Reported to the Board of Trustees March 12, 2020







# UNIVERSITY OF ILLINOIS SYSTEM

FOURTH QUARTER 2019 INVESTMENT UPDATE PREPARED FOR THE BOARD OF TRUSTEES

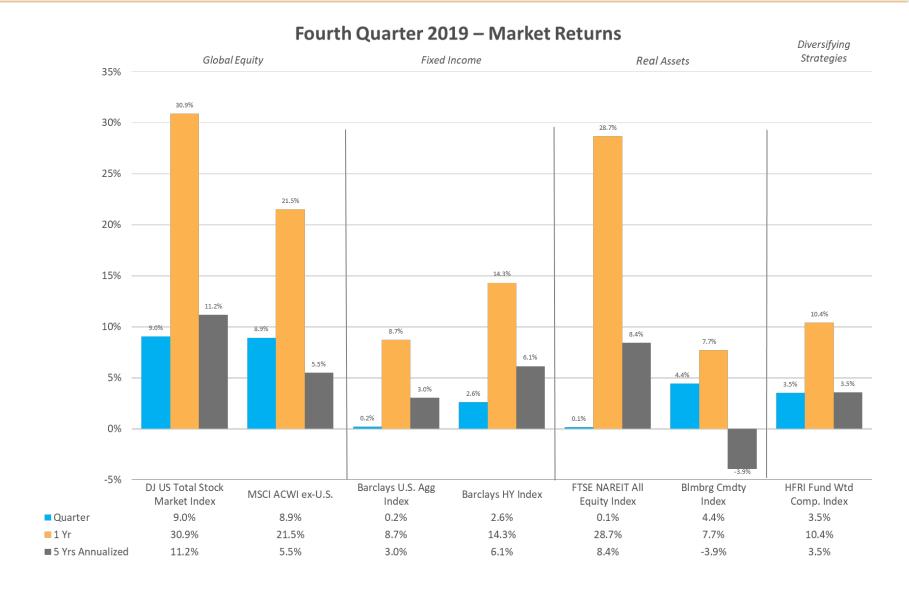
February 2020

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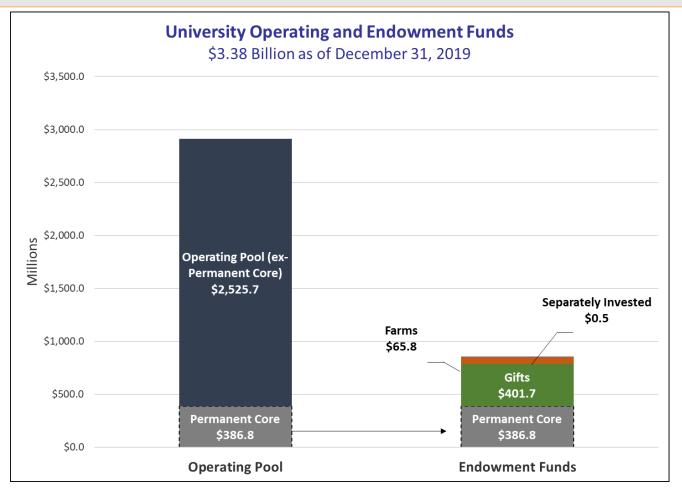
# MARKET OVERVIEW AND SYSTEM ASSETS

### CAPITAL MARKET OVERVIEW



Data sources: Lipper and Hedge Fund Research

# UNIVERSITY OPERATING AND ENDOWMENT FUNDS: DEC 31, 2019

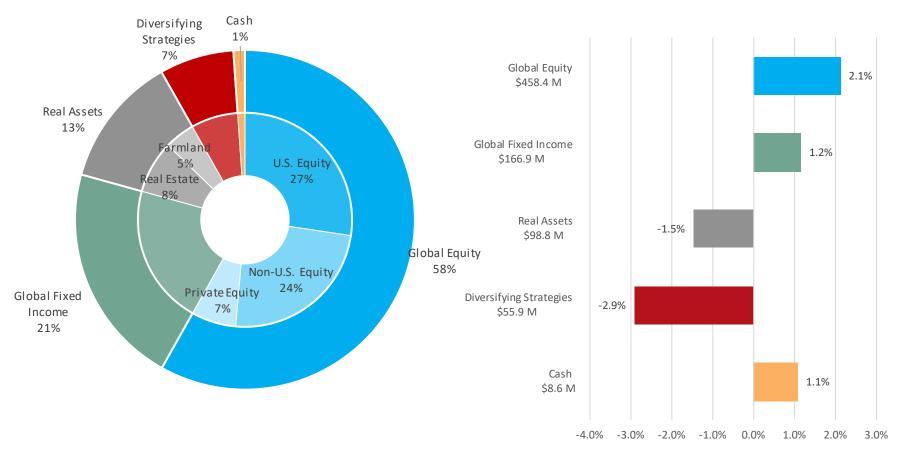


- The University Operating and Endowment Funds were valued at \$3.4 billion as of December 31, 2019.
- The Operating Pool (ex-Permanent Core) was valued at \$2.5 billion. The permanent core investment (gray bar) is a long-term investment of the operating cash in the Endowment Pool to enhance distributions to invested units.
- The combined Endowment Funds is valued at \$854.8 million (right bar) and is discussed further on the following slides.
- The Pure Endowment (excluding Operating) is valued at \$468.0 million.

# ENDOWMENT FUND UPDATE: DECEMBER 31, 2019

## Total Pool: \$788.5 Million as of 12/31/2019

# Over/Under Allocation to Long-Term Policy Targets



Note: Long-Term Policy Allocations: Global Equity 56%, Global Fixed Income 20%, Real Assets 14%, and Diversifying Strategies 10% Total sum of allocation may not equal 100% due to rounding.

# TOTAL ENDOWMENT POOL PERFORMANCE (DECEMBER 31, 2019)

#### TOTAL POOL: \$788.5 MILLION



- Over the one-year period, the endowment returned 17.3%. Cash (+2.0%) and real estate (+7.1%) hurt performance, while U.S. equity (+30.4%) did well.
- On the ten-year period, the endowment posted a strong 8.9% return, supported by solid returns from U.S. equities (+12.9%), real assets (+11.3%), and private equity (+11.3%).

<b>Endowment Pool</b>	Quarter Ending				
Market Value Change	December-2019				
Beginning Market Value	\$746.0 M				
Net Contributions	\$6.9 M				
Gain/Loss	\$35.6 M				
Ending Market Value	\$788.5 M				

Note: The beginning market value + net contributions + net investment gains referenced in the table may not equal the ending market value due to rounding.

# ASSET CLASS PERFORMANCE: ENDOWMENT POOL (DEC 31, 2019)

	Current	Policy	Quarter ending					Since	
	Allocation (%)	Allocation (%)	Dec-2019	1 Year	3 Years	5 Years	10 Years	Inception	Inception Date
Endowment Pool			4.8	17.3	8.8	6.5	8.9	8.2	Sep-87
Performance Benchmark			4.9	17.9	8.9	6.7	8.9	8.4	
GLOBAL EQUITY	58.1	56.0	8.0	24.4	12.2	8.6	10.2	8.1	Sep-87
Total U.S. Equity			9.1	30.4	13.3	10.0	12.9	9.5	Sep-87
DJ U.S. Total Stock Market Index			9.0	30.9	14.5	11.2	13.4	9.8	
Total Non-U.S. Equity			9.2	21.7	9.9	5.7	4.9	5.5	Sep-93
Non-U.S. Equity Benchmark			9.2	21.6	9.8	5.7	5.1	5.6	
Total Private Equity			0.0	12.7	15.6	13.2	11.3	4.4	Jan-04
Private Equity Benchmark			0.0	22.1	14.0	12.1	15.4	11.6	
GLOBAL FIXED INCOME <sup>1</sup>	21.2	20.0	0.0	8.6	4.3	3.4	5.1	6.8	Sep-87
Total Public Fixed Income			0.0	8.3	4.1	3.3	5.0	6.8	Sep-87
Bloomberg Barclays U.S. Aggregate			0.2	8.7	4.0	3.0	3.7	6.4	
REAL ASSETS	12.5	14.0	0.1	8.0	4.6	4.1	11.3	10.1	Dec-06
Total Real Estate			0.2	7.1	6.1	7.5	-	10.2	Aug-13
Real Estate Benchmark			1.3	4.4	5.7	7.2	-	10.1	
Total Farmland <sup>2</sup>			0.0	9.3	2.8	0.4	8.7	8.1	Dec-06
NCREIF Cornbelt Index			0.0	2.3	1.5	0.2	8.0	8.8	
DIVERSIFYING STRATEGIES <sup>1</sup>	7.1	10.0	1.8	8.2	1.4	2.3		2.8	May-13
Total Hedge Funds			1.9	8.0	1.0	2.1	-	2.7	May-13
HFRI Fund Weighted Composite Index			3.5	10.4	4.5	3.5	-	3.8	
CASH	1.1	0.0	0.4	2.0	1.4	-	-	0.9	

<sup>&</sup>lt;sup>1</sup>Global Fixed Income and Diversifying Strategies include allocations and performance of private investments.

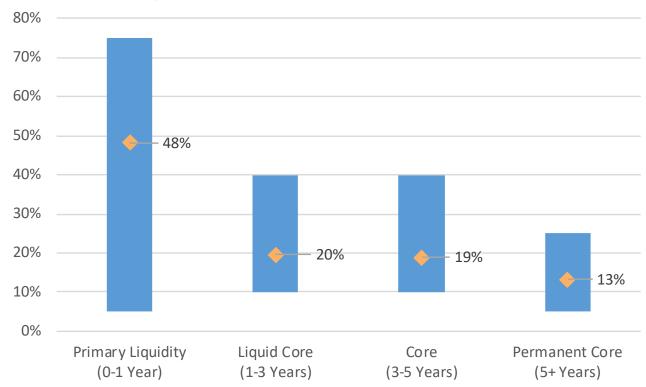
<sup>&</sup>lt;sup>2</sup>Farmland directly owned by the Endowment is valued annually on June 30.

# OPERATING POOL UPDATE: DECEMBER 31, 2019

# LIQUIDITY LAYERS: OPERATING POOL (DECEMBER 31, 2019)

#### **OPERATING POOL LIQUIDITY LAYERS**

AS OF DECEMBER 31, 2019



- The asset allocation strategy for the Operating Pool consists of investing funds across four liquidity layers. Board-approved ranges are depicted by the bars, while the diamonds represent the actual allocation.
- Funds expected to be used within one year are invested in the primary liquidity layer.
- Longer-time horizon investments, including core and permanent core, are expected to provide higher rates of return and will experience some variation in market value as capital market conditions change.
- The System's permanent core operating funds are invested in the System's Endowment Pool investment program.

Total sum of allocation may not equal 100% due to rounding.

# TOTAL OPERATING POOL PERFORMANCE (DECEMBER 31, 2019)

#### **TOTAL POOL: \$2.53 BILLION**



- Over the trailing one-year period ending December 31, 2019, the Operating Pool returned 4.0%, slightly ahead of the benchmark return.
  - All the managers in the Operating Pool outperformed their respective benchmark over the period.
- Over longer time periods, the Operating Pool has exceeded the benchmark on a consistent basis.
  - The Operating Pool's managers have each met or outperformed their respective benchmarks since inception.

	Quarter Ending			
Market Value Change	December-2019			
Beginning Market Value	\$2,668.3 M			
Net Contributions	(\$156.3 M)			
Gain/Loss	\$13.7 M			
Ending Market Value	\$2,525.7 M			

Note: The Total Pool's beginning and ending market values include bank balances in which the System earns credit to offset bank fees. The beginning market value + net contributions + net investment gains referenced in the table may not equal the ending market value due to rounding.



# MARKET ENVIRONMENT

### 2010-2019 Annual Returns of Key Indices

2010	2011	2012	2013	2014	2015	2016 2017 2018 2019		5-year annual	10-year annual		
MLPs 35.9%	MLPs 13.9%	Global REIT 27.7%	Small Cap 38.8%	Global REIT 15.0%	Large Cap 1.4%	Small Cap 21.3%	Emerging Markets 37.3%	Bonds 0.0%	Large Cap 31.5%	Large Cap 11.7%	Large Cap 13.5%
Small Cap 26.9%	Bonds 7.8%	Emerging Markets 18.2%	Large Cap 32.4%	Large Cap 13.7%	Bonds 0.5%	MLPs 18.3%	Int'l 25.0%	High Yield -2.1%	Small Cap 25.5%	Small Cap 8.2%	Small Cap 11.8%
Global REIT 19.6%	High Yield 5.0%	Int'l 17.3%	MLPs 27.6%	Bonds 6.0%	Hedge Funds -0.3%	High Yield 17.1%	Large Cap 21.8%	Hedge Funds -4.0%	Global REIT 21.9%	Global REIT 5.6%	Global REIT 8.4%
Emerging Markets 18.9%	Large Cap 2.1%	Small Cap 16.3%	Int'l 22.8%	Small Cap 4.9%	Global REIT -0.8%	Large Cap 11.9%	Small Cap 14.6%	Large Cap -4.4%	Int'l 22.0%	High Yield 6.1%	High Yield 7.6%
High Yield 15.1%	Small Cap -4.2%	Large Cap 16.0%	Hedge Funds 9.0%	MLPs 4.8%	Int'l -0.8%	Emerging Markets 11.2%	Global REIT 10.4%	Global REIT -5.6%	High Yield 14.3%	Int'l 5.7%	Int'l 5.5%
Large Cap 15.1%	Hedge Funds -5.7%	High Yield 15.8%	High Yield 7.4%	Hedge Funds 3.4%	Small Cap -4.4%	Global REIT 4.1%	Hedge Funds 7.8%	Small Cap -11.0%	Emerging Markets 18.4%	Emerging Markets 5.6%	MLPs 4.2%
Int'l 7.7%	Global REIT -6.5%	MLPs 4.8%	Global REIT 3.7%	High Yield 2.5%	High Yield -4.5%	Bonds 2.6%	High Yield 7.5%	MLPs -12.4%	Bonds 8.7%	Bonds 3.0%	Bonds 3.7%
Bonds 6.5%	Int'l -12.1%	Hedge Funds 4.8%	Bonds -2.0%	Emerging Markets -2.2%	Emerging Markets -14.9%	Int'l 1.0%	Bonds 3.5%	Int'l -13.8%	Hedge Funds 8.3%	Hedge Funds 2.4%	Emerging Markets 3.7%
Hedge Funds 5.7%	Emerging Markets -18.4%	Bonds 4.2%	Emerging Markets -2.6%	Int'l -4.9%	MLPs -32.6%	Hedge Funds 0.5%	MLPs -6.5%	Emerging Markets -14.6%	MLPs 6.6%	MLPs -7.0%	Hedge Funds 2.8%

Note: See disclosure section for a description of key indices.

## **GLOBAL EQUITY**

- Global equity performance was notably strong in 2019, marking a reversal from weakness in 2018. Domestic outpaced International, particularly Emerging Markets, throughout much of the year, a multi-year trend that reversed in 4Q thanks to a "Phase 1" trade deal between the U.S. and China, alongside a 3% decline in the USD.
- Heightened trade tensions between the U.S. and China served as a headwind to global industrial production, leading to relative underperformance among trade-sensitive regions, such as Emerging Markets.
- From a capitalization standpoint, Domestic Large Cap (+31.5%) outperformed Small Cap (+25.5%), though the trend reversed in 4Q. Stylistically, Growth outperformed Value, with sharply declining rates and flattening global term structures serving as relative headwinds to Value performance. Beginning October 11<sup>th</sup>, the Fed started purchasing T-Bills, which bolstered late-year equity performance.

#### **Global Equity Year-to-Date Performance** (in USD)

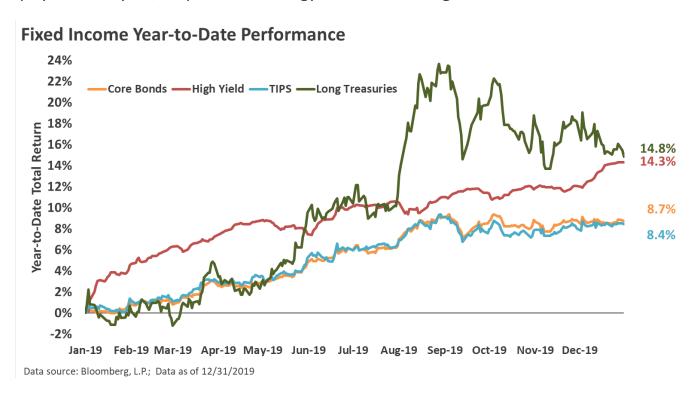


Jan-19 Feb-19 Mar-19 Apr-19 May-19 Jun-19 Jul-19 Aug-19 Sep-19 Oct-19 Nov-19 Dec-19

Data source: Bloomberg, L.P.; Data as of 12/31/2019

#### FIXED INCOME

- Global interest rates spent much of 2019 moving lower, with a new record low in the inflation-sensitive 30-Year
  Treasury Bond breached in August. A late-year risk-on rally pressured the performance of rate-sensitive sectors,
  supporting relative returns among the credit-oriented areas of the market and driving credit risk premiums lower.
- The term premium between the 10-Year Treasury Note and 3-Month Treasury Bill plunged into negative territory in March, the first occurrence since 2007 and reflective of both overly-tight monetary conditions and recessionary concerns. Three consecutive Fed interest rate cuts since July amid a "mid-cycle adjustment" helped reverse yield curve flattening forces, with most term slopes witnessing a calendar year *increase* in yield spread.
- Despite the sharp move lower in rates, credit risk premiums tightened, with spreads in U.S. High Yield declining by nearly 200 bps year-over-year, despite some energy-related widening that occurred in the second half of 2019.



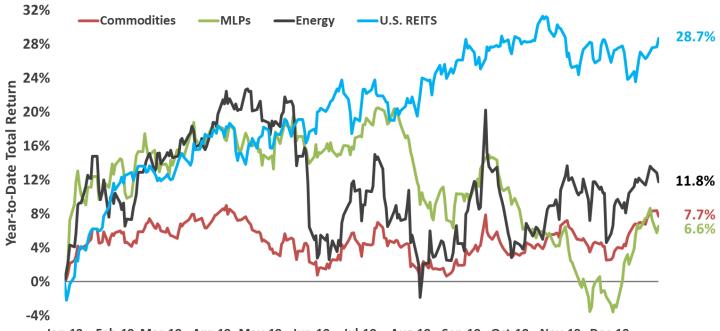
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#### **REAL ASSETS**

- Benefiting from the risk-on sentiment experienced by both equities and bonds, Real Assets spent the majority of 2019 in positive territory. Rate-sensitive sectors, such as Domestic REITs (+28.7%), had a particularly strong year.
- Commodities spent the duration of the year in positive territory, with solid, albeit volatile, returns witnessed by Energy and Precious Metals spot prices, despite global industrial weakness and growth headwinds.

#### **Real Assets Year-to-Date Performance**

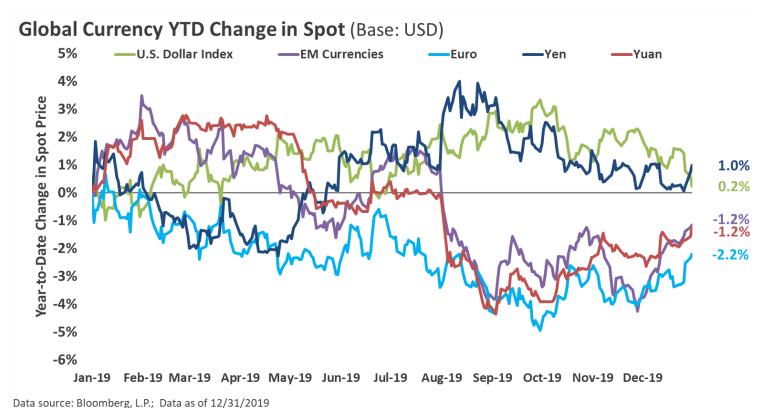


Jan-19 Feb-19 Mar-19 Apr-19 May-19 Jun-19 Jul-19 Aug-19 Sep-19 Oct-19 Nov-19 Dec-19

Data source: Bloomberg, L.P.; Data as of 12/31/2019

#### **CURRENCIES**

- The USD, as proxied by the ICE U.S. Dollar Index, ended 2019 essentially flat (+0.2%), pressured downward following the Fed's October 11<sup>th</sup> announcement of T-Bill purchases and late-year trade progress between the U.S. and China. The DXY declined by 3% in the fourth quarter, the weakest quarterly performance since 2Q 2017.
- Liquid Emerging Market currencies, proxied by the JPMorgan Emerging Market Currency Index, sunk to the lowest level on record versus the USD in August as U.S. Chinese trade tensions deepened, which helped place meaningful downward pressure on the Chinese yuan.



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**Large Cap** is represented by the S&P 500 Index which measures the performance of large capitalization U.S. stocks. The S&P 500 is a market-weighted index of 500 stocks that are traded on the NYSE, AMEX, and NASDAQ. www.standardandpoors.com

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