

# The UCLA Foundation

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## **INVESTMENT POLICY STATEMENT FOR ENDOWED INVESTMENT POOL**

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On 9-5-2012, the Investment Steering Committee reviewed the IPS, and recommended approval by the Foundation Board of Directors

Reviewed by UCLA Investment Company Board of Directors, September 18, 2012

Approved by The UCLA Foundation Board of Directors, September 21, 2012

First Proposed modifications approved by UCLA Investment Company Board of Directors and The UCLA Foundation Board of Directors, June 2, 2014

Second Proposed modifications approved by UCLA Investment Company Board of Directors and The UCLA Foundation Board of Directors, March 14, 2017

Third Proposed modifications approved by UCLA Investment Company Board of Directors and The UCLA Foundation Board of Directors, June 5, 2018

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## INTRODUCTION

The UCLA Foundation's endowment testifies to the generosity of the University's friends and alumni and their faith in University of California, Los Angeles (the "University"). The Board of Directors of The UCLA Foundation (the "Foundation") is aware of the responsibility which is theirs to prudently manage endowment funds which are given to the University. The Foundation has placed oversight responsibility for the endowment fund with its wholly owned subsidiary, UCLA Investment Company.

This Investment Policy Statement establishes policies for the administration and investment of the Foundation's endowment fund assets by UCLA Investment Company. This policy formally documents the goals, objectives, and guidelines of the endowment fund's investment program. Its purpose is to document the policies and procedures that are intended to provide the greatest probability that the funds objectives are met in a prudent manner, consistent with the established guidelines.

## MISSION

The mission of the Foundation's endowment is to support the educational mission of the University by providing a reliable source of funds for current and future use. The endowment has two primary missions. First, the purchasing power of the endowment's assets must be maintained in perpetuity and, second, the endowment must achieve investment returns sufficient to sustain the level of spending necessary to support ongoing University operations.

## PHILOSOPHY

At the core of this investment policy statement is a set of fundamental investment beliefs which are the underpinnings of all investment policies of The UCLA Foundation (the "Foundation"):

- Endowment funds are by definition perpetual funds. The Foundation can afford to take a very long-term view in setting investment policy.
- Taking into account the long-term nature of endowment funds, the Foundation should maintain a bias toward equity investments, which have historically produced higher long-term returns.
- Diversification can reduce risk and increase return.

## INVESTMENT OBJECTIVES

The primary investment objective of the Foundation endowment is to earn an average annual real total

return of at least 5% per year over the long term, net of cost. Attainment of this objective will enable the University to maintain the purchasing power of endowment assets in perpetuity and meet its current spending policy.

A secondary investment objective of the endowment is to outperform over the long term (defined as rolling five-year periods) a blended custom benchmark based on a current asset allocation policy of: 50% MSCI All Country World Index, 15% Citigroup 3 Month Treasury Bill Index X 2, 10% Cambridge Associates LLC U.S. Private Equity Index, 5% Citigroup 3 Month Treasury Bill Index (Cash), 5% Merrill Lynch High Yield Master II Index, 5% NCREIF Property Index, and 10% Consumer Price Index for All Urban Consumers (annualized CPI-U) + 6%.

## SPENDING POLICY (adopted 6-20-2000)

The Foundation's spending policy was developed to meet several objectives, namely to: (a) provide a current source of funding for UCLA endowment beneficiaries, (b) provide year-to-year budget stability and (c) meet intergenerational needs by protecting the future purchasing power of the fund against the impact of inflation.

The Foundation does not follow a specific rule for determining the spending policy. Each fiscal year, a stated payout percentage is calculated that, when applied to average market values, will result in actual payout dollars that meet the program objective.

- Twelve quarter average of market values are used to smooth monthly fluctuations
  - Prior six quarters actual investment returns
  - Forecasted next six quarters using expected returns

The combination of spendable income rate, anticipated expenses and allowance for inflation should not exceed expected returns. General economic conditions are considered in setting the spendable income rate.

## ASSET ALLOCATION POLICY

The single most important investment decision is the allocation of endowment funds to various asset classes. The primary objective of the Foundation's asset allocation policy is to provide a strategic mix of asset classes which produces the highest expected investment return within a prudent risk framework.

Each asset class should not be considered alone, but by the role it plays in a diversified portfolio. Diversification among asset classes has historically increased returns and reduced overall portfolio risk. How asset classes relate to each other is the key to making asset allocation decisions within the context of overall endowment risk and return.

As stated earlier, a core fundamental investment belief of the Foundation is to maintain a bias toward equity investments, which produce higher long-term returns. In addition, the endowment's long time horizon is well suited to exploiting illiquid, less efficient markets that offer higher potential returns.

With these basic tenets in mind:

- Equity bias – increases returns
- Diversification – reduces risk
- Long time horizon,

the Foundation has decided to invest in the following asset classes:

**DOMESTIC EQUITY:** Publicly traded U.S. stocks are a core asset class of institutional portfolios with long-term investment horizons and modest liquidity constraints. The objective of the Domestic Equity portfolio is to generate investment returns with adequate liquidity through consistent exposure to common stock investments. The Domestic Equity portfolio may contain both a passive core and an active investment strategy. The passive core is meant to provide low-cost exposure to the U.S. equity market and will primarily be achieved through the use of, but not limited to, swaps, ETFs and other derivative products, utilized from time to time to add or reduce the directionality of the portfolio. The portfolio seeks to generate incremental returns (alpha) through its active investment strategy. The active investment strategies will include both long/short and long only managers. The primary benchmarks for the Domestic Equity portfolio are the Russell 3000 and the S&P 500.

**INTERNATIONAL EQUITY:** Includes publicly traded common stock of predominantly international markets, both in developed and developing/emerging regions. In general, it is perceived that through increasing industrialization, strong demographic trends and increasing depth and efficiency of capital markets in these countries, that these markets could generate higher returns than the U.S. markets. In addition, over long-term periods of time, international equities have relatively low correlations to the U.S. markets, making them not only a return source, but a portfolio diversification tool. The objective of the International Equity portfolio is to generate investment returns with adequate liquidity and to provide a diversification benefit to the entire portfolio. The International Equity portfolio takes an active investment approach due to the less efficient nature of the markets, which should generate higher returns than a passive core and will be implemented through both long/short and long only managers, potentially in all regions of the world. Despite an active approach, from time to time there may be opportunities to add or reduce directionality to international markets through the use of, but not limited to, swaps, ETFs and other derivative products. The primary benchmark for the International Equity portfolio is the MSCI All Country World ex-U.S. index.

**GLOBAL EQUITY:** Includes publicly traded common stock from a combination of domestic, developed international and developing/emerging international markets. The objective of the Global Equity portfolio is to generate investment returns with adequate liquidity through a globally diversified portfolio of common stocks that will provide return sources from less correlated regions of the world. The Global Equity portfolio will largely employ an active investment strategy, though from time to time may utilize swaps, ETFs and other derivative products to add or reduce the overall directionality of the portfolio. Investments in the Global Equity category typically have a broader investment mandate and cannot be classified specifically into domestic or international alone due to the global approach of the portfolio management function. An investment is generally defined as global if the investment has more than 20% of its gross exposure domiciled outside of either its home country or its primary investing region and investments will include both long/short and long only managers. The primary benchmark for the Global Equity portfolio is the MSCI All Country World index.

**PRIVATE EQUITY/VENTURE CAPITAL:** Includes illiquid investments in both private and public companies both domestically and internationally. These investments include venture capital, buyouts, high yield, and subordinated debt. The Private Equity/Venture Capital portfolio's objective is to earn higher returns than the public equity markets over the long term. This portfolio invests in highly illiquid positions and should generate higher returns as compensation for that illiquidity. A secondary objective of these investments is to provide diversification. The portfolio's strategy is to invest in a select number of funds managed by the highest quality management teams usually organized as limited partnerships. Managers are sought which have proprietary deal flow and whose experience enables them to bring strategic, operational, or technical expertise to a transaction in addition to financial acumen and capital. The portfolio is diversified across categories and investment stage. The Private Equity/Venture Capital portfolio's primary benchmark is the Cambridge Associates LLC U.S. Private Equity index.

**MULTI-STRATEGY:** Includes managers specializing in asset allocation across multiple investment strategies that have low correlations and/or market exposure to other asset classes. The objective of this asset class is to generate equity-like returns with less volatility and market exposure than global equities. Diversification across strategies and positions will be wide in order to dampen portfolio volatility. The portfolio's liquidity will be moderate, less than that of the traditional public equity portfolios, but more liquid than the Private Equity/Venture Capital portfolio. This portfolio will focus on areas and strategies where value added by active management can contribute a substantial portion of the return. The portfolio may utilize swaps, derivatives, ETFs or other instruments in order to manage risk. The primary benchmark for this asset class is 2 X Citigroup 3 Month Treasury Bill Index.

**CREDIT:** Includes investments in publicly and privately traded credit and credit related securities. The portfolio can hold a mix of traditional benchmark relative strategies and absolute return strategies. It is expected that many types of securities could be considered credit sensitive and the portfolio will contain, but not be limited to, bonds, equities, derivatives, currencies and private securities. The portfolio will be diversified across credit asset classes and hold a mixture of investment grade and high yield securities of performing and non-performing debt. Liquidity and volatility will vary by strategy. The portfolio will focus on capital appreciation rather than current income and will not be managed to specific duration guidelines. The primary benchmark is the Merrill Lynch High Yield Master II Index.

**REAL ASSETS:** Real Assets represent claims on future streams of inflation-sensitive income, supplying protection against unanticipated inflation and playing an important diversifying role in the portfolio. Real Assets are comprised of investments in oil and gas, commodities, timber, and

inflation-linked bonds. The primary benchmark is the Consumer Price Index for All Urban Consumers (annualized CPI-U) + 6%.

REAL ESTATE: The long-term objective of the Real Estate portfolio is to provide equity-like returns while providing a partial hedge against inflation. In addition, Real Estate is an extraordinary diversifier within the overall endowment due to its low correlation with other asset classes. The portfolio is directed largely to illiquid investments with a long time horizon. The primary benchmark is the NCREIF Property Index – a broad index of institutional quality private real estate.

CASH: Cash is a very risky investment for an institution with a long time horizon due to its low return and the diminution of purchasing power that entails. It is considered prudent to minimize the use of cash in the overall endowment. Outside of extraordinary market dislocation periods, cash will exist from time to time for transaction and/or rebalancing needs only.

With the above serving as the approved asset classes, the Foundation has developed the following as its optimal long-term asset allocation policy.

<b><u>ASSET CLASS</u></b>	<b><u>Long-Term Desired Range</u></b>
EQUITY	
Domestic Equity	10% - 45%
International Equity	10% - 30%
Global Equity	10% - 40%
Total Equity	30% - 75%
PRIVATE EQUITY/VENTURE	0% - 25%
MULTI-STRATEGY	5% - 20%
CREDIT	0% - 15%
REAL ASSETS	0% - 15%
REAL ESTATE	0% - 10%
CASH	0% - 10%

## PORTFOLIO REBALANCING POLICY

The Foundation's Investment Policy Statement establishes the long-term asset allocation targets for the endowment and certain minimum and maximum constraints for each individual asset class. The Board of Directors of UCLA Investment Company will rely on investment staff to determine allocations within the stated ranges and to initiate rebalancing of the fund whenever minimum or maximum constraints are violated.

Rebalancing is a critical element in controlling the long-term asset allocation of the endowment. The Portfolio Rebalancing Policy will be implemented in a systematic and disciplined fashion using the following guidelines:

- In the case of an asset class being below its minimum constraint, monies will be invested in that asset class to bring it back toward its target allocation. UCLA Investment Company will use cash flow to rebalance whenever feasible. When cash is not readily available to facilitate the rebalancing, the Company will trim the asset class that is most overweight.
- In the case of an asset class being above or below its stated range, then over the subsequent two quarters, the Company will attempt to rebalance back within the stated range.
- UCLA Investment Company has the ability to make additions and withdrawals from public market investments with managers with which the Company currently has relationships with for the purpose of portfolio rebalancing.

In a market characterized by extreme volatility in which one or more asset class's minimum and/or maximum constraint is exceeded, UCLA Investment Company will develop and recommend an alternative rebalancing plan subject to the Foundation's approval should the above guidelines otherwise require the sale of investments that may not be prudent and in the best long-term interest of the Foundation.

## INVESTMENT DOCUMENTATION & REPORTING

Statements will be provided quarterly to the Foundation summarizing:

- performance for the quarter and trailing periods for the portfolio
- asset allocation of total portfolio
- market value of the total portfolio

UCLA Investment Company will rely on its investment managers for voting proxies associated with its funds.

UCLA Investment Company will meet quarterly with the Foundation to review the portfolio and its investment results.