

UNIVERSITY ENDOWMENT INVESTMENT PORTFOLIO INFORMATION BACKGROUNDER

The following backgrounder has been prepared to provide a description of the status, performance and recent changes made to the investment structure of the UBC Endowment Funds. Rates of return and performance results are based on information to fiscal year end March 31, 1998. Fund Balance and Asset Mix information is updated to September 30, 1998. This package is in the form of typical questions and answers regarding the Endowment Funds.

What is the Endowment?

The Endowment Fund is the result of 80 years of philanthropy wherein donors have sought to benefit specific aspects of the University's activities in perpetuity. In addition, the university has endowed the proceeds from the prepaid lease of Hampton Place lands. The over half billion dollar current value of the Endowment also results from annual replenishment of capital to protect against inflation erosion so purchasing power stays constant over time. The Endowment benefits over 1900 specific areas in all faculties and in Student Awards and Financial Aid. Individual endowments range from endowed chairs which receive hundreds of thousands of dollars annually all the way to yearly book prizes for outstanding students.

Who has the responsibility for directing and supervising endowment investment practices?

Overall review, performance measurement and investment guidelines for the endowment funds is directed by the University Endowment Fund Investment Advisory Committee. This Committee reports to the Finance Committee of the Board of Governors. Membership for the Committee is:

- The Chair, Board of Governors Finance Committee
- The Vice President, Administration and Finance (Chair)
- The Director, Financial Services
- The Treasurer
- The Dean or designate of the Faculty of Commerce
- The Dean or designate of the Faculty of Medicine

The Associate Treasurer is Secretary for the Committee. The Committee meets with the investment managers on a semi-annual basis to review performance and investment strategy.

What is the legal framework for investment management of the Endowment?

The majority of the UBC Endowment Fund is managed through two segregated endowment pools, the Restricted Fund and the Unrestricted Fund. Until November of 1994, the Restricted Fund was subject to the investment guidelines of the *Trustee Act* of the Province of B.C., which was very limiting as to asset mix. The University, on behalf of the other British Columbia universities, was instrumental in obtaining legislative amendments which moved investment of the Restricted Fund out from under the guidelines of the *Trustee Act* to those of the *Pension Benefits*

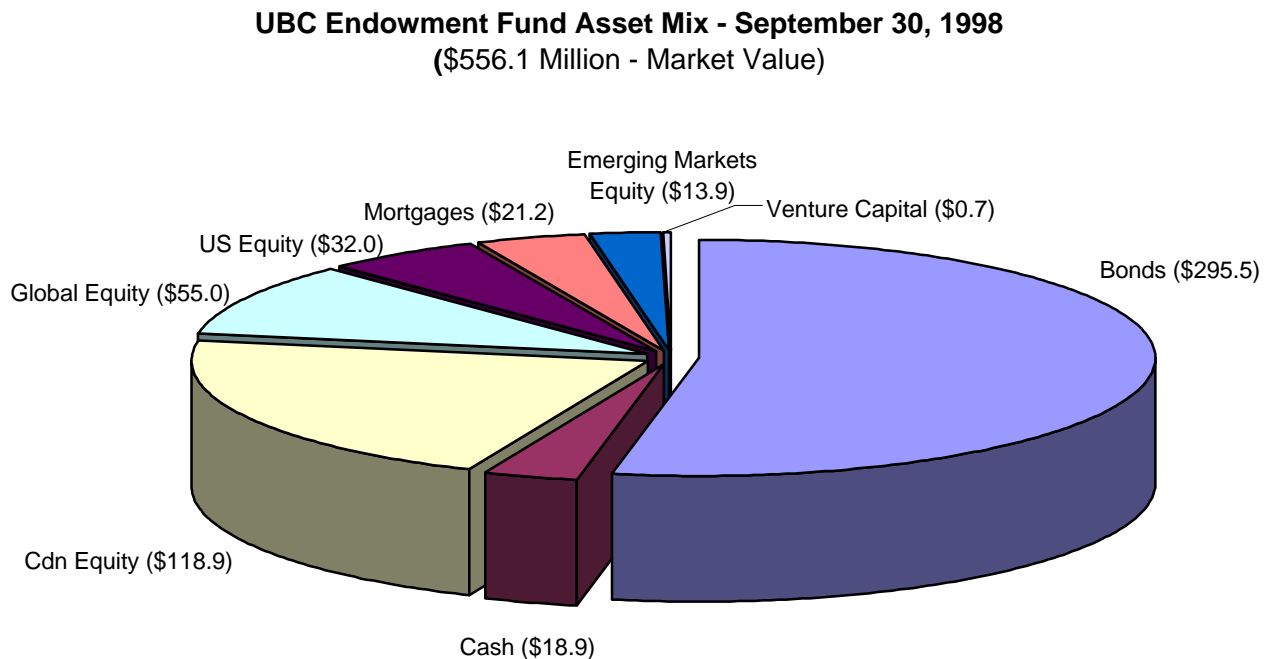
Standards Act of Canada. These guidelines provide more flexibility than the *Trustee Act* and include allowance for a 20% commitment to non-Canadian assets.

The Unrestricted Funds are governed by “prudent person”. Since the late 1980’s, new donations to the University’s Endowment Fund have been directed to this pool. Both the Restricted and Unrestricted Funds are currently invested under the guidelines of the *Pension Benefits Standards Act* of Canada.

At March 31, 1998, the market value of the Endowment was \$579.9 million, by September 30th, and after a substantial market correction, the market value of the portfolio has contracted to \$556.1 million.

What are the broad asset class directives of the Investment Committee?

The current approved long term asset mix for the funds is 60% fixed income and 40% equity. The equity allocation includes Canadian, US, global and emerging market equities. The historic origin of the over weighting in fixed income is related to annual cash requirements of the Endowment Fund. This asset mix constraint is currently under review as annual cash spending requirements may be generated by selling equity positions as readily as via bond coupons. The graph below details the asset mix at September 30, 1998.



Who invests the endowment funds?

Phillips, Hager & North (PHN), a respected Vancouver based investment management firm, manages the largest portion of the Endowment Fund. PHN runs a balanced mandate for the Endowment Fund, with investments in fixed income securities and equities, including Canadian, US and global. PHN has consistently generated above average investment returns.

Nicholas Applegate of San Diego, California and Global Asset Management (GAM) of London, England were retained in July, 1997 to invest roughly 6.0% of the total Endowment Fund. GAM has an emerging markets mandate (emerging markets are defined as global excluding US, Canada and Europe, Australia and the Far East, known as “EAFE”) while the Nicholas Applegate mandate focuses on international small cap growth companies in emerging and non-emerging countries. The allocation to PHN’s non-Canadian assets was reduced to provide funding for these mandates. The addition of these managers has also served to mitigate the so-called “manager risk”, i.e. the predominance of the assets being managed by PHN (see chart and accompanying narrative below).

UBC Properties Inc. has invested in commercial and industrial mortgages on behalf of the Endowment Fund. This mandate is being wound down as the mortgages in the portfolio mature (only one position remains).

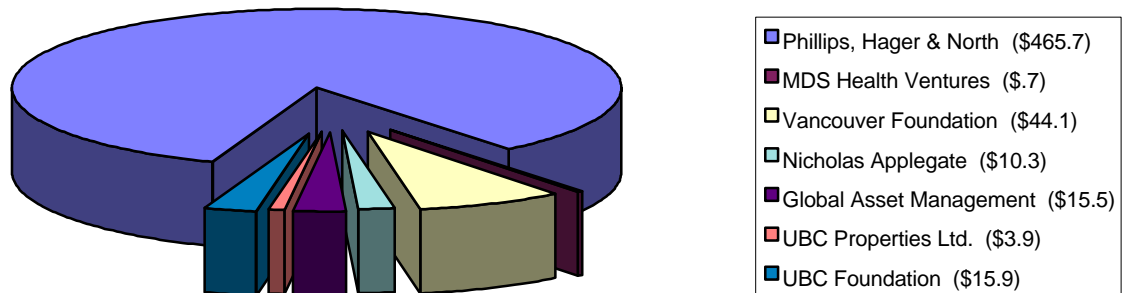
As of September 1998, \$.7 million was invested with MDS Health Ventures Fund in a venture capital fund; an additional \$.8 million remains to be invested in this fund as opportunities arise. The Vancouver Foundation holds roughly \$37.8million (market value) in assets for the benefit of the University, and \$6.3 million for the UBC Foundation. While a portion of the funds held at the Vancouver Foundation are controlled by the University (such as the President’s Fund), the remaining funds are controlled by the Vancouver Foundation with income allocated to the University on an annual basis. The rate of return on the funds held at the Vancouver Foundation for 1997 was 11.4%. The Vancouver Foundation currently uses three external advisors for investment management services.

In addition to the funds managed by the Vancouver Foundation, the UBC Foundation holds a significant position in Wall Financial Corporation for the benefit of UBC’s Peter Wall Institute (\$15.9 million market value at September, 1998).

Phillips, Hager & North also manage \$17.3 million in two Forest Renewal BC sourced funds for the benefit of UBC Forest Sciences. A portion of this endowment (\$12.5 million) is scheduled to be transferred to UBC in 1999.

At September 30, the University and UBC Foundation endowment pools were invested as follows:

UBC Endowment Fund Investment Managers
September 30, 1998
(\$556.1 Million - Market Value)



During the coming year, the Investment Committee will continue revisions of the investment structure and management of the Endowment. This process will include consideration of additional mandates, thereby diversifying risk. Scheduled activities include:

DATE	ACTIVITY	STATUS
September 30, 1997	Emerging Market Manager Selection and Funding	Completed
March 31, 1999	Asset Mix and Investment Structure Review; New Domestic Manager Search and RFP's	In process
June 30, 1999	Domestic Manager Selection and Funding	Pending
September 30, 1999	Non-Canadian Investment Review	Pending

How are investment income and capital gains allocated to endowments?

The concept is similar to that of a mutual fund. Within the pools the University has over 1900 separate endowment and scholarship funds. When a donation is made the new cash "purchases" units in the pool. The purchase price is based on the total market value of the pool divided by the number of units outstanding in the pool on the acquisition date. Income and gains are allocated to a fund based on the number of units held by an endowment.

How much of an endowment's annual income is eligible for distribution?

The objective of endowment administration, past the maximization of returns within acceptable parameters of risk, is to convey the most benefit over time to not only current beneficiaries but also future beneficiaries. In 1991, the Board of Governors approved the Endowment Fund Management Policy which ensures the purchasing power, in constant dollars, of the endowments is maintained. The policy allows for spending of up to 6% of the endowment market value on an annual basis. The University reviews this rate periodically to ensure that the amount capitalized will be sufficient to offset the effects of inflation.

How did the portfolio perform?

The annualized rate of return is calculated on a time weighted basis accounting for opening and closing balances, net contributions, purchases and sales at market value and includes realized and unrealized capital gains and losses. In evaluating investment performance, one needs to consider not only the market and/or other portfolio returns, but the preservation of purchasing power, such that beneficiaries can continue to purchase the same “basket of goods” each year (see above). Therefore, the three endowment portfolio performance objectives include:

1. rate of return equal to the spending rate plus inflation
2. risk free rate of return
3. normal portfolio return

The following table, using the most recent data available, summarizes the results for the four years ending March 31, 1998:

	<u>Objective</u>	<u>Actual</u>	<i>Variance</i>
Spending rate plus inflation	7.6%	14.3%	6.7%
Risk free rate of return:	8.5%	14.3%	5.8%
Normal portfolio return	14.6%	14.3%	-0.3%

The Endowment Fund has experienced tremendous returns in the past few years in a low inflation environment. On a relative performance basis, when compared to other endowment funds, overall returns have been constrained by the *Trustee Act and Pension Benefits Standard Act* guidelines.

Who provides custodial services for Endowment Funds?

CIBC Mellon, who acquired the institutional custody business of Canada Trust, is the custodian for the University's Endowment Funds and holds the University's securities and executes our managers' buy and sell orders.

How does the University's Endowment compare to other institutions?

As of December 1997 the University's Endowment ranked second in market value in Canada, after the University of Toronto, out of 55 universities surveyed nationally by the Canadian Association of University Business Officers (CAUBO). In North America among both privately and publicly funded universities, UBC ranked 87th. For comparative purposes, Harvard ranked number one with an endowment of \$15.1 billion (Cdn) while the University of Washington ranked 59th at \$727 million (Cdn).

The table below highlights the growth of the UBC Endowment over the past 10 years. The achievement of the last 5 year major capital campaign in the early 1990's contributed over \$100 million to the Endowment which, combined with the proceeds of Hampton Place, has firmly entrenched UBC's Endowment amongst the leading Canadian universities.

\$ Millions

Endowments by Size, December 31, 1997

