

**Minutes**  
**Investment Committee**  
**December 8, 2014**

IN ATTENDANCE:

Investment Committee Members:	Carol Martin Gatton, Chair James H. Booth William C. Britton Mark P. Bryant William S. Farish, Jr. James W. Stuckert Robert D. Vance
Community Advisory Members:	James F. Hardymon Myra L. Tobin
Investment Staff & Consultants:	Susan I. Krauss Donna A. Counts Kimberly C. Lush Rob Palmeri (R.V. Kuhns & Associates)

Mr. Gatton called the meeting to order at 1:00 p.m. Ms. Lush then conducted a roll call. Mr. Gatton extended a welcome to new Investment Committee and Community Advisory members Jim Booth, Bob Vance and Myra Tobin. Mr. Gatton then made a motion to approve the minutes from the Committee meeting on September 4, 2014. Mr. Gatton's motion was moved by Mr. Stuckert, seconded by Mr. Britton, and approved by all.

Ms. Krauss provided an update on the extension of the endowment investment consultant contract. A recommendation was made that the Investment Committee authorize the Treasurer to extend the contract with R. V. Kuhns to provide consulting and performance measurement services for the University of Kentucky Endowment for the period July 1, 2015 through June 30, 2016, under the same terms and conditions as the existing contract. As background, she mentioned that the University hired R. V. Kuhns in 2008 as a result of an RFP process. The term of the initial contract was April 1, 2008 through March 31, 2012, and it provided for four one-year extensions at the option of both parties under the same terms and conditions. The recommended extension would be the last of the renewals, with an RFP for investment consulting services anticipated for late 2015. Mr. Britton made a motion to extend the contract for an additional year, Mr. Stuckert seconded the motion, and all Committee members voted in favor of the motion. Ms. Krauss noted that Rob Palmeri of R. V. Kuhns had voluntarily left the room during the discussion.

Mr. Gatton introduced Mike Richey, the University's Vice President for Development, to provide the Committee with the 2014 Philanthropy Report. Mr. Richey began by informing the Committee that gift receipts at the end of 2014 totaled \$105.6 million, marking the first time in the University's history that gift receipts had exceeded \$100 million. Comparatively, in 2008, gift receipts totaled only \$58.9 million. Mr. Richey noted that the University's President, Dr. Capilouto, played a key role in fundraising during 2014 by his involvement with corporate and individual principal gift prospects. Gift receipts include gifts, pledge payments, and realized bequests and were categorized by purpose, with \$8.9 million going into endowments, \$32.8 million being used for capital, and \$63.9 million being designated for current

operations. Total work product, which includes gifts, new pledges, and new expectancies, totaled \$145 million in 2014, compared to \$82.2 million in 2008. Next, Mr. Richey presented the number of donors and gifts. The number of donors to the University had increased from 38,368 in 2008 to 53,724 in 2014. The number of gifts had grown from 61,885 to 91,501 during the prior six year period, with many donors giving multiple gifts. Mr. Richey stated that 14.7% of the University's alumni are contributors, which is one of the largest percentages of alumni donors in the SEC. A comparison of gifts received by SEC institutions was provided. The University of Kentucky was ranked fifth with total gifts received of \$105.6 million, trailing University of Florida, Vanderbilt University, University of Missouri, and University of Tennessee, respectively. Of those universities, Mr. Richey noted that Florida, Missouri and Tennessee recently completed capital campaigns. Also, he mentioned that the University of Florida, with \$215.2 million in gifts received, has a development budget and staff six times greater than that of the University of Kentucky. The University of Louisville's total gifts received of \$85.1 million was also reported. Additionally, a comparison was provided for the University's public research benchmark institutions. University of Michigan topped the list with \$432.6 million in gifts received.

Next, Mr. Richey provided a comparison of SEC endowment sizes. University of Florida had the largest endowment, valued at \$1.5 billion, followed by Texas A & M University with an endowment of \$1.2 billion. University of Kentucky ranked third in endowment size at \$1.2 billion. Vanderbilt University, with an endowment of \$3.5 to \$4 billion, was excluded from the comparison. Mr. Richey stated that the University was planning for a possible second comprehensive capital campaign and had enlisted the services of Marts & Lundy, a campaign consultant, to review the University's readiness for a campaign and to provide recommendations. A feasibility study is currently being conducted to determine a possible goal. Approximately 15,000 donors will be surveyed to provide their input and suggestions. Campaign considerations other than the goal include budgeting, staffing, and funding. In relation to budgeting, Mr. Richey noted that the average management fee in the SEC is 1.10%. The list of campaign priorities includes scholarships, an honors college, undergraduate research, chairs/professorships, endowment growth, fellowships, capital projects, research, college/program initiatives, and student engagement. In closing, Mr. Richey shared a reconciliation of the total new commitments to the University's financial statements.

Ms. Krauss then presented a review of the Endowment Asset Allocation and Transition Plan dated October 31, 2014, noting that Phase I, which has been completed, involved implementation of the liquid strategies and Phase II involves implementation of the illiquid strategies. Phase I activity recently completed includes the transition to the new direct hedge fund program with Grosvenor. The transition occurred over two months, on October 1, 2014 and on November 1, 2014. She noted that Grosvenor was an existing manager of a co-mingled product and the transition on October 1, 2014 was the initial investment into a direct long/short equity portfolio of seven individual hedge funds. She added that the goals for the total portfolio are to achieve an average target return of 7.5%, volatility or standard deviation of less than 12.5% each year, and a target beta to the S&P 500 of 0.6 or less. On November 1, 2014, \$18 million was transitioned out of the See Blue Fund, Grosvenor's absolute return strategy, into the new See Blue B Fund, which is the new long/short equity portfolio. An additional \$3 million in cash was added to fund the portfolio at \$60 million. Additionally, Ms. Krauss mentioned that \$9.5 million was added to the endowment pool at the end of August 2014 as an addition to the OPEB (Other Post-employment Benefits) quasi-endowment, with \$5 million being invested in the global tactical asset allocation strategy and \$4.5 million to the All Country World ex US index fund. She added that Grosvenor will be attending the February 19, 2015 Committee meeting and will provide updates on their funds. To summarize, Ms. Krauss noted that at the end of October 2014, the endowment pool had a value of \$1,196,000, comprised of 32% equities, 9% fixed income, and 59% in various alternatives.

Next, Ms. Krauss reviewed the Report on Manager Appointments, Terminations and Due Diligence for the period of September 5, 2014 through December 8, 2014. Three commitments were made during that time period. A commitment of \$100,000,000 was made to Neuberger Berman on October 13, 2014. SC

Capital Partners received a commitment of \$10,000,000 as of November 4, 2014, and a commitment of \$20,000,000 was made to Northwood Investors on November 13, 2014. There were no manager terminations. Regarding due diligence, investment staff conducted on-site visits with prospective long/short equity managers on September 10–11, 2014, attended the Chrysalis annual meeting on September 17, 2014, conducted an organizational and performance review meeting with Contrarian Capital on September 23, 2014, and conducted an organizational and performance review meeting with PIMCO on November 10, 2014. Ms. Krauss concluded by announcing that Todd Shupp has been hired as the University's first Chief Investment Officer and will begin his employment with the University on January 5, 2015.

The next item on the agenda was the Performance Review and Market Update from R.V. Kuhns. Mr. Palmeri began the review by presenting a total fund attribution analysis for the quarter ending September 30, 2014, which he noted was a challenging quarter. Total manager value added was -0.99% for the quarter, with diversified inflation strategies accounting for -0.55% of the underperformance. He then reviewed the asset allocation and performance summary for the quarter, stating that the quarter-to-date total performance of -1.61% was due in large part to the underperformance of both the diversified inflation strategy and global tactical asset allocation composites. Regarding domestic equity, he noted that the US equity market benefited from the flight to quality from the international equity markets. The University's domestic equity composite was 0.02%, outperforming the index by 0.08%. Fixed income was a challenging space with a return of -0.07%, underperforming the index by -0.24%. The diversified inflation strategies composite had a return of -4.71%, an underperformance of -5.80%, with both Wellington products that comprise the composite underperforming due to the poor performance of the energy and commodity sectors in addition to recognizing the long-term benchmark that does not reflect the market volatility of the funds' underlying investments. Global tactical asset allocation returned -3.18%, with a -4.27% underperformance. It was noted that exposure to international equities and emerging market debt negatively impacted these managers. Long/short equity returned -1.60%, underperforming by -0.60%. The absolute return strategy was up 0.26%, bettering the index by 0.11%. Ms. Counts then provided a review of the Operating Fund Cash and Investment Report for October 31, 2014. Total operating fund cash and investments equaled \$995.8 million at the end of the period, of which \$190.2 million was earmarked as bond proceeds. Total cash and investments subject to the operating fund investment policy were \$450.6 million, of which \$249.7 million was invested in overnight and short term investments yielding an annualized monthly return of 0.06%. The remaining \$200.9 million held in other investments produced an annualized monthly return of 2.77% and a fiscal year to date return of 1.02%.

Next, Ms. Krauss introduced Caleb Pitters and Chase Haymond, account managers from PIMCO. Mr. Pitters began by addressing recent changes in PIMCO's portfolio management leadership. He noted that in the wake of Bill Gross's departure from PIMCO on September 26, 2014, daily net outflows of funds saw a brief spike, but those slowed sharply in October and November 2014. He stated that retention of talent is a key objective for PIMCO and that no one else has left the organization since the exit of Bill Gross. A transition plan that was in place prior to Mr. Gross leaving was quickly implemented. Dan Ivascyn, a Deputy CIO at PIMCO, was promoted to the position of Group CIO. Mr. Ivascyn was considered a good choice and obvious candidate for both external and internal reasons. He had a strong historical performance in traditional fixed income markets and alternatives. Also, he had a long track record of working in and encouraging team structures, as well as a reputation for being both tough and fair. The five other Deputy CIO's, Andrew Balls, Mark Kiesel, Virginie Maisonneuve, Scott Mather, and Mihir Worah, were all promoted to CIO positions and Marc Seidner joined PIMCO in a CIO position. Mr. Pitters added that the Global Investment Committee remains unchanged with three Regional Committees comprised of senior portfolio managers in regions where they are located, 14 sector specialty desks, in excess of 250 portfolio managers, and 61 credit research analysts located in the US, Europe, Asia, and Latin America. Next, Mr. Haymond provided a market review and portfolio review. In relation to the market, he noted strong performance for core fixed income, non-core fixed income, global fixed

income and currency, as well as for global and US equities. The only sector with negative returns was commodities. As part of the Total Return performance review, he stated that the University's portfolio employs a core-plus fixed income strategy and is benchmarked to the Barclay's US Aggregate Bond Index. At October 31, 2014, the University's Total Return portfolio had a market value of \$22.2 million. As of November 30, 2014, the year to date return, net of fees, was 5.5%, a slight underperformance compared to the benchmark of 5.9%. However, over the longer period of time, the portfolio had outperformed the benchmark. Returns for the prior three year period were 4.2% compared to a benchmark of 3.0%. Since inception on Sept 30, 2002, the portfolio had returned 5.7%, outperforming the benchmark by 100 basis points. He stated that positioning on the yield curve had driven performance, with the focus being on the front end of the yield curve. Regarding the Unconstrained Bond Fund performance review, the University's market value was \$33.7 million at October 31, 2014. The year to date return after fees at November 30, 2014 was 3.4%. The final performance review was related to PIMCO's All Asset All Authority fund. The University's market value in this fund was \$46.2 million at October 31, 2014. The return was 1.4% at November 30, 2014, compared to the CPI+ 6.5% benchmark of 6.7%. Mr. Haymond noted that the underperformance was driven by a shortage of US equities.

The meeting was adjourned at 2:50 p.m.

Respectfully submitted,  
Kimberly C. Lush  
Office of the Treasurer