# MINUTES

# BOARD OF REGENTS COMMITTEE ON BUDGET AND FINANCE MEETING

# FEBRUARY 14, 2019

## I. CALL TO ORDER

Committee Chair Moore called the meeting to order at 11:26 a.m. on Thursday, February 14, 2019, at the University of Hawaiʻi at Mānoa, Information Technology Building, 1st Floor Conference Room 105A/B, 2520 Correa Road, Honolulu, Hawaiʻi 96822.

Committee members in attendance: Committee Chair Randy Moore; Committee Vice Chair Wayne Higaki; Regent Simeon Acoba; Regent Michael McEnerney; Regent Michelle Tagorda.

Others in attendance: Board Chair Lee Putnam; Regent Kelli Acopan; Regent Eugene Bal III; Regent Ben Kudo; Regent Alapaki Nahale-a; Regent Robert Westerman; Regent Ernest Wilson Jr.; Regent Stanford Yuen (ex officio committee members); President/UH Mānoa (UHM) Chancellor David Lassner; Vice President for Community Colleges John Morton; Vice President for Legal Affairs/University General Counsel Carrie Okinaga; Vice President for Academic Planning and Policy Donald Straney; Vice President for Research and Innovation Vassilis Syrmos; Vice President for Information Technology/Chief Information Officer Garret Yoshimi; Vice President for Budget and Finance/Chief Financial Officer Kalbert Young; Interim UH Hilo (UHH) Chancellor Marcia Sakai; UH West Oʻahu (UHWO) Chancellor Maenette Benham; Executive Administrator and Secretary of the Board of Regents (Board Secretary) Kendra Oishi; and others as noted.

## II. APPROVAL OF MINUTES OF THE NOVEMBER 1, 2018 MEETING

Committee Vice Chair Higaki moved to approve the minutes of the November 1, 2018, meeting, seconded by Regent McEnerney, and the motion carried unanimously.

## III. PUBLIC COMMENT PERIOD

Board Secretary Oishi announced that the Board Office received written testimony related to the recent tuition proposal from Jim Shon of Hawaiʻi Educational Policy Center who also provided oral testimony.

## IV. AGENDA ITEMS

### A. Recommend and Recommend Board Approval

#### 1. Amendments to the Bylaws of the Board of Regents Article II.D.2.b., Committee on Budget and Finance, and Article II.D.2.c., Committee on Planning and Facilities

The committee considered a proposal to amend the bylaws to move the capital improvement budget oversight responsibility from the Budget and Finance Committee to the Planning and Facilities Committee, which reflects current practice, and to clarify the

Budget and Finance Committee's functions to emphasize the Board's responsibility to exercise fiduciary oversight of endowment funds and other financial assets of the university, in response to a previous discussion by the committee on this subject.

Committee Vice Chair Higaki moved to recommend board approval of the amendments to the Bylaws of the Board of Regents Article II.D.2.b., Committee on Budget and Finance, and Article II.D.2.c., Committee on Planning and Facilities, seconded by Regent Acoba, and the motion carried unanimously.

## B. For Information and Discussion

### 1. Fiscal Year (FY) 2019 First and Second Quarter UBS Legacy Endowment Fund Investment Performance Report

VP Young reminded the committee that there was a migration in investment strategy between the first and second quarters of FY19, and introduced Mr. Kyle Yoneshige and Ms. Lori Hamano from UBS to provide the report on investment performance. He noted that the strategy and platform for the portfolio was being migrated from mutual and exchange traded funds to separately managed accounts between the first and second quarter.

For the benefit of new regents, Committee Chair Moore noted that before the University of Hawai‘i Foundation (UHF) was established, money given for an endowment to the university was maintained by the university. Approximately $70 million makes up this endowment, nothing is added to the fund, and the president has the discretion to withdraw up to 5% per year from the rolling average of the endowment for use according to the purpose specified by donors. The regents are responsible for engaging experts to manage the endowment under guidelines set forth by regents in board policy. Approximately 3.5 years ago, the board decided to divest the endowment from fossil fuel-producing companies because they were not thought to be prudent investments and as part of the university's commitment to sustainability. UBS was given 3 years to reduce the investment in fossil fuel producers to less than 1%.

UBS explained that the optimal asset allocation for the endowment is 1% in cash, 39% in U.S. fixed income, 34% in U.S. equities, and 26% in international equities, which is in compliance with the investment policy statement. The equity percentage for the overall portfolio remains at 60%, but international equity exposure increased significantly from 12% to 26%. The total cost for the new portfolio structure is 0.48%, the same as the previous portfolio, which includes the 0.2% UBS advisory fee, and 0.28% investment manager fees. The portfolio is also in compliance with the fossil fuel mandate of less than 1% exposure.

The committee engaged in discussion regarding benchmarks that would best help regents evaluate investment performance. UBS recommended utilizing Consolidated Benchmark 1 going forward because it is an exact asset allocation replica of the current legacy endowment fund, whereas consolidated Benchmarks 2 and 3 are the old benchmarks.

UBS indicated that the endowment value decreased 8.43% in the second quarter, slightly worse than the 7.6% decrease in the benchmark. UBS noted that there is a lot of volatility in the market, but as of the date of the committee meeting, the portfolio has rebounded and losses since December 31 had been recouped. UBS will recommend asset allocation and manager adjustments as needed according to market conditions.

Questions were raised regarding whether the four fund managers were equally weighted, and fund manager performance compared to the S&P. UBS responded that the fund managers are weighted according to the portfolio structure. The U.S. equities portfolio is indexed to the Russell 3000, which is broader than the S&P 500, and the portfolio performance was slightly below due in part to fossil fuel mandate. The portfolio changes were implemented at the end of October, so it has been less than a full quarter.

Questions were raised regarding how UBS intends to address the uncertainty surrounding globalization and international investments potentially not being as profitable as they previously were because of Brexit, trade deals, and trade tensions with China. UBS explained that they are closely monitoring what is happening globally. Most of the portfolio's international investments are focused on large, global, multinational corporations and UBS is forecasting stocks outside the U.S. to have slightly higher expected returns over the long term.

A question was raised regarding whether UBS anticipates investing in mutual funds or exchange-traded funds tailored toward energy sector holdings without being in fossil fuels that might have a lower cost ratio than the individually managed funds. UBS explained that there is a burgeoning market for these types of funds, but the trade volume is not high enough that liquidity will become an issue given the size of the university's portfolio. UBS will continue to monitor as the industry progresses, but at the current time, the current portfolio structure is the most cost-effective and efficient.

A question was raised regarding evaluating decisions when using a dynamic benchmark that changes whenever the asset allocation changes. UBS explained that they want to ensure individual asset classes are performing well and the asset allocations is adding value. UBS is recommending utilizing Consolidated Benchmark 1 and leaving it the same for any asset allocation changes made going forward. Consolidated Benchmark 2 is a standard 60% global equities/40% fixed income benchmark used for the old portfolio structure, and could also be left in place so there is another frame of reference for performance evaluation.

**2. <u>Fiscal Year 2019 Second Quarter Financial Report</u>**

VP Young provided an overview of the financial report and results for the second quarter of FY19. He noted that the second quarter financial report closely mirrored the first quarter report. Overall revenues were $6.6 million, or 0.7%, higher than projections, and expenditures were $30.5 million, or 5.5%, lower than projections. The lower-than-projected expenditures were mostly attributed to the timing of transfers or expenditures.

VP Young noted that enrollment growth doesn't necessarily translate to a growth in revenue. Although there was growth in general fund revenue, most of it was attributed to collective bargaining increases. Campuses continued to exercise diligence in expenditures, which contributed to better than expected performance.

The committee considered whether to move from quarterly to semi-annual financial reports. Most members of the committee preferred quarterly reports to ensure that the Board remains apprised of the university's financial condition. VP Young noted that they were able to accommodate a previous regent request to breakdown community college financials by campus, which is reflected in the appendix to the report.

## V. ADJOURNMENT

There being no further business, Committee Vice Chair Higaki moved to adjourn, Regent Tagorda seconded, and with unanimous approval, the meeting was adjourned at 12:50 p.m.

Respectfully Submitted,

/S/

Kendra Oishi
Executive Administrator and Secretary
of the Board of Regents