

Market Commentary

The fiscal year ended August 31, 2003 was a year of two remarkably contrasting periods. The first was the period leading up to the conclusion of the major conflict in Iraq, where uncertainty and global market weakness prevailed. The second was the subsequent months following the market low registered on March 11, during which risk taking around the world was financially rewarded. The table on the next page outlines the dramatic contrast in results between these two periods:

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Index	Equity Description	9/1/02 - 3/11/03	3/11/03 - 8/31/03
S&P 500	U.S. Large Capitalization	-11.1%	26.9%
Russell 2000	U.S. Small Capitalization	-10.8%	44.3%
MSCI EAFE	International Developed Markets	-15.7%	29.8%
MSCI Emerging Markets Free	International Emerging Markets	-7.6%	40.9%

Navigating these two disparate investment environments proved challenging. However, by maintaining a diversified asset exposure - including a meaningful allocation to absolute return strategies (hedge funds) - the Fund was able to preserve capital during the dramatic negative results of the first six months. In addition, positive performance by many of the Fund's active managers added to returns. Finally, decisions to tactically reallocate capital during the spring and summer months away from defensive assets, including fixed income, and towards more economically sensitive instruments, such as small cap and emerging markets equities, enabled the Fund to participate in the financial markets' eventual anticipation of a strong global recovery, which resulted in superior investment returns.

Use of Financial Statements and Notes

The Fund financial statements were prepared in accordance with standards issued by the Governmental Accounting Standards Board (GASB). Three financial statements are required under GASB: the Statement of Net Assets, the Statement of Operations and Changes in Net Assets, and the Statement of Cash Flows. We have also included as part of the basic financial statements the Financial Highlights and the Comparison Summary of Investment in Securities, at Fair Value.

The notes to the financial statements contain supplemental information that is essential for the fair presentation of the financial statements.

Statement of Net Assets

The Statement of Net Assets presents assets, liabilities, and net assets of the Fund as of the end of the fiscal year. This statement, along with all of the Fund's financial statements, is prepared using the accrual basis of accounting, whereby Fund investment income is recognized when earned and Fund expenses are recognized when incurred.

The Fund invests in a broad mix of investments and is actively managed to its benchmark, the Endowment Policy Portfolio. The Endowment Policy Portfolio is the index or benchmark for the endowment funds that UTIMCO manages. The return of the Endowment Policy Portfolio is the sum of the weighted benchmark returns for each asset class that comprise it. UTIMCO allocates Fund's assets to internally and externally managed portfolios in accordance with approved asset allocation policies, and attempts to supplement the original endowment corpus by increasing purchasing power over time. In doing so, UTIMCO increases the endowment resources available to fund the teaching, research, and health care programs specified by the various donors.

Net assets consist of participant contributions and accumulated net unrealized gains on investments.

Statement of Operations and Changes in Net Assets

Changes in net assets as presented on the Statement of Operations and Changes in Net Assets are based on activity of the Fund. The purpose of this statement is to present the results of operations, the changes in value of the investments of the Fund, the net participant contributions, and the distributions to participants.

The Fund earned realized and unrealized investment gains of \$346.3 million during the year compared to realized and unrealized losses of \$324.2 million for the year ended August 31, 2002. Expenses totaled \$5.8 million in fiscal year 2003 and \$7.2 million in fiscal year 2002.

The net increase in net assets resulting from operations totaled \$417.7 for the fiscal year ended August 31, 2003 compared to a net decrease in net assets resulting from operations totaling \$252.5 for the fiscal year ended August 31, 2002.

Statement of Cash Flows

The Statement of Cash Flows provides relevant information about the cash receipts and cash payments of the Fund for the periods. The PHF and LTF sell Fund units in order to create cash to pay the quarterly distributions as well as to meet any withdrawal requirements. Distributions to the PHF and LTF for such unit sales were \$208.7 million and \$285.9 million, respectively, for the years ended August 31, 2003 and 2002. Contributions to the Fund totaled \$110.1 million and \$103.5 million, respectively, for the years ended August 31, 2003 and 2002.

Statement of Financial Highlights

The inclusion of the Financial Highlights statement is to report the selected per unit data and financial ratios of the Fund by fiscal period since the inception of the Fund. As reported in the statement, the Fund's net asset value per unit increased in fiscal year 2003, reversing declines reported in the prior two fiscal years of 2002 and 2001.

Schedule of Investment in Securities, at Fair Value

The Schedule of Investment in Securities, at Fair Value provides a comparative listing of investments by type of security. The total investment in securities increased from \$3,387.0 million to \$3,671.9 million during the year.

Contacting UTIMCO

The above financial highlights are designed to provide a general overview of the Fund's investment results and insight into the following financial statements. Additional information may be found on our website and inquiries may be directed to UTIMCO via www.utimco.org.

Report of Independent Auditors

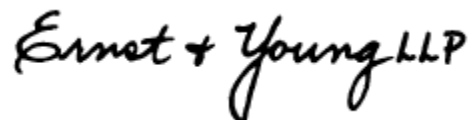
The Board of Regents of The University of Texas System
The Board of Directors of The University of Texas Investment Management Company
Austin, Texas

We have audited the accompanying statement of net assets and the summary of investment in securities of The University of Texas System General Endowment Fund (the "Fund") as of August 31, 2003, and the related statements of operations, changes in net assets, cash flows and financial highlights for the year then ended. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audit. The financial statements (excluding a statement of cash flows) of The University of Texas General Endowment Fund for the year ended August 31, 2002 and the financial highlights for the year ended August 31, 2002 and the period from inception (March 1, 2001) to August 31, 2001, were audited by other auditors whose report dated October 18, 2002, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Management's discussion and analysis on pages 1 through 3 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In our opinion, the 2003 financial statements and financial highlights, referred to above present fairly, in all material respects, the financial position of The University of Texas System General Endowment Fund as of August 31, 2003, the results of its operations, its cash flows, and changes in its net assets for the year then ended, in conformity with accounting principles generally accepted in the United States.

 Ernst & Young LLP

October 17, 2003

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Statements of Net Assets

August 31, 2003 and 2002

(Dollars in thousands, except per unit amounts)

Assets	2003	2002
Investment in Securities, at Fair Value (Cost \$3,548,461 and \$3,637,907, respectively)	\$ 3,671,854	\$ 3,387,022
Collateral for Securities Loaned, at Fair Value	78,308	68,371
Deposit with Broker for Futures Contracts	25,688	18,750
Unrealized Gains on Foreign Currency Exchange Contracts	6,920	8,130
Receivables		
Investment Securities Sold	84,818	75,207
Accrued Income	6,020	8,099
Other	<u>1,194</u>	<u>306</u>
Total Assets	<u>3,874,802</u>	<u>3,565,885</u>
 Liabilities		
Payable to Participants	40,492	12,998
Payable Upon Return of Securities Loaned	78,308	68,371
Unrealized Losses on Foreign Currency Exchange Contracts	4,826	2,342
Payables		
Investment Securities Purchased	164,790	187,329
Other	<u>1,621</u>	<u>1,651</u>
Total Liabilities	<u>290,037</u>	<u>272,691</u>
 Net Assets	 <u>\$ 3,584,765</u>	 <u>\$ 3,293,194</u>
 Supplementary Disclosure:		
Net Assets Consist Of:		
Participant Contributions (Net of Withdrawals)	\$ 3,508,386	\$ 3,587,430
Net Unrealized Appreciation (Depreciation) of Investments		
Including Translation Of Assets and Liabilities in Foreign Currencies	<u>76,379</u>	<u>(294,236)</u>
Net Assets	<u>\$ 3,584,765</u>	<u>\$ 3,293,194</u>
 Number of Units:		
Permanent Health Fund (PHF)	7,263,383	7,676,762
The University of Texas System Long Term Fund (LTF)	<u>27,696,705</u>	<u>28,539,389</u>
Total	<u>34,960,088</u>	<u>36,216,151</u>
 Net Asset Value Per Unit	 <u>\$ 102.539</u>	 <u>\$ 90.932</u>

The accompanying notes are an integral part of these financial statements.

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Statements of Operations and Changes in Net Assets

Years Ended August 31, 2003 and 2002

(in thousands)

	<u>2003</u>	<u>2002</u>
Investment Income		
Interest	\$ 34,052	\$ 40,067
Dividends	34,685	34,458
Income Distributions from Limited Partnerships	7,060	2,887
Other	<u>1,426</u>	<u>1,504</u>
Total Investment Income	<u>77,223</u>	<u>78,916</u>
Expenses		
Investment Management and Consulting Fees	5,001	6,414
Custodial Fees and Expenses	547	603
Other	<u>233</u>	<u>228</u>
Total Expenses	<u>5,781</u>	<u>7,245</u>
Net Investment Income	<u>71,442</u>	<u>71,671</u>
Realized and Unrealized Gain (Loss) on Investments		
Net Realized Loss on Investments Securities And Foreign Currency Related Transactions	(24,341)	(124,188)
Net Unrealized Appreciation (Depreciation) on Investment Securities and Foreign Currency Related Transactions	<u>370,615</u>	<u>(199,983)</u>
Net Gain (Loss) on Investments	<u>346,274</u>	<u>(324,171)</u>
Net Increase (Decrease) in Net Assets Resulting From Operations	\$ 417,716	\$ (252,500)
Net Assets		
Beginning of Period	3,293,194	3,723,912
Participant Contributions	110,074	103,516
Participant Withdrawals	<u>(236,219)</u>	<u>(281,734)</u>
End of Period	<u>\$ 3,584,765</u>	<u>\$ 3,293,194</u>

*The accompanying notes are an integral
part of these financial statements.*

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Statements of Cash Flows

*Years Ended August 31, 2003 and 2002
(in thousands)*

	2003	2002 (unaudited)
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Cash Flows From Operating Activities:		
Cash received on interest and dividends	\$ 70,816	\$ 76,777
Cash received on income distributions from limited partners	7,060	2,887
Cash received from other sources	1,426	1,605
Cash payments to investment managers and consultants	(4,413)	(6,028)
Cash payments to service providers	(1,397)	(830)
Purchase of investment securities	(3,394,048)	(4,660,306)
Proceeds from sale and maturities of investment securities	3,311,693	4,852,324
	<hr/>	<hr/>
Net Cash (Used in) Provided by Operating Activities	(8,863)	266,429
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Cash Flows from Financing Activities:		
Contributions from participants	110,074	103,516
Distributions to participants	(208,726)	(285,877)
	<hr/>	<hr/>
Net Cash Used in Financing Activities	(98,652)	(182,361)
	<hr/>	<hr/>
Net increase (decrease) in cash and cash equivalents	(107,515)	84,068
Cash and cash equivalents at beginning of year	404,900	320,832
	<hr/>	<hr/>
Cash and cash equivalents at end of year	\$ 297,385	\$ 404,900
	<hr/>	<hr/>
Reconciliation of net increase (decrease) in net investment assets provided by operating activities:		
Net increase (decrease) in net assets resulting from operations	\$ 417,716	\$ (252,500)
Adjustments to reconcile net increase (decrease) in net assets to net cash provided by operating activities:		
Unrealized (gains) losses on investment securities and foreign currency related transactions	(370,615)	199,983
Cost of investment securities purchased	(3,371,497)	(4,616,211)
Cost of investment securities sold	3,346,418	5,024,737
(Increase) decrease in receivables:		
Investment securities sold, at cost	(9,495)	(48,316)
Accrued income	2,079	2,252
Other	(888)	246
Increase (decrease) in payables:		
Investment securities purchased, at cost	(22,551)	(44,095)
Other	(30)	333
	<hr/>	<hr/>
Net Cash (Used in) Provided by Operating Activities	\$ (8,863)	\$ 266,429
	<hr/>	<hr/>

The accompanying notes are an integral part of these financial statements.

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Comparison Summary of Investment in Securities, at Fair Value

August 31, 2003 and 2002

(in thousands)

	<u>2003</u>	<u>2002</u>
Equity Securities		
Commingled Investments	\$ 992,944	\$ 617,064
Index Funds	793,380	775,885
Domestic Common Stock	566,279	507,797
Limited Partnerships	376,667	353,556
Foreign Common Stocks	126,286	98,713
Other	<u>1,784</u>	<u>1,263</u>
Total Equity Securities	<u>2,857,340</u>	<u>2,354,278</u>
Debt Securities		
U.S. Government Obligations (Direct and Guaranteed)	46,115	110,388
U.S. Government Agencies (Non-Guaranteed)	215,261	196,481
U.S. Government Agencies (Non-Guaranteed) (Non-U.S. Dollar Denominated)	567	899
Foreign Government and Provincial Obligations (U.S. Dollar Denominated)	7,479	5,865
Foreign Government and Provincial Obligations (Non-U.S. Dollar Denominated)	79,997	58,928
Municipal and County Bonds	2,542	2,831
Corporate Bonds	128,837	221,220
Foreign Corporate Bonds	10,219	10,117
Commingled Investment	10,209	8,711
Commercial Paper	-	3,086
Other	<u>1,037</u>	<u>1,470</u>
Total Debt Securities	<u>502,263</u>	<u>619,996</u>
Preferred Stock		
Domestic Preferred Stock	7,719	5,047
Foreign Preferred Stock	<u>117</u>	<u>618</u>
Total Preferred Stock	<u>7,836</u>	<u>5,665</u>
Purchased Options	<u>6,315</u>	<u>-</u>
Convertible Securities	<u>715</u>	<u>2,183</u>
Cash and Cash Equivalents		
Money Market Funds Maintained to Back Futures Contracts	212,955	201,279
Money Market Funds - Other	<u>84,430</u>	<u>203,621</u>
Total Cash and Cash Equivalents	<u>297,385</u>	<u>404,900</u>
 Total Investment in Securities	 <u>\$ 3,671,854</u>	 <u>\$ 3,387,022</u>

*The accompanying notes are an integral
part of these financial statements.*

**THE UNIVERSITY OF TEXAS SYSTEM
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Financial Highlights

Years Ended August 31, 2003 and 2002 and For the Period from Inception (March 1, 2001) to August 31, 2001

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Selected Per Unit Data			
Net Asset Value, Beginning of Period	\$ 90.932	\$ 97.811	\$ 100.00
Income from Investment Operations			
Net Investment Income	1.972	1.895	1.200
Net Realized and Unrealized Gain (Loss) on Investments	<u>9.635</u>	<u>(8.774)</u>	<u>(3.389)</u>
Total Income (Loss) from Investment Operations	<u>11.607</u>	<u>(6.879)</u>	<u>(2.189)</u>
Net Asset Value, End of Period	<u>\$ 102.539</u>	<u>\$ 90.932</u>	<u>\$ 97.811</u>
Ratios and Supplemental Data			
Net Assets, End of Period (in thousands)	\$ 3,584,765	\$ 3,293,194	\$ 3,723,912
Ratio of Expenses to Average Net Assets	0.17%	0.20%	0.09%
Ratio of Net Investment Income to Average Net Assets	2.12%	2.00%	1.22%

*The accompanying notes are an integral
part of these financial statements.*

Note 1 – Organization and Basis of Presentation

The University of Texas System General Endowment Fund (Fund), created March 1, 2001, is a pooled fund established for the collective investment of long-term funds under the control and management of the Board of Regents of The University of Texas System (Board of Regents). The Fund is organized as a mutual fund and has two participants, the Permanent Health Fund (PHF) and The University of Texas System Long Term Fund (LTF). The PHF and LTF initially purchased units of the Fund on March 1, 2001, in exchange for the contribution of their investment assets. The Fund provides for greater diversification of investments than would be possible if each account were managed separately.

Fiduciary responsibility for the Fund rests with the Board of Regents. The day-to-day operational responsibilities of the Fund are delegated to The University of Texas Investment Management Company (UTIMCO), pursuant to an Investment Management Services Agreement with the Board of Regents.

The Fund uses the accrual method of accounting, recognizing income when such items are earned and expenses when such items are incurred. The Fund is subject to the pronouncements of the Governmental Accounting Standards Board (GASB) and accounts for its activities as a proprietary enterprise fund. The Fund also applies all applicable pronouncements of the Financial Accounting Standards Board that do not conflict with pronouncements of the GASB.

The annual combined financial statements of The University of Texas System are prepared in accordance with Texas Comptroller of Public Accounts' Annual Financial Reporting Requirements and include information related to the Fund. The accompanying financial statements may differ in presentation from the Texas Comptroller of Public Accounts' Annual Financial Reporting Requirements.

Note 2 – Significant Accounting Policies

(A) ***Security Valuation*** -- Investments are primarily valued on the basis of market valuations provided by independent pricing services.

Fixed income securities held directly by the Fund are valued based upon prices supplied by Merrill Lynch Securities Pricing Service and other major fixed income pricing services, external broker quotes and internal pricing matrices.

Equity security market values are based on the New York Stock Exchange composite closing prices, if available. If not available, the market value is based on the closing price on the primary exchange on which the security is traded (if a closing price is not available, the average of the last reported bid and ask price is used).

Limited partnerships and other equity securities are valued based on a fair valuation determined as specified by policies established by the UTIMCO Board of Directors. Limited partnerships are valued using the partnership's capital account balance at the closest available reporting period (usually June 30), as communicated by the general partner, adjusted for contributions and withdrawals subsequent to the last available reporting period. In the rare case no ascertainable value is available, the limited partnership is valued at cost.

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Notes to Financial Statements (cont.)

Securities held by the Fund in index funds are generally valued as follows:

Stocks traded on security exchanges are valued at closing market prices on the valuation date.

Stocks traded on the over-the-counter market are valued at the last reported bid price, except for National Market System OTC stocks, which are valued at their closing market prices.

Fixed income securities are valued based upon bid quotations obtained from major market makers or security exchanges.

Commingled investments are valued based on net asset value information provided by the investment company.

(B) ***Foreign Currency Translation*** -- The accounting records of the Fund are maintained in U.S. dollars. Investments in securities are valued at the daily rates of exchange on the valuation date. Purchases and sales of securities of foreign entities and the related income receipts and expense payments are translated into U.S. dollars at the exchange rate on the dates of the transactions. The Fund does not isolate that portion of the results of operations resulting from changes in foreign exchange rates on investments from fluctuations arising from changes in market prices of securities held. Such fluctuations are included with the net realized and unrealized gain or loss from investments. Security classifications as domestic or foreign on the summary of investment in securities, at fair value are based on currency.

(C) ***Investment Income*** -- Interest income is accrued as earned. Dividend income is recorded on the ex-dividend date. Dividend and interest income is recorded net of foreign taxes where recovery of such taxes is not assured. Investment income includes net realized and unrealized currency gains and losses recognized between accrual and payment dates on dividend and interest transactions. Premiums and discounts on bonds are not amortized.

(D) ***Security Transactions*** -- Security transactions are recorded on a trade date basis for most securities. International index fund transactions are recorded on a settlement date basis due to trading practices which impose restrictions in acquiring per unit information on the trade date. Gains and losses on securities sold are determined on the basis of average cost. A loss is recognized if there is an impairment in the value of the security that is determined to be other than temporary.

(E) ***Distributions to Participants*** -- The Fund, for accounting purposes, allocates its net investment income and realized gain or loss to the PHF and LTF monthly, based on their ownership of Fund units at month end. The allocated investment income and realized gain amounts are considered reinvested as contributions. Any allocated realized losses reduce the cost basis of the units of the Fund. Since the allocation is proportional to the percentage ownership by the PHF and LTF, no additional units are purchased.

(F) ***Fund Valuation*** -- Valuation of the Fund's units occurs on a quarterly basis. Unit values are determined by dividing the value of the Fund's net assets by the number of units outstanding on the valuation date.

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Notes to Financial Statements (cont.)

(G) ***Purchases and Redemption of Units*** -- The value of participating units, upon admission to the Fund, is based upon the market value of net assets held as of the valuation date. Redemptions from the Fund will also be made at the market value price per unit at the valuation date at the time of the withdrawal. There are no transaction costs incurred by participants for the purchase or redemption of units.

(H) ***Participants' Net Assets*** -- All participants in the Fund have a proportionate undivided interest in the Fund's net assets.

(I) ***Federal Income Taxes*** -- The Fund is not subject to federal income tax.

(J) ***Use of Estimates*** -- The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

(K) ***Foreign Currency Contracts*** -- The Fund enters into forward foreign currency exchange contracts to hedge against foreign currency exchange rate risks on its non-U.S. dollar denominated investment securities and to facilitate trading strategies primarily as a tool to increase or decrease market exposure to various foreign currencies. When entering into a forward currency contract, the Fund agrees to receive or deliver a fixed quantity of foreign currency for an agreed-upon price on an agreed future date. These contracts are valued daily and the Fund's net equity therein, representing unrealized gain or loss on the contracts as measured by the difference between the forward foreign exchange rates at the dates of entry into the contracts and the forward rates at the reporting date, is included in the statement of assets and liabilities. Realized and unrealized gains and losses are included in the statement of operations. These instruments involve market and/or credit risk in excess of the amount recognized in the statements of assets and liabilities. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movement in currency and securities values and interest rates.

(L) ***Cash and Cash Equivalents*** -- Cash and Cash Equivalents consist of money markets, foreign currencies and other overnight funds. A portion of the Fund's cash and cash equivalents are maintained to support the notional value of futures contracts held (see Note 9). Cash and cash equivalents are an integral part of the Fund's investment activities, and as such are included in the investment in securities balance on the statement of net assets.

(M) ***Recently Issued Accounting Standards*** -- In March 2003, GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures – An Amendment of GASB Statement No. 3*, which modifies and expands disclosures regarding deposits and investments. This statement is not effective for the Fund until the fiscal year ending 2005. Management does not anticipate that the implementation of the new statement will have a material impact on the Fund's financial statement balances.

(N) ***Reclassifications*** -- Certain items in the 2002 financial statements and related notes have been reclassified to conform with 2003 classification.

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Notes to Financial Statements (cont.)

Note 3 – Investments

The Fund's investments have been categorized as defined by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements) and Reverse Repurchase Agreements*, to give an indication of the level of credit risk assumed by the Fund at August 31, 2003 and 2002. All of the securities shown in the comparison summary of investment in securities are considered credit risk category 1 investments except for commingled equity investments, index funds, limited partnerships, other equity securities, commingled debt investments, purchased options and cash and cash equivalents. Credit risk category 1 investments are investments that are insured or registered held by the Fund or its agent in the Fund's name. All of the exceptions are not categorized by credit risk category because they are not evidenced by securities that exist in physical or book entry form. The amounts identified as securities on loan that have cash held as collateral (see Note 7) would also be considered not categorized.

Note 4 – Commingled Investments

The commingled investments consist of investments in other entities in which the Fund has an ownership percentage, shares or limited partnership interest. The International Equity Fund is majority owned by the Fund and the Permanent University Fund. The market values of the commingled investments consist of the following:

	August 31,	
	2003	2002
Equity Commingled Investments:		
Merger Arbitrage and Special Situation Funds	\$ 323,688,467	\$ 266,051,280
Hedge Funds	303,507,120	180,962,896
Emerging Market Mutual Funds	168,965,780	117,991,611
International Equity Fund	68,322,813	-
Small Capitalization International Stock Fund	63,090,957	51,524,771
Fund of Hedge Funds	45,399,131	-
Opportunistic Small Cap Value Fund	19,380,770	-
Growth-Oriented, Capital Appreciation Fund	<u>588,812</u>	<u>533,314</u>
Total Equity Commingled Investments	<u>\$ 992,943,850</u>	<u>\$ 617,063,872</u>
Debt Commingled Investment:		
High Yield Bond Fund	<u>\$ 10,209,405</u>	<u>\$ 8,710,889</u>

The merger arbitrage and special situation funds invest in securities of companies facing a major corporate event. These events might include mergers, tender offers, recapitalizations, spin-offs, liquidations and substantial corporate self-tenders. In addition, these funds may invest in distressed companies that are subject to reorganizations, bankruptcies, or other special situations that can create arbitrage opportunities through the exploitation of inefficiencies in the pricing of related securities. The research-intensive investments within these funds are typically uncorrelated with the overall market and dependent on the occurrence of the specific "investment events" to realize the return.

Hedge funds invest in global equity securities both long and short. Investment return is expected to be realized from long and short security selection, and only modestly by the direction of the overall equity markets.

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Notes to Financial Statements (cont.)

The emerging market funds utilize a long and short investment strategy and invest primarily in emerging and developed markets in Asia and the Pacific region and emerging markets in Latin America, Eastern Europe, the Middle East, and Russia.

The international equity fund invests in non-U.S. equity assets, cash equivalents, currencies and currency forwards.

The fund of hedge funds invest in other hedge funds including merger arbitrage and special situation funds, hedge funds, and other relative value hedge funds and absolute return strategies.

The opportunistic small cap value fund makes active strategic-block value investments in a limited number of small-capitalization public companies.

Note 5 – Index Funds

The index funds, managed by the same investment manager, consist of several funds with different investment objectives, as follows:

The Mid-Cap Index Fund B Lendable is a portfolio of common stocks with the objective of approximating as closely as practicable the capitalization weighted total rate of return of the segment of the U.S. and Canadian markets for publicly traded common stocks represented by the medium capitalized companies. The fund tracks the S&P 400 Mid-Cap Index.

The EAFE Equity Index Fund B is managed to replicate the Morgan Stanley Capital International Europe, Australia and Far East Index (EAFE). Individual index funds are established to represent each country within the EAFE Index. The fund is a commingled ‘superfund’ comprised from the individual EAFE Index country funds managed in their appropriate capitalization weights.

The Emerging Markets Structured Tiered Fund B attempts to approximate the capitalization weighted total rates of return of the equity securities in the Morgan Stanley Capital International Emerging Markets Free Index for selected countries. The fund adopts a structured tier weighting approach across the countries.

The Russell 2000 Alpha Tilts Fund B’s objective is approximating the capitalization weighted total rate of return of the Russell 2000 Index. The fund is selected and maintained in accordance with a formula designed to select stocks through optimized tilts toward particular stock characteristics. The formula is designed to provide systematic exposure to such characteristics with the objective of producing long-term returns in excess of the total rate of return of the Russell 2000 Index.

The Equity Index Fund B Lendable is a portfolio of common stocks with the objective of approximating as closely as practicable the capitalization weighted total return of that segment of the U.S. market for publicly traded common stocks represented by the larger capitalized markets. The fund tracks the S&P 500 Index.

The Russell 3000 Alpha Tilts Fund B’s objective is approximating the capitalization weighted total rate of return of the Russell 3000 Index. The fund is selected and maintained in accordance with a quantitative formula designed to select stocks through optimized tilts toward particular stock

**THE UNIVERSITY OF TEXAS SYSTEM
GENERAL ENDOWMENT FUND**

Notes to Financial Statements (cont.)

characteristics. The formula is designed to provide systematic exposure to such characteristics with the objective of producing long-term returns in excess of the total rate of return of the Russell 3000 Index.

The EAFE Equity Index Transition Fund is a temporary fund established to accommodate the transition of existing investments into an existing index fund. The EAFE Equity Index Transition Fund will be folded into the EAFE Equity Index Fund B upon completion of the transition.

When deemed appropriate, a portion of the index funds may invest in futures contracts for the purpose of acting as a temporary substitute for investment in common stocks.

The Mid-Cap Index Fund B Lendable is majority owned by the Fund and the Permanent University Fund. The market values of the Fund's interests in these index funds are as follows:

	August 31,	
	2003	2002
Mid-Cap Index Fund B Lendable	\$ 238,928,385	\$ 313,552,230
EAFE Equity Index Fund B	166,993,484	215,431,749
Emerging Markets Structured Tiered Fund B	118,842,238	34,403,816
Russell 2000 Alpha Tilts Fund B	111,219,982	66,993,761
Equity Index Fund B Lendable	104,989,080	145,503,530
Russell 3000 Alpha Tilts Fund B	52,188,990	-
EAFE Equity Index Transition Fund	218,257	-
	<u>\$ 793,380,416</u>	<u>\$ 775,885,086</u>

Note 6 – Limited Partnerships

The limited partnerships consist of interests in privately held investments that are not registered for sale on public exchanges. The market values of the limited partnerships consist of the following:

	August 31,	
	2003	2002
U.S. Private Equity	\$ 171,367,289	\$ 164,362,231
Opportunistic	61,047,986	45,366,743
Venture Capital	60,757,306	74,679,119
Non-U.S. Private Equity	51,601,243	38,217,992
Mezzanine	21,969,831	23,361,798
Oil and Gas	7,023,086	3,107,038
Direct Investments	2,900,354	4,461,106
	<u>\$ 376,667,095</u>	<u>\$ 353,556,027</u>

The U.S. private equity interests consist of investments in private equity partnerships which primarily invest in the equity securities of private businesses that are considered to be in the post-start-up phase and that are profitable and generating income.

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Notes to Financial Statements (cont.)

The opportunistic category consists of interests in private equity partnerships that invest in distressed debt, specialized sectors or that purchase limited partnership interests in private equity partnerships on a secondary basis.

Venture capital consists of interests in private equity partnerships that provide capital to companies that are in the early stages of development.

Non-U.S. private equity interests consist of investments in private equity and venture capital partnerships that are based outside of the U.S. These partnerships focus on making investments in companies that have operations in countries other than the U.S.

Mezzanine interests consist of investments in partnerships that make subordinated debt or minority equity investments in private companies.

Oil and Gas consists of interests in private partnerships that hold royalty interests and other non-working interests in oil and gas properties. These properties create an income stream over the life of the partnership.

Direct investments represent the Fund's direct interests in private companies.

Note 7 – Securities Lending

The Fund loans securities to certain brokers who pay the Fund negotiated lenders' fees. These fees are included in investment income. The Fund receives qualified securities and/or cash as collateral against the loaned securities. The collateral, when received, will have a market value of 102% of loaned securities of U.S. issuers and a market value of 105% for loaned securities of non-U.S. issuers. If the market value of the collateral held in connection with loans of securities of U.S. issuers is less than 100% at the close of trading on any business day, the borrower is required to deliver additional collateral by the close of the next business day to equal 102% of the market value. For non-U.S. issuers, the collateral should remain at 105% of the market value of the loaned securities at the close of any business day. If it falls below 105%, the borrower must deliver additional collateral by the close of the following business day. The value of securities loaned and the value of collateral held are as follows at August 31, 2003 and 2002:

Securities on Loan	2003 Value	2002 Value	Type of Collateral	2003 Value of Collateral	2002 Value of Collateral
U.S. Government	\$ 33,846,231	\$ 35,514,900	Cash	\$ 34,293,065	\$ 35,961,724
Foreign Government	9,265,920	961,421	Cash	9,744,659	1,010,345
Corporate Bonds	12,707,965	23,687,864	Cash	13,138,006	24,460,254
Common Stock	<u>20,226,902</u>	<u>6,546,729</u>	Cash	<u>21,132,580</u>	<u>6,939,041</u>
Total	<u>\$ 76,047,018</u>	<u>\$ 66,710,914</u>	Total	<u>\$ 78,308,310</u>	<u>\$ 68,371,364</u>
U.S. Government	<u>\$ 3,777,301</u>	<u>\$ 1,921,464</u>	Non-Cash	<u>\$ 3,918,834</u>	<u>\$ 2,073,215</u>

Cash received as collateral for securities lending activities is recorded as an asset with an equal and offsetting liability to return the collateral. Investments received as collateral for securities lending activities are not recorded as assets because the investments remain under the control of the transferor, except in the event of default.

Note 8 – Commitments

The Fund had unfunded contractual commitments for Limited Partnerships and Other assets of \$367,614,272 as of August 31, 2003.

Note 9 – Futures Contracts

The Fund's activities include trading in derivatives such as futures contracts. Futures contracts are used to facilitate various trading strategies, primarily as a tool to increase or decrease market exposure to various asset classes of the Fund. The asset classes that used futures during the year include domestic and foreign equities, domestic and foreign debt, and commodities. Commodity index exposure was obtained through the Goldman Sachs Commodity Index (GSCI). The GSCI is a composite index of commodity sector returns, representing an unleveraged, long-only investment in commodity futures that is broadly diversified across the spectrum of commodities. The Fund had \$25,688,593 and \$18,749,761 on deposit with a broker for collateral as margin for the futures contracts as of August 31, 2003 and 2002, respectively. It is the intention of the Fund not to utilize leverage when entering into these contracts and to maintain cash balances that, when combined with the collateral deposited with a broker, exceed the notional value of the futures contracts held. Short futures may be used by a limited number of the Fund's external managers to hedge the Fund's interest rate or country risk associated with security positions.

Futures contracts are marked to market daily; that is, they are valued at the close of business each day, and a gain or loss is recorded between the value of the contracts that day and on the previous day. The daily gain or loss is referred to as the daily variation margin, which is settled in cash with the broker each morning for the amount of the previous day's mark to market. The amount that is settled in cash with the broker each morning is the carrying and fair value of the futures contracts. Such carrying value at August 31, 2003 and 2002, is included in "Receivables Other" on the accompanying statements of net assets. The amount of net realized gain on the futures contracts was \$33,017,005 for the year ended August 31, 2003. The amount of net realized loss on futures contracts was \$10,002,498 for the year ended August 31, 2002. The Fund executes such contracts either on major exchanges or with major international financial institutions and minimizes market and credit risk associated with these contracts through the managers' various trading and credit monitoring techniques.

The following discloses the notional, carrying and fair values at August 31, 2003, and the average carrying and fair values for the year ended August 31, 2003, for futures contracts:

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Notes to Financial Statements (cont.)

	Notional Value at August 31, 2003		Carrying and Fair Value at August 31, 2003		Average Carrying and Fair Value for the Year Ended August 31, 2003	
	Long	Short	Assets	Liabilities	Assets	Liabilities
Domestic Fixed Income Futures	\$ 72,789,813	\$ 99,985,328	\$ 108,983	\$ 116,997	\$ 177,945	\$ 182,285
International Fixed Income Futures	78,974,879	22,371,194	58,659	47,569	186,596	178,056
Domestic Equity Futures	177,914,900	16,951,700	1,164,500	116,100	899,086	815,519
International Equity Futures	16,086,163	38,674,776	221,604	99,864	273,933	282,968
Commodities Futures	53,668,500	-	-	55,500	482,478	428,823

The following discloses the notional, carrying and fair values at August 31, 2002, and the average carrying and fair values at August 31, 2002 for futures contracts:

	Notional Value at August 31, 2002		Carrying and Fair Value at August 31, 2002		Average Carrying and Fair Value for the Year Ended August 31, 2002	
	Long	Short	Assets	Liabilities	Assets	Liabilities
Domestic Fixed Income Futures	\$ 45,079,078	\$ 114,685,328	\$ 70,476	\$ 142,385	\$ 232,098	\$ 243,703
International Fixed Income Futures	127,082,192	50,349,578	284,621	30,284	135,077	124,471
Domestic Equity Futures	143,919,310	4,888,125	54,470	-	492,278	560,172
International Equity Futures	15,099,006	9,455,356	156,976	132,581	261,156	261,299
Commodities Futures	95,424,900	-	44,425	-	382,932	310,496

Note 10 – Foreign Currency Exchange Contracts

The table on the next page summarizes by currency the contractual amounts of the Fund's foreign currency exchange contracts at August 31, 2003 and 2002. Foreign currency amounts are translated at exchange rates as of August 31, 2003 and 2002. The "Net Buy" amounts represent the U.S. dollar equivalent of net commitments to purchase foreign currencies, and the "Net Sell" amounts represent the U.S. dollar equivalent of net commitments to sell foreign currencies.

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Notes to Financial Statements (cont.)

<u>Currency</u>	<u>Net Buy August 31, 2003</u>	<u>Net Sell August 31, 2003</u>	<u>Unrealized Gains on Foreign Currency Exchange Contracts August 31, 2003</u>	<u>Unrealized Losses on Foreign Currency Exchange Contracts August 31, 2003</u>
Australian Dollar	\$ 14,223,196	\$ -	\$ 168,533	\$ 577,305
Canadian Dollar	-	23,530,711	326,608	245,250
Danish Krone	1,970,471	-	1,608	113,382
Euro	22,347,686	-	678,155	451,817
Hong Kong Dollar	-	363,291	326	43
Japanese Yen	71,256,328	-	1,225,925	610,242
New Zealand Dollar	-	1,073,812	208,291	34,693
Norwegian Krone	-	1,720,609	1,412,015	74,655
Polish Zloty	797,339	-	19,928	53,483
Singapore Dollar	8,767,217	-	239,438	26,314
Swedish Krona	18,692,592	-	943,981	887,193
Swiss Franc	-	18,097,729	1,392,352	1,040,342
UK Pound	13,922,233	-	302,402	711,562
	<u>\$ 151,977,062</u>	<u>\$ 44,786,152</u>	<u>\$ 6,919,562</u>	<u>\$ 4,826,281</u>

<u>Currency</u>	<u>Net Buy August 31, 2002</u>	<u>Net Sell August 31, 2002</u>	<u>Unrealized Gains on Foreign Currency Exchange Contracts August 31, 2002</u>	<u>Unrealized Losses on Foreign Currency Exchange Contracts August 31, 2002</u>
Australian Dollar	\$ 3,811,858	\$ -	\$ 342,307	\$ 2,411
Canadian Dollar	-	7,939,281	375,516	131,481
Danish Krone	966,650	-	42,799	-
Euro	45,956,285	-	830,451	17,141
Japanese Yen	67,210,003	-	3,639,620	384,501
New Zealand Dollar	3,081,427	-	172,269	13,694
Norwegian Krone	5,160,496	-	2,395,377	307,868
Singapore Dollar	916,954	-	101	83,302
Swedish Krona	22,262,844	-	74,857	87,773
Swiss Franc	-	23,050,955	158,668	977,873
UK Pound	14,516,673	-	98,372	336,134
	<u>\$ 163,883,190</u>	<u>\$ 30,990,236</u>	<u>\$ 8,130,337</u>	<u>\$ 2,342,178</u>

Note 11 – Fees and Expenses

The Fund incurs investment management fees from various external managers of the Fund. The fees, generally assessed quarterly, are based on a percentage of the market value of investments held by each individual investment manager and currently range from 0.01% to 1.0%. In addition to quarterly investment management fees, the Fund may pay annual performance-based management fees for investment performance in excess of certain defined benchmarks as provided for in the managers' contracts. In addition, the Fund incurs consulting fees for investment planning and oversight services with regard to limited partnerships and hedge funds.

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GENERAL ENDOWMENT FUND

Notes to Financial Statements (cont.)

Custodial fees and expenses are assessed by the financial institution which holds the Fund's assets. Fees are based on the number of accounts, market value of the Fund, and transaction activity in accordance with the contractual agreement with the institution. Additional fees are assessed for performance measurement and on-line communication services per the contractual agreement.

The Fund incurs other expenses related to its operations primarily consisting of audit fees, printing and graphic expenses, legal and consultation fees.