

**MINUTES
UNIVERSITY OF HOUSTON SYSTEM
BOARD OF REGENTS
ENDOWMENT MANAGEMENT COMMITTEE**

Tuesday, August 16, 2011 - The members of Endowment Management Committee of the University of Houston System convened at 1:02 p.m. on Tuesday, August 16, 2011, at the Hilton University of Houston Hotel, Waldorf Astoria Ballroom E, Second Floor, Houston, Texas, with the following members participating:

ATTENDANCE –

Present

Jarvis V. Hollingsworth, Chair
Jim P. Wise, Vice Chair
Carroll Robertson Ray, Ex Officio
Michael J. Cemo, Advisory Member
J. Christopher Jones, Advisory Member

Member(s) Absent

Mica Mosbacher, Member

In accordance with a notice being timely posted with the Secretary of State and there being a quorum present, the Chair of the Committee, Jarvis V. Hollingsworth, called the meeting to order.

For the record and in line with our investment policy, Regent Hollingsworth stated there had been specific actions taken with regards to a couple of managers in the Endowment Fund:

- During the May committee meeting, the committee agreed to delegate authority to Regent Hollingsworth regarding a recommendation by Cambridge to invest an additional \$5.8 million with Wellington Diversified Inflation Hedge. This recommendation was approved and the investment was made effective July 1, 2011.
- During the June monthly performance conference call, Cambridge notified the committee participants that the portfolio manager for the REIT product, in which we invested, was leaving the firm. Given this significant personnel change, the committee members on the call agreed that Salient should be terminated immediately. Salient was terminated effective June 30, 2011. Cambridge recommended investing the \$3.6 million of Salient proceeds in State Street Global Advisors, our existing indexed, large cap equity manager. This action was completed on July 14, 2011.

After these actions were announced, Regent Hollingsworth continued with the meeting.

The first item requiring committee approval was the approval of the minutes from the Endowment Management Committee meeting held on Tuesday, May 17, 2011.

AGENDA ITEMS

Action Items

1. Approval of Minutes – Item B

On motion of Regent Wise, seconded by Regent Ray and by a unanimous vote of the committee members in attendance, the following minutes from the meeting listed below were approved:

- May 17, 2011, Endowment Management Committee Meeting

Regent Hollingsworth noted there were four additional action items on the agenda and introduced the next item.

2. Resolution in Appreciation – Michael J.Cemo – University of Houston System – EM-C

Regent Hollingsworth presented this item to the committee. Below is a summary of his remarks:

- Mr. Cemo was appointed as an advisory member of the Endowment Management Committee of the University of Houston System Board of Regents in April 2008, serving three (3) consecutive one-year terms until August 31, 2011;
- Mr. Cemo was the first advisory member appointed unanimously by the Chair of the Board, the Chancellor of the UH System, and the Chair of the Endowment Management Committee;
- Mr. Cemo had applied his vast experience and knowledge during his term of service and was involved in various investment policy reviews that led to improvements in the oversight of the UH System's investment portfolio, engaged in the process of restructuring the domestic equity, fixed income, and hedge fund asset classes to enhance risk-adjusted returns over time, and recommended increased exposure to additional asset classes to diversity portfolio risk;
- Mr. Cemo advocated for increased funding of university advancement operations to further increase the size of the endowment for the benefit of current and future generations of students, focused on peer comparison to benchmark the endowment's performance, and was involved in the decision to expand the investment consultant's role in the endowment, which has led to improved returns relative to our peer group;
- Mr. Cemo, a proud alumnus of the University of Houston, had previously served the institution with diligence, commitment, and vision for a six-year term as a Member of the UH System Board of Regents, including terms as Secretary and Vice Chair; and
- The Endowment Management Committee of the University of Houston System Board of Regents issued the resolution in appreciation of Mr. Cemo's committed and distinguished service to the University of Houston System Board of Regents.

On motion of Regent Wise, seconded by Regent Ray and by a unanimous vote of the committee members in attendance, the Resolution in Appreciation for Michael J. Cemo was approved by the committee. This item requires committee approval only.

3. Resolution in Appreciation – J. Christopher “Chris” Jones – University of Houston System – EM-D

Vice Chair of the Committee, Jim P. Wise presented this item to the committee. Below is a summary of his remarks:

- Mr. Jones served as an advisory member of the Endowment Management Committee of the University of Houston System Board of Regents for the years 2008-2009, 2009-2010, and 2010-2011;
- Mr. Jones was the second advisory member appointed unanimously by the Chair of the Board, the Chancellor of the UH System, and the Chair of the Endowment Management Committee;
- Mr. Jones had applied his vast experience and knowledge during his term of service and was involved in various investment policy reviews that led to improvements in the oversight of the UH System’s investment portfolio, engaged in the process of restructuring the domestic equity, fixed income, and hedge fund asset classes to enhance risk-adjusted returns over time, and recommended increased exposure to additional asset classes to diversity portfolio risk;
- Mr. Jones supported funding of university advancement operations to further increase the size of the endowment for the benefit of current future generations of students, focused the endowment to raise its exposure to private equity to be in line with its peer group in order to improve its long-term returns, and was involved in the decision to expand the investment consultant’s role in the endowment, which has led to improved returns relative to our peer group; and
- The Endowment Management Committee of the University of Houston System Board of Regents issued the resolution in appreciation of Mr. John’s committed and distinguished service to the University of Houston System Board of Regents.

On motion of Regent Ray, seconded by Regent Wise and by a unanimous vote of the committee members in attendance, the Resolution in Appreciation for J. Christopher “Chris” Jones was approved by the committee. This item requires committee approval only.

Information/Approval Items

4. Report and Recommendations from Cambridge Associates Regarding Endowed and Non-Endowed Assets – University of Houston System, Item E – EM-E

Regent Hollingsworth asked Hamilton Lee, from Cambridge Associates, to brief the committee on the performance of the endowed and non-endowed assets since the Endowment Management Committee’s last meeting held on May 17, 2011.

Below is an executive summary of Mr. Lee’s remarks:

Mr. Lee’s discussion points highlighted key performance of the Endowment and included a market commentary. Despite rallying in late June, broad-based global equity and domestic equity markets ended the second quarter flat with the MSCI World and S&P 500 returning 0.5% and 0.1%, respectively (all returns in U.S. \$ terms). Commodities sustained a

significant correction, losing almost 8.0% for the quarter on fears of an economic slowdown. U.S. Treasuries were up 2.4%, and the dollar ended the quarter down 1.8% in trade weighted terms.

The University of Houston's Endowment returned 1.0% for the quarter, besting both the Implementation and Dynamic Benchmarks by 90 bps. For the trailing one-year period, the Endowment has gained 19.3%, due to strong performance from U.S. equities (+34.6%), global equities (+27.6%), and inflation hedging assets (+23.4%). The portfolio benchmarks, approved at the May meeting were reflected in the University's performance reports. The Benchmark Update section reiterated the composition of these approved benchmarks and outlined minor changes that had been made to the inflation hedging components of both benchmarks. Additionally, a Watch List benchmark legend had been included in order to specify the applicable manager benchmark that would be used for Watch List purposes. In future discussion materials, this exhibit will be included along with the Watch List. This issue was discussed at length.

Mr. Lee outlined the decision items and recommendations that the committee would address at the meeting:

1. Approve changes to both the composite inflation hedging benchmark and Wellington Diversified Inflation Hedges portfolio benchmark;
2. Approve a \$1.5 million partial redemption from York Capital Management;
3. Approve a \$6.0 million investment in absolute return manager, Covalent Capital Partners (Offshore), L.P.; and
4. Approve \$4.0 million commitment to Denham Commodity Partners VI, L.P.

Mr. Jeff Blazek, from Cambridge Associates, gave the committee an overview of the current market. Below is a brief summary of his remarks:

- Flat quarter for U.S. equities; significant drop in commodity prices in 2Q;
- Equities by Country and U.S. Sector were addressed with strong gains in France and Germany but U.S. financials weak;
- U.S. recovery is unusually soft, relative to the substantial size of the recession;
- Greek bond insurance has surged; Euro relatively stable;
- S&P 500 earnings are approaching all-time highs; and cash continues to build;
- Small businesses are not bouncing back which is not an ideal situation for job creation;
- Consumers remain under pressure – inflation is hindering spending, while wages are sluggish;

An update and summary on composite benchmark was addressed. Modified benchmarks approved at the May 17, 2011 meeting are now in place. Flash and Performance Reports now incorporate the following benchmarks:

1. Implementation Benchmark
2. Dynamic Benchmark
3. CPI + 5.5% Benchmark

An updated Composite Benchmark was included in the report and the only change in this composite versus the May meeting version was changing the inflation hedge portfolio

benchmark from “Wellington DIH” to a “Custom IH Benchmark” that Cambridge believes is more appropriate. The Custom IH Benchmark is an equal weighted blend of TIPS, commodities, REITS, and natural resource equities.

The Watch List Legend which formally identifies how each individual manager will be measured for Watch List purposes will be included in the Watch List section in future materials.

Gene Lohmeyer, from Cambridge Associates, presented the committee with the Hedge Fund Program recommendations for consideration and approval. Mr. Lohmeyer stated Cambridge recommended that the University of Houston invest \$6.0 million with Covalent Capital Partners, an opportunistic, event-driven hedge fund focused on companies and industry sectors undergoing turmoil. The fund’s key characteristics are as follows:

- Talented and experienced investment team;
- Flexible and opportunistic mandate; and
- Modest fund size

Cambridge believes that Covalent is an excellent complement to the University’s existing hedge fund holdings based on the investment team’s ability to pursue smaller, less publicized event-driven opportunities and the fund’s historically low correlation to other hedge funds and broad equity markets.

The summary of the Covalent Capital Partners’ terms are as follows:

- Management Fee – 1.75%
- Incentive Fee – 20%
- Liquidity – Quarterly with 60 days’ notice, 25% investor level gate

Mr. Lohmeyer also addressed the rebalancing of the hedge fund portfolio recommending a \$1.5 million redemption from York Capital Management as of December 31, 2011; notice is due by November 15, 2011.

On a motion from Regent Ray, seconded by Regent Wise, and by a unanimous vote of the committee members in attendance, the committee approved the delegation of authority to the Chancellor to negotiate and execute a contract for the hiring of Covalent Capital Partners and the recommendation that the University of Houston invest \$6.0 million for the University of Houston System Endowment Fund. This recommendation required committee approval only.

On a motion from Regent Ray, seconded by Regent Wise, and by a unanimous vote of the committee members in attendance, the recommendation to rebalance the hedge fund portfolio by approving a \$1.5 million redemption from York Capital Management as of 12/31/2011 was approved. This recommendation required committee approval only.

Regent Hollingsworth requested a 10 minute recess at 2:25 p.m.; and at 2:35 p.m. Regent Hollingsworth reconvened the committee meeting.

Mr. Phil Fiske, from Cambridge Associates, presented the committee with the recommendation that the University of Houston commit \$4.0 million to Denham Commodity Partners Fund VI, LP.

There were several issues discussed regarding this recommendation:

- Denham's vision and global expansion plans differentiates the manager from other energy managers who are focused on the United States. The key for Denham is to remain focused on familiar risks, reproduce their successful model, and source deals through the firm's well-connected team of professionals.
- Denham is comfortable with more risk than other managers focused on the energy sector. The distribution of returns is biased toward the positive end of the range, which is evidence of Denham's efforts to structure deals to limit downside. Diversity of asset types, management teams, regions and industries, together with the firm's intensive risk management program, may ultimately outweigh any additional risks introduced by Denham's strategy.

Mr. Fiske stated that Denham is an attractive investment opportunity and would provide the University of Houston's private investments portfolio with diversified exposure to natural resources, a segment of the market that Cambridge views as particularly attractive in today's market environment. A lengthy discussion followed.

The summary of Denham's Commodity Partners Fund VI, LP expected terms are as follows:

- Management Fee – 2.0% on commitments up to \$2.0 billion and 1.75% on commitments above \$2.0 billion. After commitment period, 1.5% on net invested capital
- GP Commitment – 2.0%
- Carried Interest – 20% after 8% preferred return
- Fee Sharing – 100% to LPs, offset against management fees
- Investment Period – 5 years after the final closing.

On a motion from Regent Wise, seconded by Regent Ray, and by a unanimous vote of the committee members in attendance, the committee agreed to delegate to Regent Hollingsworth authority regarding the proposed \$4.0 million investment in Denham Commodity Partners Fund VI, LP and the recommendation to delegate authority to the Chancellor to negotiate and execute a contract for the hiring of Denham Commodity Partners Fund VI, LP. Regent Hollingsworth stated that additional due diligence needs to be completed on this manager before any decision is made to invest in this fund. This recommendation requires committee approval only.

There being no further business to come before the Committee, the meeting adjourned at 3:02 p.m.

All documentation submitted to the Committee in support of the foregoing action items, including but not limited to "Passed" agenda items and supporting documentation presented to the Committee, is incorporated herein and made a part of these minutes for all purposes; however, this does not constitute a waiver of any privileges contained herein.

Others Present:

Renu Khator
Carl Carlucci
Dona Cornell
Barbara Stanley
Lisa Holdeman
Troy Golden
Gerry Mathisen

Hamilton Lee
Jeff Blazek
Raymond Bartlett
Eli Cipriano
Ed Jones
Philip Aldrich

Gene Lohmeyer
Phil Fiske
Tom Ehardt
T. J. Weinardi
Jon Aldrich
Marquette Hobbs