

Meeting Minutes of the Investment Committee  
University of Kentucky  
Monday, December 14, 2020

The Investment Committee of the University of Kentucky Board of Trustees met on Monday, December 14, 2020, via Zoom Webinar.

A. Meeting Opened

Chair of the Investment Committee, Elizabeth McCoy, called the meeting to order at 2:00 p.m. and requested a roll call.

B. Roll Call

The following members of the Investment Committee were in attendance: Elizabeth McCoy, Joe R. Bowen, Michael A. Christian, Hollie Swanson and Barbara Young. The following Committee member was not in attendance: Carol Martin "Bill" Gatton.

The following Community Advisory members were in attendance: William C. Britton, James F. Hardyman, Quint Tatro and Myra L. Tobin.

The University Investment Staff was represented by Chief Investment Officer, Todd D. Shupp, and Investment Officer, Nancy K. Rohde.

Fund Evaluation Group (FEG) was represented by Michael J. Aluise, Christian Busken and Rebecca S. Wood.

C. Approval of Minutes for September 10, 2020

Chair McCoy called for a motion to approve the minutes from the Committee meeting on September 10, 2020. The motion was moved by Trustee Swanson and seconded by Trustee Bowen. The motion passed without dissent.

D. Real Assets Strategy Review

Senior Vice President – Head of Real Assets, of Fund Evaluation Group, Mr. Christian Busken, presented a real assets strategy review. He began with the main reasons that the Portfolio is invested in real assets which include diversification benefits, total return, inflation protection, and current income. The Portfolio allocates across three broad categories (real estate, natural resources, and infrastructure) via both public and private investments. Mr. Aluise addressed the role of real assets within the Portfolio. Given that inflation is a primary component of the Portfolio's return objective, allocating capital to inflation-sensitive securities is prudent. Of the 7.5% primary return objective, 5% is made up of spending and expenses, while 2.5% is the inflation assumption. Mr. Busken noted that while we have not seen inflation in a while, it does not mean we never

will. It is difficult to predict inflation and it is therefore prudent to evaluate the total return expectation of an investment within this area of the portfolio rather than solely potential inflation protection.

Mr. Busken then discussed how various real asset investments behave during periods of rising inflation and falling inflation. Diversified exposure across real asset segments is important to build a well-rounded portfolio. Broadening out to other areas of the portfolio, Mr. Aluise provided a comparison of how equities and core bonds perform in similar periods of rising inflation and falling inflation. He noted that equities have produced real returns in periods of rising inflation while core bonds provide some of the weakest results in periods of rising inflation.

Trustee Ramsey asked how the incoming Biden administration might affect our Portfolio strategy as it relates to wind and solar energy. Mr. Aluise replied that FEG remains vigilant in their research on both sides of the energy spectrum and they have been reviewing opportunities on the public and private side, including renewable energy. Mr. Busken added that renewable energy has been getting a lot of attention recently and FEG is staying selective in reviewing the opportunity set. Trustee Swanson asked if FEG similarly expects increased interest in infrastructure as a result of the new administration. Mr. Busken remarked on the large capital flow that has moved into infrastructure. FEG's approach to this area has been to invest in smaller managers who can operate at the less efficient end of the market, reposition those assets, and sell to bigger managers.

Mr. Aluise next addressed two important features of private investments, with a focus on the private real asset portfolio. The first is the ongoing modeling of implementation pacing for private real assets, which is necessary to ensure the Portfolio stays fully invested as private funds are regularly realized and proceeds are distributed. The second is the specialized approach to measuring performance within the private space, which is needed given the unique timing of asset flows in these strategies.

Lastly, Mr. Busken discussed the impact of COVID-19 on the real assets landscape and highlighted some managers within the UK Portfolio. Overall, the real assets Portfolio has produced strong results relative to asset class benchmarks and remains well-diversified, balanced between inflation-sensitive assets and return-seeking assets. Trustee Ramsay asked for Mr. Busken's opinion on the office real estate sector, specifically the impact from the work-from-home trend that accelerated during the pandemic. Mr. Busken replied that the outlook for this sector is uncertain. He pointed out that due diligence is currently underway for investment in a fund that focuses on data centers, an area that is considered a beneficiary of the same work-from-home trend that is impacting traditional offices.

#### E. ICR 1 – Approval of Endowment Investment Policy

Mr. Shupp presented a recommendation that the Investment Committee approve the revised Endowment Investment Policy. The revised policy reflects the adoption of modestly shifted asset allocation targets intended to enhance the Portfolio's expected

return while maintaining prudent diversification. Other minor changes include policy benchmark adjustments that correspond with the asset allocation targets and updates to accurately reflect current staff designations. Chair McCoy called for a motion to approve ICR 1. The motion was moved by Trustee Bowen and seconded by Trustee Swanson. The motion was passed without dissent.

#### F. Investment Staff Report

Mr. Shupp presented the Investment Staff Report beginning with an overview of the Endowment asset allocation as of October 31, 2020. He noted a substantial amount of capital call activity within private equity as well as a modest decline in public equities. There was a slight uptick in global fixed income due to higher valuations coming in for private credit strategies. Real assets were down slightly, driven by a decrease in public real assets. However, private real assets ticked up slightly due to capital call activity. Finally, diversifying strategies remained unchanged for the period. Turning to rebalancing activity, UK received an addition of approximately \$4.4 million to the Operating Post-Employment Benefits (OPEB) in September and a \$35 million inflow to the Quasi-Operating Endowment in late October. These funds were reinvested in a diversified manner across asset classes.

Next, Ms. Nancy Rohde discussed recent manager appointments, terminations and due diligence for the period. Beginning with manager appointments, UK made two new commitments within the private equity portion of the Portfolio. The first was a \$10 million commitment to Staple Street and the second was a \$5 million commitment to Carousel Capital Partners. Regarding terminations, a full redemption was made from RWC Frontier Markets Equity Fund due to changes made within the emerging markets allocation earlier this year. Finally, Ms. Rohde discussed manager due diligence and research during the period, which featured many investment manager annual meetings and industry conferences that took place remotely via Zoom webinar.

#### G. Performance Review and Market Update

Mr. Aluise began the performance review and market update with a review of major asset class market returns, drawing attention to the year-to-date performance and the impact the month of November had on these values. He then addressed UK performance as of October 31, 2020. Mr. Aluise commented on what worked well and not as well for the October year-to-date period. High-quality fixed income significantly outperformed, and hedged equity and U.S. equity also contributed. The Portfolio's value-oriented international equity allocation, U.S. small-cap equities, and diversifying strategies managers did not work as well for the period. He stated that many of these laggards could be moving to the positive side of the sheet, once November performance is accounted for, given that equity performance has shown signs of broadening. In summary, the Portfolio has bounced back materially off the March 2020 lows and performance is positive fiscal year to date. Moving forward, steps will be taken to prudently transition the Portfolio toward the newly approved asset allocation targets.

Mr. Shupp echoed Mr. Aluise's comments regarding the positive broadening market shift seen since late October. He also noted a paper recently published by Mr. Busken and FEG related to inflation which will be published to Director's Desk. Trustee Young asked if the recent market shift should be viewed as a longer-standing rotation or a short-term blip in market leadership that will quickly revert. Mr. Shupp replied that the broadening in market performance seems tied to the recent rollout of the COVID-19 vaccine, which gave investors optimism that more cyclical segments of the market may begin a recovery. He stated that we are not making a bet on a fast return to normalcy and acknowledge that we are not out of the woods yet, but the improved performance of cyclical sectors is a positive sign that warrants highlighting.

H. Other Business

Mr. Shupp reviewed the 2021 Investment Committee meeting schedule and tentative agenda items. The upcoming February meeting will include an emerging markets discussion as part of the public equity strategy review. Subsequent meetings will include the risk review in May, as well as the annual retreat in September.

I. Meeting Adjourned

Hearing no further business, the meeting was adjourned at 3:07 p.m.

Respectfully submitted,



Kristina W. Goins  
University Financial Services