

**Minutes
Investment Committee
Board of Trustees
September 15, 2009**

IN ATTENDANCE:

Investment Committee Members:	Dr. Edward Britt Brockman, Chair Mr. Stephen P. Branscum Mr. James W. Stuckert
Community Advisory Members:	Mr. Henry Clay Owen Mr. Billy B. Wilcoxson
Board of Trustees Members:	Ms. Mira S. Ball Mr. Carol Martin Gatton Ms. Pamela T. May Ms. Sandy Bugie Patterson Ms. Robynn M. Pease Mr. Erwin Roberts
Investment Staff & Consultants:	Ms. Angela S. Martin Ms. Susan I. Krauss Ms. Donna A. Counts Mr. Rob Palmeri (R.V. Kuhns & Associates) Mr. Steve Hahn (R.V. Kuhns & Associates)
Others:	Dr. Lee T. Todd, Jr. Mr. Frank A. Butler Dr. Michael Karpf Ms. Barbara W. Jones Mr. D. Michael Richey Mr. Sergio L. Melgar Ms. Ronda S. Beck

The Investment Committee meeting was called to order at 9:00 a.m. Dr. Brockman noted that Jim Stuckert had been named as a board member and was no longer serving in the community advisor position. He also congratulated Angie Martin on her appointment to Treasurer.

Dr. Brockman asked for a motion to approve the June 9, 2009 minutes. Mr. Gatton made the motion to approve the minutes, Mr. Branscum seconded the motion and all approved.

Dr. Brockman introduced IC1 and asked for a motion to approve the recommendation that the Investment Committee authorize investment staff and consultant R. V. Kuhns & Associates (RVK) to issue a request for proposals for a value added real-estate manager. Mr. Stuckert made the motion to approve and Mr. Branscum seconded the motion.

Ms. Krauss pointed out that the RFP would focus on Value Added Real Estate and staff hoped to bring a recommendation to the Committee at the March, 2010 meeting. Ms. Krauss reviewed the proposed timeline from the updated Real Estate Pacing Study included with the IC1 summary. This pacing study is

completed one to two times per year as a planning tool with the objective of building the real estate allocation prudently over the next few years. She noted that RREEF had been notified last June that they would be terminated as UBS will be the sole core manager with the 4% allocation. RREEF has suspended fund redemptions and it is anticipated that it will be twelve to eighteen months before RREEF begins paying down redemptions. Currently the value added managers are Wrightwood Capital and TA Associates. It is anticipated that two more value added managers will be added over the next two years. The asset allocation plan also includes the addition of four opportunistic managers and this allocation could be initiated late next year. At this point it is anticipated that the twelve percent target allocation will be reached by December 2013, with the total real estate investment portfolio allocated 33.3% to Core Real Estate, 33.3% to Value Added Real Estate and 33.3% to Opportunistic Real Estate. Mr. Stuckert asked how the real estate allocation was reviewed. Ms. Krauss responded that it was reviewed annually as part of the overall asset allocation study, and on an on-going basis as needed in response to changing economic conditions and capital markets. The Committee unanimously approved IC1.

Dr. Brockman introduced Steve Hahn of RVK to discuss the private equity pacing analysis. Mr. Hahn began by stating that the most recent private equity valuation date was March 31, 2009 due to the illiquid nature of the securities. The private equity allocation on March 31, 2009 was \$17,580,981, or 2.89%. The target allocation is seven percent. He reminded the committee that private equity commitments are drawn down over time and require a regular commitment to establish appropriate targets. Mr. Hahn noted that paid in capital closely tracked previously estimated levels. Capital calls from current commitments are expected to continue in the near term. Distributed capital has lagged early expectations, but is expected to increase with the maturation of the investments, noting that distributions are returned to investors as they occur rather than be re-invested. Valuation and allocations outpaced expectations in recent periods, and it is expected that these will peak near 2013 and will continue to decline afterward with distribution activities, assuming no new commitments are made. As of March 31, 2009 a total of \$80,968,203 had been committed to private equity funds. Mr. Hahn noted that for future private equity allocations, it will be important to diversify across global geographies and by stage of investments (i.e. multistage, buy-out, venture and opportunistic.). Mr. Hahn reviewed a proposed commitment budget for the next five years that will allow UK to reach and maintain the seven percent target allocation prudently over the next few years. Mr. Hahn noted that this commitment budget is updated and reviewed periodically with staff. The plan outlines annual funding of \$20 million initially and gradually increasing to \$30 million by 2013. Mr. Hahn recommended consideration be given to continuing with follow-on investments for both Pantheon and Commonfund. He also recommended a continued allocation to distressed debt opportunities as a component of the opportunistic allocation as distressed is a very attractive investment in the current environment.

Mr. Stuckert asked who developed the private equity valuations. Mr. Hahn replied that those were valued by the individual funds managers and also by the fund-of-funds managers, consistent with FASB 157. The manager valuations are subject to two external audits as the individual fund statements are audited, as well as the fund of fund statements.

Ms. Krauss discussed the next item on the agenda, an update on the investment strategy implementation plan. Ms. Krauss referred to the chart in the Committee notebook that summarized the current asset allocation, the target allocation and the transition plan. The Phase 1 transition is complete and primarily involved the implementation of the new non-US strategies and Wellington's real return strategy. During Phase 1 of the transition, from December 1, 2008 through March 2, 2009, the US Equity allocation was reduced by roughly \$55 million and used to fund Non-US Equity. Also, Fixed Income was reduced by roughly \$50 million and replaced with \$35 million in non-US Equity, \$12 million in Real Return and \$3 million in Real Estate.

Ms. Krauss reported on Phase 2 of the transition, which will be implemented in four quarterly installments and began June 2009. The second installment will be complete at the end of this month, the

third installment will be in December and the final installment in March 2010. Upon completion, the Phase II transactions will reduce US Equity by roughly \$38 million, Non-US Equity by roughly \$27 million, and Global Equity by roughly \$51 million. The reductions these asset classes will be used to fund Absolute and Real Return and rebalance Fixed Income.

Ms. Krauss reported during Phase 3, planned to occur over the next several years, US Equity (roughly \$18 million) and Non-US Equity (roughly \$13 million) will be used to fund Private Equity. Additionally, Fixed Income (roughly \$31 million) will be used to fund Real Estate.

Dr. Brockman introduced the next item on the agenda, the performance review and market update by RVK. Mr. Palmeri began with a market review for the period ending June 30, 2009. The second quarter of calendar year 2009 saw an increase in all major equity indexes. The rally that started in early March was considered a “low quality” rally, which is typical when an economy initially comes out of a recession. The only negative in the market was real estate indexes, which typically lag in market recoveries. RVK is anticipating lower returns in Real Estate and that is why the investment in opportunistic real estate has been put on hold for a while. While it was a good quarter, the fiscal year shows a decline across all sectors, for the worst year since the Depression.

Mr. Palmeri moved on to review the UK Endowment investment allocation and performance. The UK endowment portfolio allocation was overweight in domestic and international equities and underweight in other areas in relation to the policy targets. This was anticipated as a part of the implementation plan to reduce overall equity slowly over time to fund other asset classes and will continue until the new allocation is implemented. For the fiscal year ended June 30, 2009 the total fund returned -20.94%, net of fees, underperforming the policy benchmark by 1.34%. Most of the underperformance was due to the overweight in poor performing equity asset classes compared to the benchmark. For the quarter ending June 30, 2009, the fund had a total return of 15.14%, far exceeding the policy benchmark of 10.45%, which was primarily due to the overweight to equities relative to the policy benchmark.

The review of the asset class performance shows that for the fiscal year ended June 30, 2009, the Fixed Income composite outperformed, while Domestic Equity, Global Equity International Equity and Real Estate Composites underperformed their respective benchmarks. For the quarter ending June 30, 2009 the Domestic Equity, Global Equity and Fixed Income composite outperformed while the International Equity and Real Estate composites underperformed their benchmarks. Mr. Palmeri commented on the Real Estate manager RREEF America II as having underperformed its benchmark, net of fees, by 14.31% for the fiscal year. He noted that RREEF has appraised 100% of its portfolio over the past few quarters marking down property valuations, while properties in the NCREIF Property Index are appraised once per year, with one-fourth of the properties appraised each quarter. The RREEF accelerated appraisal process was a large factor in the underperformance. He stated that the index will likely fall as valuations of its properties take place over time. However, RREEF will be eliminated from the portfolio as UK reduces its core real estate in order to gain exposure to value added and opportunistic real estate strategies in a designed plan to diversify the total real estate component of the portfolio as part of the new asset allocation strategy.

Committee members asked questions related to the investment performance report. Mr. Stuckert asked what institution was represented by the square in the top left quadrant on the scattergram on page 28 of the performance report for the quarter ending June 30, 2009. Mr. Palmeri responded that he will try to find out the asset allocation represented by the point, but that the institution names in the database are confidential. More questions were asked about the real estate sector performance and valuations. Mr. Palmeri offered to bring the real estate expert to a future meeting to discuss this asset class in more detail.

The next item on the agenda was a review of the Cash, Overnight and Short-Term Investment Report. Ms. Counts reported that as of July 31, 2009 the total portfolio subject to the short term investment policy

was \$405.8 million. Overnight investments totaled \$139.6 million, and had a rate of return of 0.49% due to an agreement between OFM and US Bank. Staff anticipates that these returns will not continue in light of the other market returns. Short term investments totaled \$266.2 million, of which \$65.0 million was invested in the OFM short term investment pool with an annualized monthly return of 0.84%; \$60.0 million was invested in the OFM intermediate pool with an annualized monthly return of 4.08%; \$43.8 million was invested in the Fidelity Government Fund, with an annual return of 0.25%; \$83.7 thousand was invested in the Dreyfus Governmental Fund with an annual return of 0.07%; and, another \$93.3 million was invested directly in federal agencies and instrumentalities having yields ranging from 1.25% to 3.77%. Ms. Counts reported that investment returns compared favorably to the market performance indices of the three month T-bill rate of 0.18%, the fed funds yield of 0.18% and the 2 year Treasury note rate of 1.12% as of July 31, 2009.

Committee members asked a few follow-up questions related to the endowment investments. Mr. Wilcoxson asked about the value of the hospital quasi endowment, with an original value of \$225 million. Ms. Krauss responded that the endowment had a value of approximately \$175 million as of August 31, 2009. Mr. Gatton asked Mr. Palmeri what is being done with the portfolio in anticipation of inflation. Mr. Palmeri responded that there was some exposure to real return strategies which is closely correlated to inflation.

With no further business the meeting adjourned at 10:30 a.m.

Donna Counts
Office of the Treasurer