MINUTES
UNIVERSITY OF HOUSTON SYSTEM
BOARD OF REGENTS
ENDOWMENT MANAGEMENT COMMITTEE

Monday, May 13, 2013 – The members of the Endowment Management Committee of the University of Houston System convened at 1:45 p.m. on Monday, May 13, 2013, at the Hilton University of Houston Hotel, Waldorf Astoria Ballroom E, Second Floor, Houston, Texas, with the following member(s) and alternate member(s) participating. Three (3) committee board members were unable to attend the meeting. Nelda Luce Blair, Chair of the UH System Board of Regents, appointed two (2) alternate committee board members; therefore, constituting a quorum of the committee for this meeting.

ATTENDANCE –

Present
Jarvis V. Hollingsworth, Vice Chair
Spencer D. Armour III, Alternate Member
Roger F. Welder, Alternate Member

Non-Member(s) Present
Welcome W. Wilson, Jr., Regent
Gage A. Raba, Student Regent

Member(s) Absent
Mica Mosbacher, Chair
Jacob M. Monty, Member
Nelda Luce Blair, Ex Officio
Carroll Robertson Ray, Advisory Member
Jim P. Wise, Advisory Member

In accordance with a notice being timely posted with the Secretary of State and there being a quorum in attendance, in absence of the Chair of the Committee, Mica Mosbacher, Vice Chair, Jarvis Hollingsworth called the meeting to order.

The first item requiring committee approval were the minutes from the Endowment Management Committee meeting held on Monday, January 28, 2013.

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AGENDA ITEMS

Action Items:

1. Approval of Minutes – Item B

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

   - January 28, 2013, Endowment Management Committee Meeting

Action/Information Items:

Regent Hollingsworth noted there were several action items and three (3) information items on the agenda; and stated the committee would hear presentations from Cambridge Associates; recommendations to liquidate three (3) endowments; reports on the UH System Capital Campaign, UH System Organizations, and the UH System's Invested Funds and Bank Deposits.

Ms. Eloise Dunn Stuhr, Vice Chancellor for University Advancement was asked to present the first two information items to the committee as follows.

1. Report on UH System Capital Campaign – University of Houston System, Item C – EM-C1

   Ms. Stuhr provided the committee with a powerpoint presentation on the UH System Capital Campaign. Below is a brief summary of Ms. Stuhr's report.
   - The University of Houston is currently in year one (1) of a seven (7) year capital campaign. There are three phases to the campaign timeline:
     (a) Planning Phase;
     (b) Quiet Phase; and
     (c) Public Phase.
   - A Campaign Planning Committee has been recruited that will transform into the full Campaign Volunteer Planning Committee. There are currently 13-members on the committee and their first meeting was held on May 9, 2013. This committee is currently charged with providing advice, assistance, posting, and thinking through the ways in which this campaign takes form.
   - The Campaign Planning Committee could have up to 20-members; and during the specific campaign it would be expected to have approximately 200-300 volunteers who would be actively engaged in spreading the word throughout Houston, the nation and the world.
   - The campaign budget was addressed. This campaign cannot be done without a significant infusion of resources.
   - The Branding and Marketing Campaign will be launched shortly and will provide the initial enthusiasm for the constituency in order to embrace this campaign.
   - The firm 160 Over 90 was addressed. They are working with the University of Houston in order to think of new and creative ways to think of Houston and launch our campaign.
   - A Board of Visitors is being formed and will be launched in September 2013. This is not a fundraising board, but one which is a large board which has ambassadorial functions within the community.

   A complete copy of Ms. Stuhr's powerpoint presentation has been filed in the Board office.

   This item was presented for information only and required no committee action.

2. Report on UH System Organizations – University of Houston System, Item D – EM-D5
   - Compliance Review of UH System Support Organizations
   - UH System Support Organizations Report

Ms. Stuhr presented this item to the committee. Board of Regents Policy 32.06 requires an annual report on compliance of private support organizations and foundations. Ms. Stuhr requested Don Guyton, Chief Audit Executive, brief the committee on this issue. Below is a summary of Mr. Guyton's remarks.

- This item refers to the compliance review of the UH System Support Organizations and the UH System Support Organizations Report.
- The compliance review of the UH System Support Organizations indicates the status of the receipt of this information.
- Some of the information from some the foundations have not been received to date.
- The UH System Support Organizations Report is a compilation of information from audited financial statements, IRS Forms 990, investment reports, and other information furnished to the UH System by the Support Organizations.
- The purpose of this report was to provide information on Support Organizations' activities and the Board of Regents and UH System's responsibilities with respect to the foundations.
- The regents' fiduciary responsibilities to the UH System related to these organizations are addressed in agreements between the UH System and the Support Organizations. In meeting the requirements of the Board of Regents' policy on Support Organizations, the UH System implemented a policy on Support Organizations which requires the Support Organizations to furnish certain information to the UH System. This requirement is spelled out in the UH System agreements with the Support Organizations.
- The UH System has been in the process of trying to update these agreements for some time and listed on these reports was the last time these agreements had been updated.

Ms. Stuhr updated the committee on the status of the Support Organizations' agreements and reported that they were in the final stages of reaching an agreement with all of the Support Organizations. Some of these agreements date back to 1999 with the most recent ones being signed in 2006. This has been a long process and much discussion regarding the assessment which was originally designed to be in perfect harmony with the assessment being charged on the University's endowment. There had also been a discussion on the ex officio membership and the respective responsibilities of the Support Organizations versus the University. It is anticipated that all of the signed agreements will be completed and presented at the August 14, 2013 Board of Regents meeting. A brief discussion followed.

This item was presented for information only and required no committee action.

Following the presentation of the two (2) information items, Ms. Stuhr presented the following three (3) action items for the committee's consideration.

3. Approval is requested to liquidate the John J. and Rebecca B. Moores University Priorities Endowment Fund – University of Houston System, Item E – EM-E10

   Ms. Stuhr stated that in accordance with UH System Policy 3.F.02, Section 3.15.3, approval was requested to liquidate the John J. and Rebecca B. Moores University Priorities Endowment Fund currently invested in the UH System Endowment. This endowment had a market value of $21.3 million as of March 31, 2013. This was initiated at the request of the donors in order to free the money to be used for University priorities as designated by the President of the University of Houston.

Mr. Bartlett stated that when the endowment has been dissolved, the funds will then be deposited into an unrestricted fund and used at the discretion of the President for University priorities.

On motion of Regent Armour, seconded by Regent Welder, and by a unanimous vote of the committee members in attendance, the approval to liquidate the John J. and Rebecca B. Moores University Priorities Endowment Fund was approved.

4. <u>Approval is requested to liquidate the Jayne and Albert H. Wiggins Music Scholarship Endowment and transfer the proceeds to the University of Houston Foundation – University of Houston System, Item F – EM-F11</u>.

   Ms. Stuhr requested approval to liquidate the Jayne and Albert H. Wiggins Music Scholarship Endowment and transfer the proceeds to the University of Houston Foundation. This was an endowment that was set up with the stipulation that the recipients are U.S. citizens, which by law, we are no longer allowed to accept and so it is requested that this fund be liquidated and transferred to the University of Houston Foundation. There are no known family members to notify. The spouse is deceased and there were no other known relatives.

   Dr. Carlucci stated the market value of the endowment as of January 31, 2013 was $132,085.

On motion of Regent Welder, seconded by Regent Armour, and by a unanimous vote of the committee members in attendance, the approval to liquidate the Jayne and Albert H. Wiggins Music Scholarship Endowment and transfer the proceeds to the University of Houston Foundation was approved.

5. <u>Approval is requested to partially liquidate the Bill D. Cook Faculty Scholars Endowment in Mechanical Engineering - University of Houston System, Item G – EM-G12</u>

   Ms. Stuhr requested approval to partially liquidate the Bill D. Cook Faculty Scholars Endowment in Mechanical Engineering. The current value is $461,000. The new corpus amount once liquidated would be $400,000 and the proceeds would be transferred to a fund in the Mechanical Engineering Department and used to provide support to junior faculty support consistent with the original agreement while allowing the remaining value of the endowment to grow to provide a sustainable income distribution in future years. The donor and the UH System recently revised the agreement to prevent further principal reductions in order to preserve the endowment in perpetuity at a corpus amount of $400,000.

On motion of Regent Welder, seconded by Regent Armour, and by a unanimous vote of the committee members in attendance, the approval to liquidate the Bill D. Cooke Faculty Scholars Endowment in Mechanical Engineering was approved.

At the conclusion and presentation of the three (3) approval items, Regent Hollingsworth requested a motion to place these three (3) action items on the Board's Consent Docket Agenda for final board approval.

On motion of Regent Armour, seconded by Regent Welder, and by a unanimous vote of the committee members in attendance, the following three (3) action items, approved by the committee, will be placed on the Board's Consent Docket Agenda at the Board of Regents meeting scheduled for May 14, 2013 for final board approval.

(a) Approval is requested to liquidate the John J. and Rebecca B. Moores University Priorities Endowment Fund – University of Houston System;
(b) Approval is requested to liquidate the Jayne and Albert H. Wiggins Music Scholarship Endowment and transfer the proceeds to the University of Houston Foundation – University of Houston System; and
(c) Approval is requested to partially liquidate the Bill D. Cook Faculty Scholars Endowment in Mechanical Engineering – University of Houston System.

Regent Hollingsworth moved to the remaining three (3) items listed on the agenda, and asked Dr. Carlucci, Executive Vice Chancellor for Administration and Finance to introduce these items to the committee.

6. Report and Recommendations from Cambridge Associates Regarding Endowed and Non-Endowed Assets – University of Houston System, Item H – EM-H13.

Dr. Carlucci introduced this item and requested Hamilton Lee and Shannon Thomas, both from Cambridge Associates, give an update to the committee regarding this item.

Mr. Lee stated there were several items to address before the committee and asked Shannon Thomas to give the committee an overview of the Executive Summary. Below is a brief summary of Ms. Thomas' remarks:

- As of March 31, 2013, the University of Houston's portfolio gained 4.4%, which was in line with the Implementation Benchmark; and 7.6% for the quarter and trailing one-year, respectively, outperforming the Dynamic Benchmark by 10 bps and 40 bps, respectively.
- Over the trailing one-year, the portfolio had outpaced the inflation + 5.5% spending rate for the trailing one-year by 60 bps.
- Global developed equities continue to surge, while emerging markets equities and bonds lag.
- The S&P 500 price index hit an all-time high, but remains well below its inflation-adjusted peak.
- Japan's economic forecasts have jumped, driven by recent Bank of Japan initiatives and Yen weakness.
- The U.S. recovery has gained momentum across consumer spending, job growth, and household wealth, while Europe remains challenged. Unemployment continues to diverge between Germany and other Euro constituents.

- Foreign Holders and the Fed have funded the vast majority of Treasury debt growth over the last 20 years. In 1993, Foreign Holders comprised 18% of the treasury securities outstanding, in contrast with 48% in 2012.
- Cambridge Associates' Current Valuations Summary was briefly discussed.

Mr. Lee presented the committee with an Asset Allocation Review and mentioned the University of Houston System's Investment Policy Guidelines states the Endowment Management Committee is required to review asset allocation annually in order to ensure the allocation targets are appropriate to meet the endowment's return objectives with a minimum of risk. Below is a brief summary of Mr. Lee's remarks on this issue.

- Every five (5) years there should be a very comprehensive review of asset allocation completed. In 2010, an extensive, quantitative analysis was done; but the policy also stipulates that once a year the asset allocation be reviewed to make certain we are keeping within our objectives for the portfolio.
- Cambridge Associates discussed some qualitative and quantitative tools they have been developing over the past few years. Collectively they refer to these tools as the Risk Allocation Framework. This is the new way of assessing risks to the portfolio both at the total portfolio level from the standpoint of asset allocation, but also in terms of active risks and implementation risks at the manager selection and implementation levels.
- Their review was segmented into three (3) sections:
  - (a) Asset Allocation vs. Current Return Objectives – The objectives used here were 5.5% over the long period which was broken up into 4.0% payout plus 1.5% assessment fee;
  - (b) Asset Allocation vs. Peers – While each university's circumstances are unique and decisions should not be made based simply on what others are doing, it is nonetheless informative to understand how other institutions with similar assets and similar objectives have allocated their portfolios; and
  - (c) Enterprise Review – This analysis attempts to define how the endowment fits into the broader financial picture of the whole University, including budgetary dependence on the endowment and how the endowment relates to other financial obligations of the System. This has philosophical implications for the role of the endowment, its objectives, and the level of risk necessary to assume in order to achieve them.
- Manager selection and implementation are an important component of return enhancement.
- Low portfolio volatility (defensive portfolio – 20/80) versus high portfolio volatility (aggressive portfolio – 80/20).
- The assessment of short-term risk, in terms of the probability of significant loss (20%+) at any point during a short-term time (5 years) horizon and long-term risks, in terms of the probability of failing to earn (in real terms) the policy spending rate over a long-term horizon, was addressed. Under the short-term risk category, UH is assuming a moderate level of short-term risk at 34% (lower is better) versus the long-term risk at 52% (lower is better). The University of Houston is in between a defensive (60/40 equity to fixed income) and aggressive (80/20) portfolio; but it's still a 52% likelihood that UH will be unable to hit the 5.5% real return target.

- Mr. Lee pointed out that every incremental bit of return moves the needle in a large way; so if the asset allocation were reduced, for example to 5.0%, he believes the numbers would shift down to 44% risk of not hitting that target over a 20-year period.
- The other elements of this analysis was taking a look at what other risks were facing the portfolio, not just in terms of short-tem or long-term volatility, but liquidity risk, maverick risk, and other forms of sensitivity to inflation or interest rates.
- As of March 31, 2013, the liquidity of the UH portfolio was reviewed and it is an extremely liquid portfolio. Even in a worst case scenario, the portfolio maintains sufficient liquidity despite the increasing allocation to private investments.
- The Peer Group Analysis was addressed. The most useful peer comparison was one across institutions with similar resources, similar objectives, and similar constraints.
  - Public universities face different constraints from private ones, which may influence asset allocation decisions.
  - The degree of reliance on the endowment for a university's total operating budget can have significant influence on the way the portfolio is allocated, so the most useful peer group may be one that accounts for this factor as well.
- For Cambridge's Peer Group analysis, two separate peer groups were created.
  - College and University (C&U) endowments between $500m and $700m. This represents institutions with similar assets, and, presumably, similar resources to dedicate to investment management, similar scale to access top managers, etc.
  - Public Colleges and Universities whose payout represents 4% or less of the overall operating budget. This group further expands the range of assets in order to encompass institutions with similar budgetary and other constraints. A discussion followed.
- An Enterprise Review was conducted by Cambridge. Understanding how the endowment relates to the budget, operating, and risk considerations of the University as a whole is fundamental to reviewing the strategic asset allocation of the portfolio.
- Observations on the University of Houston's financial structure were addressed. Overall, Cambridge stated the University of Houston appears to be in a strong financial position, and does not depend heavily on its endowment to support operations. The endowment represents 3% of the annual budget, and there are multiple other sources of revenue available to the University.
- Cambridge asked the committee that given the health of the university, and the fact that the budget does not turn on what happens with the endowment, Cambridge believes the university could take on more short-term risk, and not just in the form of volatility but in the form of illiquidity and other areas in order to reduce the long-term risk of not growing the endowment in real terms. This was a recommendation from Cambridge, but they wanted the committee to review this scenario to see if this, in fact, was the direction the committee would like to go. If so, Cambridge's objective at the August 13, 2013 meeting would be to present a recommendation for changes to the long-term allocation targets for the committee's consideration. A discussion followed.

Mr. Lee introduced Phil Fiske, from Cambridge Associates, to give his recommendation concerning private equity managers.

Mr. Fiske recommended that the University of Houston approve a commitment of $4.0 million to Great Hill Equity Partners V, L.P. ("Fund V"). Great Hill Partners is seeking $1.0 billion in commitments, with a maximum capitalization of $1.25 billion, for its fifth fund. This firm focuses on growth equity but they particularly focus on technology such as digital media, e-commerce, Internet infrastructure, financial services, healthcare information technology, and software companies.

Great Hill will invest predominately in North American companies and is restricted from investing greater than 20% of the fund outside the U.S. However, the firm has selectively invested in international companies that operate in sectors the firm knows well. Fund II had the highest percentage of capital invested outside North America at 12.3%; Fund IV had invested just under 10% as of December 31, 2012.

A commitment to Great Hill Partners V represents an opportunity for the University of Houston to establish a relationship with a quality growth equity manager. The senior investment team is experienced and cohesive and they have been together since 2002. They employ a thesis-driven sourcing model and all investment professionals, including principals, vice presidents, and associates, are encouraged to put forth new investment ideas or initiatives. Associates and vice presidents are primarily responsible for pursuing research around new theses and developing a list of target companies. However, unlike other firms, partners will often reach out to target companies very early in a process, which helps the firm win deals against other firms where outreach is consigned mostly to associates.

Mr. Fiske summarized Great Hill Partners V terms were as follows:

- Target Fund Size - $1.0 billion/$1.25 billion hard cap
- GP Commitment – $30,000,000
- Management Fee – 2% years 1-6; reduced fee years 7-10; weighted average 1.78%
- Carried Interest – 20% of net profits
- Fee Offset – 100% of investment banking, consulting or directors' fees
- Investment Period – 5 years from the commencement date.

Mr. Fiske also made mention to the committee that Cambridge had recently become aware of an outstanding suit in one of their portfolio companies and that complaint against the company was amended to include Great Hill Partners as a party to that suit.

Regent Hollingsworth called for a motion to approve this private equity investment manager.

On motion of Regent Welder, seconded by Regent Armour and by a unanimous vote of the committee members in attendance, the recommendation to invest $4.0 million in Great Hill Equity Partners V, L.P. was approved. This action requires committee approval only and no further board action was required.

Mr. Gene Lohmeyer, from Cambridge Associates, presented the committee with a hedge fund program update and a recommendation for full redemption from Maverick Capital as of September 30, 2013, which will require notice prior to July 30, 2013. A replacement recommendation will be made at the August 13, 2013 Endowment Management Committee meeting.

As of March 31, 2013, the University of Houston's hedge fund allocation had generated over 70% of the return of global equities on a 1- and 3- year basis with less than 1/3rd of the risk while outperforming the HFRI benchmark by approximately 400 basis points.

A recommendation of a full redemption from Maverick Capital was addressed by Mr. Lohmeyer. Maverick recently informed Cambridge Associates that one of the firm's senior investment professionals, Mike Pausic, had resigned and would be launching his own hedge fund after 16 years with the firm. In conjunction with Mr. Pausic's departure, there were several factors also taken into consideration. Cambridge was also informed that the general partner of Maverick (the management company, not the fund itself), would be making an investment in Pausic's new fund. This decision is particularly notable given that Maverick, which was founded in 1995, had never previously seeded a departing employee. Being this is a strong endorsement for Pausic, it is also indicative of his contributions to the investment process and value to the organization, and by extension the impact of his departure.

Other minor changes at Maverick have also occurred – specifically, two (2) members of the investment team, Stephen Schrieder and Steve Galbraith, resigned from their roles in Q4 of last year and the team also began instituting a new position sizing framework known internally as MavRank in early 2012. Mr. Lohmeyer's concern that while none of these changes have negatively impacted Maverick's investment results to date, each successive change makes it increasingly difficult to assess the degree of organizational continuity and the repeatability of the firm's prior success.

Regent Hollingsworth called for a motion to redeem the University of Houston's allocation in Maverick Capital.

On motion of Regent Armour, seconded by Regent Welder and by a unanimous vote of the committee members in attendance, the recommendation for full redemption from Maverick Capital as of September 30, 2013, which would require notice prior to July 30, 2013 was approved. This action requires committee approval only and no further board action is required.

Mr. Lohmeyer addressed the pending rebalancing items that had been approved at the January 29, 2013 Endowment Management Committee meeting, and outlined the pro forma cash flow schedule as follows.

- $2.6 million partial redemption from Anchorage as of June 30, 2013. Notice submitted to manager, funds anticipated in mid-to-late July, available for reinvestment as of August 1, 2013.
- $2.0 million partial redemption from Davidson Kempner as of June 30, 2013. Notice submitted to manager, funds anticipated in mid-to-late July, available for reinvestment as of August 1, 2013.
- $2.1 million partial redemption from Samlyn as of June 30, 2013. Notice submitted to manager, funds anticipated in mid-to-date July, available for reinvestment as of August 1, 2013.

- $3.0 million add to BlueCrest AllBlue. Target investment date August 1, 2013.
- $2.0 million add to Senator. Target investment date August 1, 2013.

Raymond Bartlett asked Mr. Lee to address the committee on William Blair. Mr. Lee stated that William Blair was one of two international developed equity managers in the University of Houston portfolio. A couple of years ago, William Blair had been on the Watch List for performance purposes but in the last few years had turned things around and has had a strong long-term track record. George Greig, founder and co-PM of the International Growth strategy, recently announced his retirement effective 2014. Jeff Urbina, who joined the firm with Mr. Greig 17 years ago, will share co-PM responsibilities with Simon Fennell in the London office, who was made partner in 2003. Mr. Lee stated there is no immediate need for concern or action but Cambridge would consider bringing ideas for a possible replacement of William Blair at the next Endowment Management Committee meeting held in August 2013.

Regent Hollingsworth asked Mr. Lee to brief the committee on the criteria Cambridge uses for inclusion on, and removal from, the Watch List. Mr. Lee stated that it varies by asset class; and distinguishes between performance-related issues and business-related issues in order to more easily prioritize the need for action.

Dr. Carlucci introduced the final item to the committee, Item J, Report on the UH System's Invested Funds and Bank Deposits – University of Houston System, EM-J17 and asked Raymond Bartlett, Treasurer, to present the item.

Mr. Bartlett gave an update which summarized all of the University of Houston System's outstanding investment funds and bank deposits. This report is presented to the committee on a quarterly basis. Cambridge has provided information and provides oversight on the endowment and non-endowed funds; and the other two components of invested funds are our bond proceeds that support our capital projects and any residual amounts that are in our debt service funds. The intent of this summary was to layout where all of the university's investment balances and deposits were; and it totals $1.3 billion as of the fiscal quarter ended February 28, 2013.

It was noted that prior to the end of February 2013, in consultation with Dr. Carlucci and Cambridge Associates, Mr. Bartlett stated we rebalanced $77 million from our money market funds into our short-term fixed income to bring it more in line with the long-term policy target of 50/50.

This item was presented for information only and required no committee action.

No Executive Session was called.

There being no further business to come before the Committee, the meeting adjourned at 3:27 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.

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<u>Others Present:</u>

Renu Khator	Steve Wallace	David Ellis
Carl Carlucci	Raymond Bartlett	Shannon Thomas
Paula Myrick Short	Hamilton Lee	Gene Lohmeyer
Dona Cornell	Phil Fiske	Eli Cipriano
Eloise Dunn Stuhr	Jeanne Wilson	Rani Ramchandani
Don Guyton	Cristina Milligan	Jeff Heflin
Jon Aldrich	Ed Jones	Marquette Hobbs
Brenda Robles	Gerry Mathisen	