

MINUTES

BOARD OF REGENTS COMMITTEE ON BUDGET AND FINANCE MEETING

JUNE 2, 2022

I. CALL TO ORDER

Vice-Chair Wayne Higaki called the meeting to order at 10:36 a.m. on Thursday, June 2, 2022, with regents participating from various locations.

Committee members in attendance: Chair Robert Westerman; Vice-Chair Wayne Higaki; Regent Benjamin Kudo; Regent Alapaki Nahale-a; and Regent Diane Paloma.

Others in attendance: Board Chair Randy Moore; Regent Simeon Acoba; Regent Kelli Acopan; Regent Eugene Bal; Regent William Haning; Regent Ernest Wilson (ex officio committee members); President David Lassner; Vice President (VP) for Legal Affairs/University General Counsel Carrie Okinaga; VP for Research and Innovation Vassilis Syrmos; VP for Information Technology/Chief Information Officer Garret Yoshimi; VP for Budget and Finance/Chief Financial Officer Kalbert Young; VP for Advancement/UH Foundation Chief Executive Officer Tim Dolan; UH Mānoa (UHM) Provost Michael Bruno; UH Hilo Chancellor Bonnie Irwin; UH West O’ahu Chancellor Maenette Benham; Executive Administrator and Secretary of the Board of Regents (Board Secretary) Kendra Oishi; and others as noted.

II. APPROVAL OF MINUTES

Vice-Chair Higaki inquired if there were any corrections to the minutes of the March 3, 2022, committee meeting which had been distributed. Hearing none, the minutes were approved.

III. PUBLIC COMMENT PERIOD

Board Secretary Oishi announced that the Board Office did not receive any written testimony, and that no individuals signed up to provide oral testimony.

IV. AGENDA ITEMS

A. Fiscal Year (FY) 2021-2022 Third Quarter UBS Legacy Endowment Fund (Fund) Investment Performance Report

Kyle Yoneshige and Lori Hamano from UBS provided a report on the Fund for the third quarter of FY 2021-2022, reviewing both asset allocation and investment performance. Ms. Hamano stated that the asset allocation of the Fund consisted of 6.06 percent cash, 23.21 percent fixed-income, and 70.73 percent equities; provided a detailed breakdown of each asset class; and noted that asset performance continues to be negatively impacted by high inflation and increasing interest rates. She also spoke about a decision made at the end of the 2021 calendar year to raise \$3 million in cash explaining that this was a strategic maneuver given UBS’s heightened concerns about

market volatility and the impact this would have on cash and equity assets of the Fund. Of the total amount raised, \$1 million was deployed in United States equities at the beginning of May 2022 with \$2 million in tactical cash remaining for reinvestment in equities when the investment markets become more favorable or for application toward the university's need for liquid assets.

Mr. Yoneshige provided an overview of the Fund's portfolio performance stating that as of March 31, 2022, the value of the Fund stood at just over \$92.1 million. He noted that the Fund experienced an overall decrease in performance through the first three quarters of the fiscal year that was mainly attributed to a lackluster performance by the Fund's international equity holdings and lagging fixed-income asset returns throughout the third quarter. He also stated that the Fund was continuing to experience flat performance in the fourth quarter of the fiscal year, with a contraction of slightly more than six percent in the two months since the close of the third quarter. As such, the Fund's value has declined to \$85.8 million as of May 31, 2022. Despite these downturns, the portfolio's performance remains in line with long-term expectations relative to established benchmarks. It was noted that internal compliance reviews confirmed that the Fund was in accord with fossil fuel divestiture mandates and all investment policies. Additionally, no material changes or weaknesses have been identified with respect to the management of the Fund.

Mr. Yoneshige reported that an annual study on the performance of legacy endowment funds issued by the National Association of College and University Business Officers showed that the financial performance of the Fund is in line with the performance of similarly sized endowment funds of between \$50 and \$100 million at other public institutions. He provided a synopsis of the report stating that the most recent data available for comparison purposes indicated that the Fund's average investment return of 25.81 percent is comparable to the 26.63 percent experienced by its peer group. With respect to comparisons of the average five-year rate of return, the Fund's investment performance of 11.81 percent exceeded the investment performance of all other foundations and endowments which averaged 10.46 percent.

Ms. Hamano and Mr. Yoneshige briefed the committee on the financial outlook of the Fund and the direction UBS was considering given the current economic and market situation. They also provided an overview of market performance over the past 42 years. Market volatility, due in part to decades' high inflation and the Federal Reserve's rapid increase in interest rates to combat inflationary pressures, continues to weigh on the Fund's portfolio performance and is anticipated to do so for the near-term. As previously noted, the hike in inflation and increasing interest rates have impacted all asset classes. The bond markets experienced unusual volatility which has led to the worst bond market in nearly four decades with the bond index being down by approximately 8.92 percent as of May 31, 2022. While the Fund's fixed-income portfolio was decreased to near the minimum asset allocation threshold level established by Regents Policy in anticipation of increasing interest rates, recent upticks in the yields for ten-year government bonds may provide for investment opportunities in fixed-income in the future. It was also noted that, despite economic challenges, corporate earnings remain strong. Given these factors, along with improved valuations of United States

equities and highly discounted international equities, UBS continues to believe that equities currently offer the best opportunities for long-term returns-on-investment. UBS will continue to monitor the financial markets, focusing on long-term returns that consider inflation and market volatility, and adjust its investment strategy accordingly.

Regent Kudo asked about UBS's anticipated timeline for market stabilization and questioned whether the purchase of growth stocks or value stocks will be emphasized in the future given the Fund's long-term investment focus. Mr. Yoneshige replied that it is unlikely that the markets will completely stabilize until 2023 given ongoing supply chain issues that are expected to continue to at least the end of the 2022 calendar year. He also stated that growth stocks have outperformed expectations over the last three years while the outperformance experienced by value stocks has been transitory. As such, UBS continues to advocate for long-term investment in growth stocks.

Regent Nahale-a questioned whether global interdependence and changing geopolitical climates are taken into consideration by UBS when assessing the Fund's performance. Ms. Hamano and Mr. Yoneshige responded that while global interdependency and changing geo- and socio-political climates have an impact on the markets and has led to challenging situations, fundamentals with respect to long-term investing and factors leading to short-term volatility have not changed.

Regent Acoba requested clarification on the use of the \$3 million in cash raised at the end of 2021, asked about UBS's current approach to investing to decrease loss-risk, and inquired as to how UBS manages this approach given the management of funds by individual managers. Ms. Hamano replied that \$3 million in cash was raised from the sale of equities at the end of the 2021 calendar year and that \$1 million of this amount was reinvested in United States equities in early May 2022 due to favorable conditions. A balance of \$2 million in tactical cash remains and UBS will continue to evaluate equity markets to determine if and when to deploy these funds. She also stated that, while funds are being managed by individual investment managers, UBS is responsible for determining where monies will be deployed to achieve the Fund's overall investment objectives and ensuring that its directives are carried out by the individual investment managers. Mr. Yoneshige added that UBS must balance loss-risk with long-term growth to ensure the perpetuity of the Fund when developing an investment strategy.

B. FY 2021-2022 Third Quarter Financial Report

VP Young provided the financial report for the third quarter of FY 2021-2022 stating that while the fiscal condition of the university appears generally positive, the administration will continue monitoring revenues and expenditures to better gauge the overall fiscal condition and progress of the university.

Chair Westerman arrived at 11:13 a.m.

Data on general fund (GF) and special fund revenues and expenditures was presented for each of the major units of the university. Although total revenues were approximately \$134.2 million higher than the same period last fiscal year, VP Young explained that this was attributable to a change in the GF distribution methodology used

by the State Department of Budget and Finance which led to the university already receiving its entire FY 2021-2022 GF allocation as opposed to FY 2020-2021 when funds were released on a quarterly basis. He also emphasized that GF revenues available to be distributed this fiscal year were less than what was appropriated last year. An increase in tuition and fees revenues, which were \$6.4 million higher than the same period last year, was attributed to the notable rise in enrollment at UHM which more than offset enrollment declines experienced by all other campuses. The uptick in on-campus activity also boosted revenues generated for other special and revolving funds, though it was noted that they remained below pre-pandemic levels. While overall expenditures were \$39.2 million lower than the same period last fiscal year, greater on-campus activity is also expected to result in higher expenses. As such, campuses continue to implement cost mitigation strategies and efforts to improve the management of expenses so as to mute large increases in expenditures due to the increased on-campus activity.

Regent Kudo asked about the impact of rising interest rates on the university. VP Young replied that, while increased interest rates will have some positive impacts on the university's short-term investment interest income, largely negative effects will be experienced in the form of increased costs due to the price escalation of commodities. Additionally, the hike in interest rates may impact the university in terms of increased costs associated with bond financing for capital improvement projects (CIPs), affect the availability of CIP funding from the Legislature, and increase overall construction costs. Given this information, Regent Kudo inquired as to whether the administration has considered entering into standstill agreements on development projects to hedge against inflationary pressures. VP Young replied that the administration is not currently considering measures regarding price guarantees or interest rate hedges on any current or potential development projects.

Regent Acoba inquired as to whether all of the major units of the university are compliant with funding reserve requirements contained in the RPs. VP Young responded that all university campuses are at or above established funding reserve requirements when considering the Tuition and Fees Special Fund, which is the primary funding reserve for campuses.

Regent Acopan arrived at 11:32 a.m.

C. Status of Higher Education Emergency Relief Funds (HEERF)

VP Young reported on the status of the expenditure of HEERF funds received by the university as part of the federal coronavirus stimulus response funding packages and briefly reviewed the three tranches of funding available, the amounts received, the expenditures of funds by campus, and funding restrictions. As of March 31, 2022, the university expended about \$144.9 million of the \$242.4 million it was awarded. He also noted that the United States Department of Education has extended the deadline to expend all federal funds received to June 30, 2023.

Regent Haning asked whether HEERF funds could be used for infrastructure development or real property acquisitions. VP Young noted the restrictions placed upon

HEERF funds stating that they could not be used for infrastructure improvements or to purchase real property unless there was a direct tie to an issue related to COVID-19 such as the purchase of building air filtration equipment to protect the health and safety of building occupants.

Board Chair Moore questioned whether HEERF funds not awarded as direct student aid could be used to eliminate student-debt to the university. VP Young responded in the affirmative stating that funds have been used by the university to settle past accounts for a number of students. However, he stressed that the use of funds for this purpose was restricted to student debt incurred during the pandemic.

D. Committee Annual Review

Vice-Chair Higaki referenced the committee annual review matrix provided in the materials packet stating that it sets forth the actions carried out by the committee throughout the year. He relayed Chair Westerman's thoughts on the work of the committee and expressed Chair Westerman's thanks to everyone for their hard work over the past academic year. He also asked if committee members had any questions or comments about the matrix.

Regent Haning questioned why the stated committee duty of discussing the implementation of budgetary decisions with the administration did not take place. Vice-Chair Higaki replied that he was unaware of the reasons for the committee's lack of discussions on this topic and requested follow-up by the Board Office on this matter.

V. ADJOURNMENT

There being no further business, Vice-Chair Higaki adjourned the meeting at 11:48 a.m.

Respectfully Submitted,

/S/

Kendra Oishi
Executive Administrator and Secretary
of the Board of Regents