UTIMCO AT A GLANCE

- Created March 1996
- Manages the investment assets under the fiduciary care of the U.T. System Board of Regents
- $47.7 billion under management as of August 31, 2019
- Governed by a nine-member board consisting of at least three members of the U.T. System Board of Regents, four members appointed by the U.T. System Board of Regents, three of which must have substantial background and expertise in investments, and two members appointed by the Texas A&M System Board of Regents, one of which must have a substantial background and expertise in investments
- Day-to-day management responsibility for the investment assets is delegated to UTIMCO investment team
- Diversified portfolio includes US and global equities, fixed income investments, real estate, private equity, venture capital, and hedge funds

OUR MISSION

We generate superior long-term investment returns to support The University of Texas and Texas A&M University systems as they provide world-class teaching, push the boundaries of discovery, and achieve excellence in patient healthcare for the people of Texas and beyond.
Total Endowment Results

For the year ended August 31, 2019, the Permanent University Fund (PUF) and the General Endowment Fund (GEF) returned +4.5%. The value added by the active management decisions of the UTIMCO team was +0.1% over the Endowments’ Benchmark Policy Portfolio returns of +4.4%. Over the last 10 years, the Endowments have grown at an annualized rate of +8.4% which exceeded the benchmark return by +1.3% annually.

During the year, the total value of the Endowments grew from $32.3 billion to $35.5 billion, an increase of $3.2 billion, and total assets managed by UTIMCO grew by $2.6 billion to end the year at $47.7 billion. Over the last ten years the Endowments have increased in value by $20.4 billion from their starting value of $15.1 billion in August 2009. Over that same 10 year period total asset managed increased by $27.2 billion. At present, the Total Endowment assets managed by UTIMCO rank second in size relative to all other endowments in America.

Market Conditions

This period marked the tenth consecutive year of an equity market expansion and is now the longest bull market period without a significant downward correction in equity market history. The US stock market bottomed on March 9, 2009 and has since gone up a cumulative 333%, leading to total returns of 439% including dividends. Despite relatively slow GDP growth and limited productivity advances in the US, stock markets have moved steadily upwards, supported initially by low valuations and accommodative monetary policy.

Following the “Great Financial Crisis” central banks globally, led by the US Federal Reserve Bank (the “Fed”), drew short-term interest rates down to near zero and went on to use previously untested monetary policies designed to avoid a potential depression. The intended impact of these policies was to spread out the potential negative implications over a longer period of time. In 2018, the Fed began raising rates which led to a sharp equity market decline in the fourth quarter of 2018 with the S&P 500 narrowly missing the 20% decline.

Figure 1
Economic and Financial Condition Indicators

<table>
<thead>
<tr>
<th></th>
<th>Then</th>
<th>Now</th>
<th>Total Change</th>
<th>Annualized</th>
</tr>
</thead>
<tbody>
<tr>
<td>S&amp;P 500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price</td>
<td>676.5</td>
<td>2,926.5</td>
<td>+332.6%</td>
<td>15.0%</td>
</tr>
<tr>
<td>Price/Earnings Ratio (Forward/Trailing)</td>
<td>11.2/11.1</td>
<td>17.7/19.3</td>
<td>+6.5/+8.2</td>
<td></td>
</tr>
<tr>
<td>Volatility</td>
<td>38.5</td>
<td>15.4</td>
<td>23.1%</td>
<td></td>
</tr>
<tr>
<td>US UNEMPLOYMENT (%)</td>
<td>8.3</td>
<td>3.7</td>
<td>-4.6%</td>
<td></td>
</tr>
<tr>
<td>10-YEAR TREASURY-NOTE YIELD (%)</td>
<td>2.9</td>
<td>1.5</td>
<td>-1.4%</td>
<td></td>
</tr>
<tr>
<td>GROSS DOMESTIC PRODUCT GROWTH YEAR OVER YEAR (%)</td>
<td>0.6</td>
<td>4.3</td>
<td>+3.7%</td>
<td></td>
</tr>
<tr>
<td>INFLATION YEAR OVER YEAR (%)</td>
<td>0.2</td>
<td>1.7</td>
<td>+1.5%</td>
<td></td>
</tr>
<tr>
<td>FEDERAL FUNDS RATE (%)</td>
<td>0.25</td>
<td>2.25</td>
<td>+2.0%</td>
<td></td>
</tr>
<tr>
<td>SIZE OF FEDERAL BALANCE SHEETS ($, TRILLIONS)</td>
<td>$1.9</td>
<td>$2.7</td>
<td>$1.9</td>
<td></td>
</tr>
</tbody>
</table>

1 Source: Bloomberg

Then refers to 3/9/2009, now refers to 8/31/2019
which typically represents a bear market. The Fed reversed this trend in 2019 and equity markets rallied strongly. The Fiscal Year straddled both of these periods which led to moderate investment returns for the funds managed by UTIMCO.

Asset Allocation

The Endowments’ goals are to produce attractive long-term returns within a sound and well diversified asset allocation structure, professionally and prudently implemented at all times. In order to achieve these goals over time, three complementary investment portfolios are simultaneously maintained.

- A Global Equity portfolio designed to capture the increase in the value of companies driven by the revenue growth and improved corporate profits that generally accompany periods of positive Gross Domestic Product (GDP) growth and moderate inflation.
- A Stable Value portfolio intended to provide diversification against deflationary conditions (e.g., typical recessions) which see slowing GDP growth and falling profits that generally result in a decline in equity values.
- A Real Return portfolio intended to provide diversification against the wealth-eroding effects on asset values that result from periods where inflation exceeds expectations.

Set out in Figure 2 on the next page is the Endowments’ current asset allocation to the various components of each of the three strategies.

![Joan Moeller](image)

**Joan Moeller**
Senior Managing Director and Chief Operating Officer

### Figure 2

**Endowments Asset Allocation**

<table>
<thead>
<tr>
<th></th>
<th>2019</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GLOBAL EQUITY</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Equity</td>
<td>$10,830.5</td>
<td>$9,911.3</td>
</tr>
<tr>
<td>Directional Hedge Funds</td>
<td>4,221.0</td>
<td>4,538.2</td>
</tr>
<tr>
<td>Private Equity</td>
<td>7,531.4</td>
<td>6,811.8</td>
</tr>
<tr>
<td><strong>TOTAL GLOBAL EQUITY</strong></td>
<td>22,582.9</td>
<td>21,261.3</td>
</tr>
<tr>
<td><strong>STABLE VALUE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global Fixed Income</td>
<td>3,266.8</td>
<td>2,286.4</td>
</tr>
<tr>
<td>Stable Value Hedge Funds</td>
<td>2,621.2</td>
<td>1,330.4</td>
</tr>
<tr>
<td>Cash and Other Assets/Liabilities</td>
<td>397.0</td>
<td>614.3</td>
</tr>
<tr>
<td><strong>TOTAL STABLE VALUE</strong></td>
<td>6,285.0</td>
<td>4,231.1</td>
</tr>
<tr>
<td><strong>REAL RETURN</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gold and Commodities</td>
<td>490.6</td>
<td>818.2</td>
</tr>
<tr>
<td>Natural Resources</td>
<td>2,522.1</td>
<td>2,923.4</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>799.8</td>
<td>554.5</td>
</tr>
<tr>
<td>Real Estate</td>
<td>2,791.3</td>
<td>2,497.3</td>
</tr>
<tr>
<td><strong>TOTAL REAL RETURN</strong></td>
<td>6,603.8</td>
<td>6,803.4</td>
</tr>
<tr>
<td><strong>TOTAL ENDOWMENTS</strong></td>
<td>$35,471.7</td>
<td>$32,295.8</td>
</tr>
</tbody>
</table>

as of August 31,
Investment Philosophy—Creating Long-Term Returns

The Endowments are managed as long-term investment funds with a time horizon exceeding that of most other investors. They have consistent sources of funding with relatively low and reasonably predictable short-term funding requirements. As a result, the Endowments are able to assume significant equity risk as well as higher levels of illiquidity than the typical investor. These two factors alone should typically produce higher long-term returns relative to most other funds. When combined with effective risk systems and risk management, attractive and consistent results have been achieved.

In addition, other factors are key to creating superior risk-adjusted long-term returns.

The Risk-Free Rate

The returns available to an investor without taking incremental risk have declined meaningfully over the past 20+ years. Using the 10 Year US Treasury Bond as a proxy, this rate rose from a low of 1.3% in 2016 to 1.9% today. When taking inflation into account, the deterioration is even more pronounced. Assuming that most investors are trying to earn returns of 5% in excess of inflation, risk-free government bonds are simply no longer helpful in achieving an investor’s return goals. Today, the US 10 year rate is 1.9% versus annual inflation of 1.7%.

Creating “Alpha” (Returns that Exceed Passive Benchmarks)

To achieve this consistently requires both skill and the assumption that markets are not completely efficient, or that their efficiency varies over time and across market cycles. Over the past one and five year periods UTIMCO’s portfolios have produced the results shown in Figure 4 versus passive or competing benchmarks.

Aligning Costs

To achieve cost alignment, UTIMCO seeks to negotiate fees with external managers that are below market and where the manager’s incentives are aligned with our own. Recently, UTIMCO has been collaborating with its key investor relationships to assure that the Endowments receive either a high return or a substantial portion of any excess return over a properly constructed passive benchmark. Attractive co-investment opportunities are also developed with key investment relationships which add to returns and lower costs.

Figure 4

Investments Returns by Portfolio

<table>
<thead>
<tr>
<th>Portfolio</th>
<th>ONE YEAR</th>
<th>FIVE YEARS</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Return</td>
<td>Benchmark</td>
</tr>
<tr>
<td><strong>GLOBAL EQUITY</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Equity</td>
<td>1.6%</td>
<td>(1.3%)</td>
</tr>
<tr>
<td>Directional Hedge Funds</td>
<td>3.8%</td>
<td>0.4%</td>
</tr>
<tr>
<td>Private Equity</td>
<td>11.3%</td>
<td>11.9%</td>
</tr>
<tr>
<td><strong>TOTAL GLOBAL EQUITY</strong></td>
<td>5.3%</td>
<td>3.8%</td>
</tr>
<tr>
<td><strong>STABLE VALUE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global Fixed Income</td>
<td>8.8%</td>
<td>10.7%</td>
</tr>
<tr>
<td>Stable Value Hedge Funds</td>
<td>6.1%</td>
<td>2.2%</td>
</tr>
<tr>
<td>Cash</td>
<td>2.4%</td>
<td>2.4%</td>
</tr>
<tr>
<td><strong>TOTAL STABLE VALUE</strong></td>
<td>6.2%</td>
<td>6.8%</td>
</tr>
<tr>
<td><strong>REAL RETURN</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gold</td>
<td>26.5%</td>
<td>26.6%</td>
</tr>
<tr>
<td>Natural Resources</td>
<td>(9.6%)</td>
<td>(5.3%)</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>3.6%</td>
<td>9.6%</td>
</tr>
<tr>
<td>Public Real Estate</td>
<td>4.5%</td>
<td>8.1%</td>
</tr>
<tr>
<td>Private Real Estate</td>
<td>8.5%</td>
<td>6.6%</td>
</tr>
<tr>
<td><strong>TOTAL REAL RETURN</strong></td>
<td>1.2%</td>
<td>3.7%</td>
</tr>
<tr>
<td><strong>TOTAL ENDOWMENTS</strong></td>
<td>4.5%</td>
<td>4.4%</td>
</tr>
</tbody>
</table>

1Sharpe Ratio is the average return earned in excess of the risk free rate per unit of volatility or total risk.
Investment Philosophy—Risk Management

Managing risk is central to the execution of any investment process and is a priority for the UTIMCO team. This is done primarily by focusing on longer-term outcomes rather than short-term results; prudent and effective diversification; a series of risk systems that monitor economic and market conditions; and professional collaboration with both the UTIMCO Board of Directors and a global network of investment organizations. Most importantly, UTIMCO maintains an organization of high character and professional investment personnel dedicated to integrity and transparency.

Figure 5
Trust Universe Comparison Service Risk vs Total Returns of Master Trusts—Foundation & Endowment

<table>
<thead>
<tr>
<th>Trust Type</th>
<th>Risk Value</th>
<th>Risk Rank</th>
<th>Return Value</th>
<th>Return Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>GEF TOTAL FUND</td>
<td>4.09</td>
<td>94</td>
<td>9.25</td>
<td>20</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>12.25</td>
<td>1</td>
<td>13.39</td>
<td>1</td>
</tr>
</tbody>
</table>

Thank you for your continued dedication to the important work that these Endowments support.

Sincerely Yours,

Britt Harris
President, CEO and Chief Investment Officer