

Financial Statements
and Independent Auditors' Report
Permanent Health Fund
Years Ended August 31, 2007 and 2006

Permanent Health Fund

Financial Statements

Years Ended August 31, 2007 and 2006

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Independent Auditors' Report

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

We have audited the accompanying Statement of Fiduciary Net Assets of the Permanent Health Fund (the "Fund"), as of August 31, 2007, and the related Statement of Changes in Fiduciary Net Assets for the year then ended. These financial statements are the responsibility of The University of Texas Investment Management Company ("UTIMCO" or "management"). Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Fund as of and for the year ended August 31, 2006, were audited by other auditors whose report, dated October 27, 2006, expressed an unqualified opinion on those statements and included an explanatory paragraph noting that the financial statements of the Fund were not intended to present the financial positions of UTIMCO or The University of Texas System.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing the audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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.

As discussed in Note 1, the financial statements of the Fund are intended only to present the financial position of the Fund and do not purport to, and do not, present the financial positions of UTIMCO or The University of Texas System as of August 31, 2007, and the changes in their financial positions for the year then ended in conformity with accounting principles generally accepted in the United States.

As discussed in Note 3, the financial statements include an investment in The University of Texas System General Endowment Fund (the "GEF"), valued at \$1,099,759,614. The GEF has 40.8% of its net assets invested in assets whose fair value has been estimated by management in the absence of readily determinable fair values. Management's estimate of the value of the Fund is based upon the net asset value per unit of GEF, which is also calculated by UTIMCO.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Fund as of August 31, 2007, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages 3 through 6 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements of the Fund. The supplemental schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information is the responsibility of management. The supplemental schedules as of and for the year ended August 31, 2007 have been subjected to the audit procedures applied by us (with 2006, 2005, 2004 and 2003 being subject to audit procedures by other auditors) in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Deloitte & Touche LLP

October 29, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

Our discussion and analysis of the Permanent Health Fund's (Fund) financial performance provides an overview of its activities for the year ended August 31, 2007. 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 a pooled investment fund for the collective investment of state endowment funds for health-related institutions of higher education. The University of Texas System Board of Regents (UT Board) established the Fund in August 1999 with proceeds from state tobacco litigation. The Texas Constitution and various state statutes designate the 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.

On March 1, 2001, the Fund purchased units in the General Endowment Fund (GEF) in exchange for the contribution of its investment assets. The GEF, established by the UT Board effective March 1, 2001, is a pooled fund for the collective investment of long-term funds under the control and management of the UT Board. The GEF has only two participants: the Fund and The University of Texas System Long Term Fund (LTF), which was also established by the UT Board. The GEF is organized as a pooled investment fund in which the Fund and the LTF purchase and redeem units quarterly. The GEF is under the fiduciary responsibility of the UT Board and is provided day-to-day operations by 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 fiduciary assets after distributions, increased by \$113.1 million from \$987.0 million to \$1,100.1 million or by approximately 11.5% for the year ended August 31, 2007, compared to an increase of \$61.1 million or approximately 6.6% for the year ended August 31, 2006. The change in net fiduciary assets from year to year is mainly attributable to the following:
 1. The Fund posted a net investment return of 15.76%, calculated using the Modified Dietz Method as described by the CFA Institute, for the fiscal year ended August 31, 2007, compared to a net investment return of 11.05% for the prior fiscal year. The net investment return of the Fund is dependent on the results of the investments held in the GEF. The GEF's investments in private market investment funds, emerging markets equities and directional hedge funds were the leading contributors to the 2007 return. For the fiscal year ended August 31, 2006, the real estate investment trusts, private market investment funds and global equities asset classes were the leading performers.
 2. The Fund's distribution rate was increased by 2.9%, approximately the rate of inflation, for the year ended August 31, 2007. This equated to an increase in the 2007 rate to \$.0496 per unit from the 2006 rate of \$.0482 per unit. The 2006 rate was

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increased by 2.6% from the fiscal year ended August 31, 2005 rate. The fiscal year distributions represented 3.86% of the Fund's average net asset value for the year ended August 31, 2007, and 4.13% of the Fund's average net asset value for the year ended August 31, 2006.

3. There were no participant contributions to the Fund or withdrawals from the Fund during the years ended August 31, 2007 and 2006.

Use of Financial Statements and Notes

The Fund's financial statements were prepared in accordance with standards issued by the Governmental Accounting Standards Board (GASB). Two financial statements are required by the GASB: the Statement of Fiduciary Net Assets and the Statement of Changes in Fiduciary Net Assets.

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

Statements of Fiduciary Net Assets

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

Since the Fund no longer invests in individual securities except for the GEF units and a negligible amount of cash, the majority of the Fund's Statements of Fiduciary Net Assets is reflected in its investment in GEF units.

As of August 31, 2007, the Fund owned 6,118,081 GEF units representing an ownership percentage of 17.10%, compared to 6,359,817 GEF units representing an ownership percentage of 18.18% as of August 31, 2006. As of August 31, 2007 and 2006, the fair value of the GEF units was \$1,099.8 million and \$986.8 million, respectively.

The GEF 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. UTIMCO allocates GEF'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.

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The following summarizes the Statements of Fiduciary Net Assets (in millions):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Assets			
General Endowment Fund Units, at Fair Value	\$ 1,099.8	\$ 986.8	\$ 925.7
Cash and Cash Equivalents	0.3	0.2	0.2
Net Assets Held in Trust	<u>\$ 1,100.1</u>	<u>\$ 987.0</u>	<u>\$ 925.9</u>

Statements of Changes in Fiduciary Net Assets

Changes in fiduciary net assets as presented on the Statements of Changes in Fiduciary Net Assets are based on activity of the Fund. The purpose of these statements is to present additions to the Fund resulting from net investment income and participant contributions and to present deductions from the Fund resulting from participant distributions.

The net increase in investments of the Fund was \$135.0 million during the year compared to \$82.6 million for the fiscal year ended August 31, 2006. Investment expenses totaled \$0.8 million for the fiscal year ended August 31, 2007 and \$0.5 for each of the fiscal years ended August 31, 2006 and 2005.

Distributions to participants totaled \$40.7 million, \$39.5 million and \$38.5 million, respectively, for the years ended August 31, 2007, 2006 and 2005. The increase in distributions is a result of the UT Board increasing the distribution rate from \$0.0482 per unit to \$0.0496 per unit for fiscal year 2007. The increase for fiscal year 2006, is a result of the UT Board's increase of the distribution rate from \$0.047 per unit to \$0.0482 per unit.

The Fund's two primary investment objectives are:

- Provide for current beneficiaries by increasing the annual distribution rate at least equal to the rate of inflation so that real purchasing power is maintained, and
- Provide for future beneficiaries by increasing the market value of endowment funds after the annual distribution at a rate at least equal to the rate of inflation so that future distributions maintain purchasing power as well.

Fund distributions are controlled by a spending policy approved by the UT Board. The key to preservation of endowment purchasing power over the long-term is control of spending through a target distribution rate. This target rate should not exceed the endowment's average annual investment return after fund expenses and inflation. The Fund distributions are increased annually at an average rate of inflation provided that the distribution rate remains within a range of 3.5% to 5.5% of the Fund's net asset value. As reported on the financial highlights schedule of the financial statements, the ratio of distributions to average net assets (12-quarter average) has remained between 3.5% to 5.5%.

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The following table summarizes the Statements of Changes in Fiduciary Net Assets (in millions):

	2007	2006	2005
Investment Income	\$ 154.6	\$ 101.2	\$ 150.6
Less Investment Expenses	(0.8)	(0.5)	(0.5)
Net Investment Income	153.8	100.7	150.1
Administrative Fee for UT System Oversight	-	0.1	-
Participant Distributions	40.7	39.5	38.6
Total Deductions	40.7	39.6	38.6
Change in Fiduciary Net Assets	113.1	61.1	111.5
Net Assets Held in Trust, Beginning of Year	987.0	925.9	814.4
Net Assets Held in Trust, End of Year	<u>\$ 1,100.1</u>	<u>\$ 987.0</u>	<u>\$ 925.9</u>

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.

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Statements of Fiduciary Net Assets

August 31, 2007 and 2006

(Dollars in thousands, except per unit amounts)

	<u>2007</u>	<u>2006</u>
Assets		
General Endowment Fund Units, at Fair Value	\$ 1,099,760	\$ 986,754
Cash and Cash Equivalents	<u>296</u>	<u>274</u>
Net Assets Held in Trust (820,000,000 Units)	<u>\$ 1,100,056</u>	<u>\$ 987,028</u>
Net Asset Value Held in Trust Per Unit	<u>\$ 1.342</u>	<u>\$ 1.204</u>

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

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Statements of Changes in Fiduciary Net Assets

Years Ended August 31, 2007 and 2006

(in thousands)

	<u>2007</u>	<u>2006</u>
Additions		
Investment Income:		
Net Increase in Investments	\$ 135,011	\$ 82,649
Allocation of General Endowment Fund Net Investment Income	19,587	18,594
Other	<u>3</u>	<u>1</u>
Total Investment Income	<u>154,601</u>	<u>101,244</u>
Less Investment Expenses:		
UTIMCO Management Fee	840	528
Other Expenses	<u>16</u>	<u>16</u>
Total Investment Expenses	<u>856</u>	<u>544</u>
Net Investment Income	153,745	100,700
Deductions		
Administrative Fee for UT System Oversight	45	46
Participant Distributions	<u>40,672</u>	<u>39,524</u>
Total Deductions	<u>40,717</u>	<u>39,570</u>
Change in Fiduciary Net Assets	113,028	61,130
Net Assets Held in Trust, Beginning of Year	<u>987,028</u>	<u>925,898</u>
Net Assets Held in Trust, End of Year	<u>\$ 1,100,056</u>	<u>\$ 987,028</u>

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

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Notes to Financial Statements

Note 1 – Organization and Basis of Presentation

The Permanent Health Fund (Fund) is a pooled investment fund established for the collective investment of state endowment funds for health-related institutions of higher education, created August 30, 1999. The distributions from the Fund endowments support programs that benefit medical research, health education, public health, nursing, and treatment programs at health-related institutions of higher education. Fiduciary responsibility for the Fund rests with the Board of Regents of The University of Texas System (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.

On March 1, 2001, the Fund purchased units in the General Endowment Fund (GEF) in exchange for the contribution of its investment assets. The GEF, established by the Board of Regents effective March 1, 2001, is a pooled fund for the collective investment of long-term funds under the control and management of the Board of Regents. The performance of the Fund is significantly impacted by the performance of the GEF. The GEF has only two participants: the Fund and The University of Texas System Long Term Fund (LTF), which was also established by the Board of Regents. The GEF is organized as a pooled investment fund in which the Fund and the LTF purchase and redeem units quarterly. The GEF is under the fiduciary responsibility of the Board of Regents and is provided day-to-day operations by UTIMCO.

The activities of the Fund are accounted for as a fiduciary fund. The financial statements of the Fund use an economic resources measurement focus and the accrual basis of accounting, whereby revenues are recorded when earned and expenses are recorded when a liability is incurred regardless of the timing of cash flows. The financial statements of the Fund are prepared in accordance with the requirements of the Governmental Accounting Standards Board (GASB).

The annual combined financial statements of The University of Texas System are prepared in accordance with the 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 – Investment in GEF

Beginning with the purchase of GEF units on March 1, 2001, the Fund no longer invests in individual securities except for GEF units and a negligible amount of cash. The Fund also continues to receive securities as proceeds in class action suits from the securities the Fund previously owned. These securities are normally sold when received, but from time to time will be reflected as a Fund investment. At August 31, 2007, the Fund is the minority participant in the GEF, with ownership of 6,118,081 units, which represents 17.10% of the GEF. At August 31, 2006, the Fund held 6,359,817 units, which represented 18.18% of the GEF.

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Notes to Financial Statements (cont.)

The GEF and the Fund have identical investment objectives. Additionally, the GEF's accounting policies follow the Fund's, as described in Note 3, except for the distributions to participants. On a monthly basis for accounting purposes, the GEF allocates its net investment income and realized gain or loss to the Fund based on its ownership of GEF units at month end. The allocated investment income and realized gain amounts increase the cost basis of the units in the GEF, and any allocated realized losses reduce the cost basis of the units in the GEF. Since the allocation is proportional to the percentage of ownership by the unitholders, no additional units are purchased. The Fund redeems GEF units quarterly to meet its distribution requirements to its unitholders.

Note 3 – Significant Accounting Policies

(A) **Security Valuation** -- The Fund's investment in GEF units is valued at the net asset value per unit reported by the GEF. Investment assets which are held in the GEF that have readily determinable fair values are primarily valued on the basis of market valuations provided by independent pricing services. The GEF's investments in private market, marketable alternative, U.S. equity, non-U.S. equity, emerging market and fixed income investment funds and certain other equity securities are fair valued by management using partnership capital balances and net asset value information provided by the investment fund or company.

(B) **Investment Income** -- Interest income is accrued as earned.

(C) **Security Transactions** -- A gain or loss is recognized on GEF unit sales on the basis of average cost.

(D) **Distributions to Participants** -- Cash distributions to participants are paid quarterly based on a per unit payout established by the Board of Regents. For the year ended August 31, 2007 the quarterly rate was \$.01240 per unit which equates to an annual rate of \$.0496 per unit and for the year ended August 31, 2006 the quarterly rate was \$.01205 per unit which equated to an annual rate of \$.0482 per unit. The ratio of distributions to average net assets (12-quarter average) was 4.06% as of August 31, 2007. The investment policy provides that the annual payout will be adjusted by the average consumer price index of the prior 36 months subject to a maximum distribution of 5.5% of the Fund's average market value and a minimum distribution of 3.5% of the Fund's average market value.

(E) **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.

(F) **Purchases and Redemption of Units** -- Unit purchases occur on the first business day of each fiscal quarter. Unit redemptions occur on the last business day of each fiscal quarter. The value of participating units, upon admission to the Fund, is based upon the market value of net assets held as of the quarterly valuation date. Redemptions from the Fund will also be made at the market value price per unit at the quarterly valuation date at the time of the withdrawal. There are no transaction costs incurred by participants for the purchase or redemption of units.

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Notes to Financial Statements (cont.)

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

(H) **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.

(I) **Cash and Cash Equivalents** -- Cash and Cash Equivalents consist of money market investments and other overnight funds.

Note 4 – Investment Risk

The investment risk disclosure that follows relates to the GEF's investments before securities lending transactions and the investment of cash collateral. Disclosures relating to the GEF's securities lending transactions are provided in Note 5. Values presented are the Fund's pro-rata share of GEF investments based on its unit ownership in the GEF. As of August 31, 2007 and 2006, the Fund's unit ownership in the GEF was 17.10% and 18.18%, respectively, of the total.

(A) Credit Risk

Article VII, Section 11b of the Texas Constitution authorizes the Board of Regents, subject to procedures and restrictions it establishes, to invest the Permanent University Fund (the "PUF") in any kind of investment and in amounts it considers appropriate, provided that it adheres to the prudent investor standard. This standard provides that the Board of Regents, in making investments, may acquire, exchange, sell, supervise, manage, or retain, through procedures and subject to restrictions it establishes and in amounts it considers appropriate, any kind of investment that prudent investors, exercising reasonable care, skill and caution, would acquire or retain in light of the purposes, terms, distribution requirements, and other circumstances of the fund then prevailing, taking into consideration the investment of all of the assets of the fund rather than a single investment. Pursuant to Section 51.0031(c) of the Texas Education Code, the Board of Regents has elected the PUF prudent investor standard to govern its management of the GEF.

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization (NRSRO). The Fund's investment policy limits investments in U.S. Domestic bonds and non-dollar denominated bond investments to those that are rated investment grade, Baa3 or better by Moody's Investor Services, BBB- or better, by Standard & Poor's Corporation, or BBB- or better by Fitch Investors Service at the time of acquisition. This requirement does not apply to investment managers that are authorized by the terms of an investment advisory agreement to invest in below investment grade bonds. Per GASB Statement No. 40 (GASB 40), *Deposit and Investment Risk Disclosures, an amendment to GASB Statement No. 3*, unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. GASB 40 also provides that securities with split ratings, or a different rating assignment between NRSROs, are disclosed using

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Notes to Financial Statements (cont.)

the rating indicative of the greatest degree of risk. The following table presents the Fund's pro-rata share of each applicable GEF investment type grouped by rating as of August 31, 2007 and 2006:

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Notes to Financial Statements (cont.)

GEF Investment Type	Fund's Pro-Rata Share August 31,		Rating
	2007	2006	
Investments:			
U.S. Government Guaranteed	\$ 50,221,014	\$ 88,831,313	Exempt from Disclosure
U.S. Government Non-Guaranteed:			
U.S. Agency	2,353,221	2,682,186	AAA
U.S. Agency Asset Backed	52,820,112	30,057,998	AAA
Total U.S. Government Non-Guaranteed	55,173,333	32,740,184	
Total U.S. Government	105,394,347	121,571,497	
Corporate Obligations:			
Domestic	7,771,660	5,917,455	AAA
Domestic	2,699,306	956,179	AA
Domestic	3,528,257	3,140,510	A
Domestic	3,010,300	4,058,612	BAA/BBB
Domestic	817,215	820,068	BA/BB
Domestic	400,825	1,057,177	B
Domestic	97,265	31,213	CAA
Domestic	51,449	21,377	CCC
Domestic	25,136	-	P
Domestic	-	1,912	Rating Withdrawn
Commercial Paper	5,574,564	18,541,901	P
Commercial Paper	324,563	22,840,498	A
Certificates of Deposit	1,128,767	-	AA
Foreign	1,343,903	938,548	AAA
Foreign	1,037,829	611,061	AA
Foreign	1,437,275	1,512,200	A
Foreign	1,349,574	1,285,030	BAA/BBB
Total Corporate Obligations	30,597,888	61,733,741	
Foreign Government and Provincial Obligations	6,610,720	6,746,046	AAA
Foreign Government and Provincial Obligations	304,617	2,150,279	AA
Foreign Government and Provincial Obligations	2,377,102	661,842	A
Foreign Government and Provincial Obligations	305,790	348,708	BAA/BBB
Foreign Government and Provincial Obligations	249,297	266,973	BA/BB
Total Foreign Government and Provincial Obligations	9,847,526	10,173,848	
Other Debt Securities	223,512	290,653	AAA
Other Debt Securities	165,828	106,636	AA
Other Debt Securities	91,176	679,497	BAA/BBB
Total Other Debt Securities	480,516	1,076,786	
Total Debt Securities	\$ 146,320,277	\$ 194,555,872	
Other Investment Funds - Debt	\$ 2,846,691	\$ 6,494,927	AAA
Other Investment Funds - Debt	3,672,945	9,403,482	AA
Other Investment Funds - Debt	9,166,928	-	A
Other Investment Funds - Debt	820,765	797,883	BA/BB
Other Investment Funds - Debt	532,270	-	B
Total Other Investment Funds - Debt	\$ 17,039,599	\$ 16,696,292	
Cash and Cash Equivalents - Money Market Funds	\$ 150,942,361	\$ 94,874,160	AAA
Cash and Cash Equivalents - Other	1,369,456	1,182,946	Exempt from Disclosure
Total Cash and Cash Equivalents	\$ 152,311,817	\$ 96,057,106	
Deposit with Brokers for Derivative Contracts:			
U.S. Government Guaranteed	\$ 7,241,395	\$ 8,008,689	Exempt from Disclosure
Cash	239,569	2,342,435	Exempt from Disclosure
	\$ 7,480,964	\$ 10,351,124	
Deposit with Broker for Securities Sold Short:			
Cash	\$ -	\$ 732,697	Exempt from Disclosure
	\$ -	\$ 732,697	

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

(B) Concentrations of Credit Risk

The GEF's investment policy statement contains the limitation that no more than 5% of the market value of domestic fixed income securities may be invested in corporate or municipal bonds of a single issuer. The GEF does not hold any direct investments in any one issuer of corporate or municipal bonds that is 5% or more of the market value of the GEF's domestic fixed income investments.

(C) Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the GEF will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the GEF will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Texas State Statutes and the GEF's investment policy statements do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments. As of August 31, 2007 and 2006, the GEF does not have any deposits or investments that are exposed to custodial credit risk.

(D) Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its value to changes in market interest rates. Interest rate risk inherent in the GEF is measured by monitoring the modified duration of the overall investment portfolio. Modified duration estimates the sensitivity of the GEF's investments to changes in interest rates. The GEF has no specific policy statement limitations with respect to its overall modified duration. The following table summarizes the GEF's modified duration and the Fund's pro-rata share of the GEF investment value by investment type as of August 31, 2007 and 2006:

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Notes to Financial Statements (cont.)

GEF Investment Type	Fund's Pro-Rata Share			
	August 31,			
	2007		2006	
	Value	Modified Duration	Value	Modified Duration
Investments in Securities:				
U.S. Government Guaranteed:				
U.S. Treasury Bonds and Notes	\$ 11,666,079	7.34	\$ 22,433,062	7.28
U.S. Treasury Strips	481,959	3.98	531,603	5.00
U.S. Treasury Bills	1,018,157	0.06	904,935	0.04
U.S. Treasury Inflation Protected	36,740,453	8.63	64,545,590	7.91
U.S. Agency Asset Backed	314,366	5.56	416,123	5.88
Total U.S. Government Guaranteed	<u>50,221,014</u>	8.10	<u>88,831,313</u>	7.65
U.S. Government Non-Guaranteed:				
U.S. Agency	2,114,143	2.18	2,682,186	3.05
U.S. Agency Asset Backed	52,820,112	4.93	30,057,998	5.46
U.S. Agency Commercial Paper	239,078	0.02	-	-
Total U.S. Government Non-Guaranteed	<u>55,173,333</u>	4.80	<u>32,740,184</u>	5.26
Total U.S. Government	<u>105,394,347</u>	6.37	<u>121,571,497</u>	7.00
Corporate Obligations:				
Domestic	18,401,413	4.10	16,054,014	4.41
Commercial Paper	5,899,126	0.18	41,332,888	0.07
Certificates of Deposit	1,128,767	1.16	-	-
Foreign	5,168,582	5.87	4,346,840	11.18
Total Corporate Obligations	<u>30,597,888</u>	3.54	<u>61,733,742</u>	1.98
Foreign Government and Provincial Obligations	<u>9,847,526</u>	5.48	<u>10,173,848</u>	6.52
Other Debt Securities	<u>480,516</u>	11.67	<u>1,076,786</u>	12.30
Total Debt Securities	<u>146,320,277</u>	5.74	<u>194,555,873</u>	5.41
Other Investment Funds - Debt	<u>17,039,599</u>	3.58	<u>16,696,291</u>	3.77
Cash and Cash Equivalents:				
Money Market Funds	150,942,361	0.08	94,874,160	0.08
Other	1,369,456	-	1,182,946	-
Total Cash and Cash Equivalents	<u>152,311,817</u>	0.08	<u>96,057,106</u>	0.08
Total	<u>\$ 315,671,693</u>	2.89	<u>\$ 307,309,270</u>	3.66
Deposit with Brokers for Derivative Contracts:				
U.S. Government Guaranteed:				
U.S. Treasury Bills	\$ 7,241,395	0.15	\$ 7,799,252	0.15
U.S. Treasury Inflation Protected	-	-	209,437	0.36
Total U.S. Government Guaranteed	<u>7,241,395</u>	0.15	<u>8,008,689</u>	0.16
Cash	<u>239,569</u>	-	<u>2,342,435</u>	-
Total Deposit with Brokers for Derivative Contracts	<u>\$ 7,480,964</u>	0.15	<u>\$ 10,351,124</u>	0.11
Deposit with Broker for Securities Sold Short:				
Cash	<u>\$ -</u>	-	<u>\$ 732,697</u>	-

(E) Investments with Fair Values That Are Highly Sensitive to Interest Rate Changes

In accordance with the GEF's investment policy statement, the GEF may invest in various mortgage backed securities, such as collateralized mortgage backed obligations. The GEF also may invest in investments that have floating rates with periodic coupon changes in market rates, zero coupon bonds and stripped Treasury and Agency securities created from coupon securities. No percentage of

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

holdings limitations are specified in the investment policy statements regarding these types of securities. As of August 31, 2007 and 2006, the GEF's investments include the following investments that are highly sensitive to interest rate changes.

Collateralized mortgage obligations which are subject to early payment in a period of declining interest rates. The resultant reduction in expected total cash flows will affect the fair value of these securities. The Fund's pro-rata share of these securities amounted to \$13,253,610 and \$6,563,375 as of August 31, 2007 and 2006, respectively.

Mortgage backed securities which are subject to early payment in a period of declining interest rates. The resultant reduction in expected total cash flows will affect the fair value of these securities. The Fund's pro-rata share of these securities amounted to \$45,348,538 and \$27,693,008 as of August 31, 2007 and 2006, respectively.

Asset backed securities which are backed by home equity loans, auto loans, equipment loans and credit card receivables. Prepayments by the obligees of the underlying assets in periods of decreasing interest rates could reduce or eliminate the stream of income that would have been received. The Fund's pro-rata share of these securities amounted to \$2,283,808 and \$2,407,495 as of August 31, 2007 and 2006, respectively.

Step-up notes that grant the issuer the option to call the note on certain specified dates. At each call date, should the issuer not call the note, the coupon rate of the note increases (steps up) by an amount specified at the inception of the note. The call feature embedded within a step-up note causes the fair value of the instrument to be considered highly sensitive to interest rate changes. The Fund's pro-rata share of these securities amounted to \$421,147 and \$360,658 as of August 31, 2007 and 2006, respectively.

(F) Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of the GEF's non-U.S. dollar investments. The GEF's investment policy statement limits investments in non-U.S. denominated bonds to 50% of the GEF's total fixed income exposure. The following table summarizes the Fund's pro-rata exposure of the GEF's non-U.S. dollar investments at August 31, 2007 and 2006:

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

GEF Investment Type	Fund's Pro-Rata Share	
	August 31,	
	2007	2006
Foreign Common Stock:		
Australian Dollar	\$ 1,802,380	\$ 1,551,517
Canadian Dollar	6,011,020	6,848,226
Swiss Franc	969,185	926,184
Danish Krone	259,136	340,018
Euro	4,621,934	4,065,576
UK Pound	5,811,714	4,951,252
Hong Kong Dollar	1,742,323	2,048,875
Japanese Yen	18,727,270	22,310,803
South Korean Won	-	611,893
New Zealand Dollar	-	66,122
Norwegian Krone	1,161,722	530,783
Swedish Krona	880,307	645,710
Singapore Dollar	356,290	1,042,960
Total Foreign Common Stock	42,343,281	45,939,919
Other - Equity Securities		
Canadian Dollar	-	5
Foreign Government and Provincial Obligations:		
Canadian Dollar	20,653	23,100
Danish Krone	87,955	90,793
Euro	8,001,404	8,140,313
Japanese Yen	516,935	399,895
New Zealand Dollar	59,294	61,147
Polish Zloty	338,170	331,323
UK Pound	89,719	-
Total Foreign Government and Provincial Obligations	9,114,130	9,046,571
Corporate Obligations:		
Canadian Dollar	161,918	-
Danish Krone	236,229	-
Euro	2,069,994	1,992,362
UK Pound	205,185	139,370
Japanese Yen	605,119	311,969
Total Corporate Obligations	3,278,445	2,443,701
Purchased Options:		
Canadian Dollar	-	6,595
Euro	28,114	92,941
UK Pound	2,769	14,082
Japanese Yen	-	306,662
Total Purchased Options	30,883	420,280
Private Market Investment Funds:		
Euro	15,977,261	10,434,168
UK Pound	147,192	496,265
Total Private Market Investment Funds	16,124,453	10,930,433
Cash and Cash Equivalents:		
Australian Dollar	19,803	16,503
Canadian Dollar	179,907	125,270
Swiss Franc	38,640	8,868
Danish Krone	12,667	3,170
Euro	585,729	187,499
UK Pound	228,244	92,237
Hong Kong Dollar	1,781	21,729
Japanese Yen	677,771	952,898
Mexican Peso	1,243	-
Norwegian Kroner	29,621	7,361
New Zealand Dollar	12,582	50,939
Polish Zloty	16,909	36,891
Swedish Krona	16,179	24,633
Singapore Dollar	16,205	20,354
Taiwan Dollar	57	60
Total Cash and Cash Equivalents	1,837,338	1,548,412
Total	\$ 72,728,530	\$ 70,329,321

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

Note 5 – Securities Lending

In accordance with the prudent investor investment standards, the GEF loans securities to certain brokers who pay the GEF negotiated lenders' fees. These fees are included in GEF investment income, and the related expenses are included in investment expenses. The GEF 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 Fund's pro-rata share of the value of GEF securities loaned and the value of collateral held are as follows at August 31, 2007 and 2006:

GEF Securities on Loan	2007 Value	2006 Value	Type of Collateral	2007 Value of Collateral	2006 Value of Collateral
U.S. Government	\$ 35,001,340	\$ 61,313,467	Cash	\$ 35,380,040	\$ 62,383,217
Foreign					
Government	-	2,203,533	Cash	-	2,313,380
Corporate Bonds	1,055,220	868,745	Cash	1,085,021	890,524
Common Stock	28,751,475	19,292,683	Cash	29,939,757	20,110,117
Total	\$ 64,808,035	\$ 83,678,428	Total	\$ 66,404,818	\$ 85,697,238
U.S. Government	\$ 6,120,242	\$ 4,079,466	Non-Cash	\$ 6,225,107	\$ 4,167,536
Corporate Bonds	19,162	-	Non-Cash	19,468	-
Common Stock	2,017,782	137,629	Non-Cash	2,050,010	140,416
Total	\$ 8,157,186	\$ 4,217,095	Total	\$ 8,294,585	\$ 4,307,952

Cash received as collateral for securities lending activities is invested and reinvested in a commingled pool managed exclusively for the benefit of the GEF, the Permanent University Fund, the Intermediate Term Fund and other Board of Regent accounts that participate in securities lending activities. The pool is managed in accordance with investment guidelines established in the securities lending contract between the GEF and its securities lending agent. The maturities of the investments in the pool do not necessarily match the term of the loans, rather the pool is managed to maintain a maximum dollar weighted average maturity of 60 days and an overnight liquidity of 20%. Lending income is earned if the returns on those investments exceed the rebate paid to borrowers of the securities. The income remaining after the borrower rebates is then shared with the lending agent on a contractually negotiated split. If the investment of the cash collateral does not provide a return exceeding the rebate or if the investment incurs a loss of principal, the payment of the shortfall to the borrower would come from the GEF and the securities lending agent in the same proportion as the split of income.

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

The Fund's pro-rata share of the GEF's portion of the collateral pool investments, rating by NRSRO, and weighted average maturity as of August 31, 2007 and 2006 is shown in the following table.

Description	August 31,					
	2007			2006		
	Fund's Pro-Rata Share Fair Value	Rating	Weighted Average Maturity In Days	Fund's Pro-Rata Share Fair Value	Rating	Weighted Average Maturity In Days
Repurchase Agreements	\$ 21,598,148	No Rating		\$ 31,199,406	No Rating	
Commercial Paper	18,210,886	Available	4	37,267,657	Available	14
Floating Rate Notes	4,782,187	P	38	4,890,987	P	26
Floating Rate Notes	13,600,073	AAA		3,512,959	AAA	
Total Floating Rate Notes	<u>18,382,260</u>	AA		<u>8,403,946</u>	AA	
Fixed Rate Notes	211,723		13	-		69
Certificates of Deposit	-	AAA	105	-	-	-
Asset Backed Securities	8,113,781	-	-	10,722,413	P	67
Asset Backed Securities	84,785	AAA		153,692	AAA	
Total Asset Backed Securities	<u>8,198,566</u>	P		<u>153,692</u>	-	
Other Receivables/Payables	(196,765)		32	(2,049,877)		11
Total Collateral Pool Investment	<u>\$ 66,404,818</u>	Not Rated	-	<u>\$ 85,697,237</u>	Not Rated	-
			20			31

Collateral pool investments are uninsured, and are held by the securities lending agent, in its name, on behalf of the GEF, except for the investments in repurchase agreements which are held in the securities lending agent's name by a third party custodian not affiliated with the GEF or the borrower of the associated loaned securities. Therefore, the collateral pool is not exposed to custodial credit risk because the pool investments are not held by counterparties to the lending transactions or a counterparties' trust department or agent.

Cash collateral is recorded as an asset with an equal and offsetting liability to return the collateral on the statements of fiduciary net assets. 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.

In the event of default, where the borrower is unable to return the securities loaned, the GEF has authorized the securities lending agent to seize the collateral held. The collateral is then used to replace the borrowed securities where possible. Due to some market conditions, it is possible that the original securities cannot be replaced. If the collateral is insufficient to replace the securities, the securities lending agent has indemnified the GEF from any loss due to borrower default.

As of August 31, 2007 and 2006, the GEF had no credit risk exposure to borrowers because the amounts the GEF owed to borrowers exceeded the amounts the borrowers owed the GEF.

There were no significant violations of legal or contractual provisions, no borrower or securities lending agent default losses, and no recoveries of prior period losses during the years ended August 31, 2007 and 2006.

PERMANENT HEALTH FUND

Notes to Financial Statements (cont.)

Note 6 – Fees and Expenses

The Fund is assessed a management fee by UTIMCO to cover the costs of managing the Fund and providing day-to-day operations. The fee assessed for the year ended August 31, 2007, was \$839,949. The fee assessed for the year ended August 31, 2006, was \$528,017, net of a rebate of \$176,800 of excess reserves from UTIMCO to the Fund.

The Fund is assessed a fee to cover costs associated with UT System personnel in their effort to provide assistance to the Board of Regents and the Chancellor of the UT System in their oversight responsibilities of UTIMCO. For the years ended August 31, 2007 and 2006, the fees amounted to \$44,548 and \$46,295, respectively.

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

PERMANENT HEALTH FUND
Supplemental Schedule

Financial Highlights
Years Ended August 31,

	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
Selected Per Unit Data					
Net Asset Value, Beginning of Year	\$ 1.204	\$ 1.129	\$ 0.993	\$ 0.908	\$ 0.852
Income From Investment Operations					
Net Investment Income	0.023	0.022	0.023	0.019	0.017
Net Realized and Unrealized Gain on Investments	<u>0.165</u>	<u>0.101</u>	<u>0.160</u>	<u>0.113</u>	<u>0.086</u>
Total Income from Investment Operations	<u>0.188</u>	<u>0.123</u>	<u>0.183</u>	<u>0.132</u>	<u>0.103</u>
Less Distributions					
From Net Investment Income	0.023	0.022	0.023	0.019	0.017
From Net Realized Gain and In Excess of Net Realized Investment Return	<u>0.027</u>	<u>0.026</u>	<u>0.024</u>	<u>0.028</u>	<u>0.030</u>
Total Distributions	<u>0.050</u>	<u>0.048</u>	<u>0.047</u>	<u>0.047</u>	<u>0.047</u>
Net Asset Value, End of Year	<u>\$ 1.342</u>	<u>\$ 1.204</u>	<u>\$ 1.129</u>	<u>\$ 0.993</u>	<u>\$ 0.908</u>
Ratios and Supplemental Data					
Net Assets, End of Year (in thousands)	\$ 1,100,056	\$ 987,028	\$ 925,898	\$ 814,424	\$ 744,961
Ratio of Expenses to Average Net Assets	0.28%	0.39%	0.32%	0.31%	0.27%
Ratio of Net Investment Income to Average Net Assets	1.78%	1.88%	2.13%	1.92%	2.01%
Ratio of Distributions to Average Net Assets (5-quarter average)	3.86%	4.13%	4.39%	4.81%	5.48%
Ratio of Distributions to Average Net Assets (12-quarter average)	4.06%	4.36%	4.79%	5.14%	5.08%