

Board Meeting
December 2, 2011

ROLL CALL

AUTHORIZE INVESTMENT MANAGERS

Action: Approve Hiring of Firms to Provide Investment Management Services for Endowment and Operating Funds

Funding: Investment Income

In January 2011, the Board of Trustees approved amendments to the investment policy for the endowment and operating funds. These revisions require the hiring of additional fixed income managers to meet the University's investment mandates.

Endowment Funds

Endowment funds are received from a donor with the restriction that the principal is not expendable. As established by the Board of Trustees in previous actions, the primary objectives for management of the University of Illinois Endowment are to preserve the real value, or purchasing power, of the endowment assets and to maximize the sustainable spending stream provided by these assets.

University treasury staff and the University's investment consultant, Hewitt EnnisKnupp, conducted a comprehensive asset allocation review of the University's endowment investment program during fall 2010. The revised endowment asset

allocation, approved by the Board of Trustees in January 2011, utilized new asset classes and made changes to existing asset class strategies. A conservative core fixed income investment mandate, requiring a new manager, was added to the existing endowment pool fixed income allocation.

Operating Funds

Operating funds are expended to support the University's teaching, research, and public service missions. Operating funds include tuition revenues, State dollars, grant funds, self-insurance reserves, hospital and physician revenues, as well as plant and auxiliary funds. Operating funds are pooled and invested to preserve the value and safety of the principal.

Previously approved Board policies structured operating fund investments into liquidity layers designed to meet forecasted University expenditures. Funds expected to be used within one year are invested in money market instruments to provide primary liquidity. Core operating funds are invested in longer maturity instruments in order to earn a higher return. The operating pool asset allocation, approved by the Board of Trustees in January 2011, expanded the allowable ranges within the different liquidity layers. These revisions were instituted in order to enhance potential returns and improve flexibility to cope with lagging State of Illinois receipts. The expanded liquidity layers present an opportunity to increase the number of fixed income investment managers. Additional managers will provide for diversification of investment strategies, including enhanced cash and short duration assignments, to employ within the liquidity layers.

Manager Selection Process and Recommendation

A request for proposal to qualify investment firms for the operating and endowment pool fixed income mandates was listed on the Illinois Procurement Bulletin website. The University received proposals from 28 firms for the enhanced cash, short duration, and core fixed income mandates. The proposals were carefully evaluated and scored based on stringent review criteria. Eleven of the firms were selected as semi-finalists and interviewed by telephone; three of these were eliminated. In-person interviews were conducted with eight finalist managers by University staff and Hewitt EnnisKnupp; three of these were eliminated. The following five investment managers were deemed the most suitable firms to meet the University's fixed income mandates: Galliard Capital Management, Income Research and Management, JP Morgan Asset Management, Neuberger Berman, and Wells Capital.¹ These managers were selected due to their organizational strength, investment process, risk management, and past performance record. The Vice President/Chief Financial Officer and Comptroller recommends the hiring of these five managers. The footnote shows estimated pricing for each manager to manage \$100.0 million for one year.

The Board action recommended in this item complies in all material respects with applicable State and federal laws, University of Illinois *Statutes, The*

¹The annual fees, in basis points (bp), are as follows: Galliard--25 bp, Income Research and Management--29 bp, JP Morgan--30 bp, Neuberger Berman--18 bp, and Wells Capital--9 bp. A 25 basis points fee is equivalent to 0.25 percent, or \$250,000 on a \$100.0 million portfolio.

General Rules Concerning University Organization and Procedure, and Board of Trustees policies and directives.

The President of the University concurs.