

Annual Finance Policy Reports

*Board of Trustees Finance Committee
August 27, 2018*

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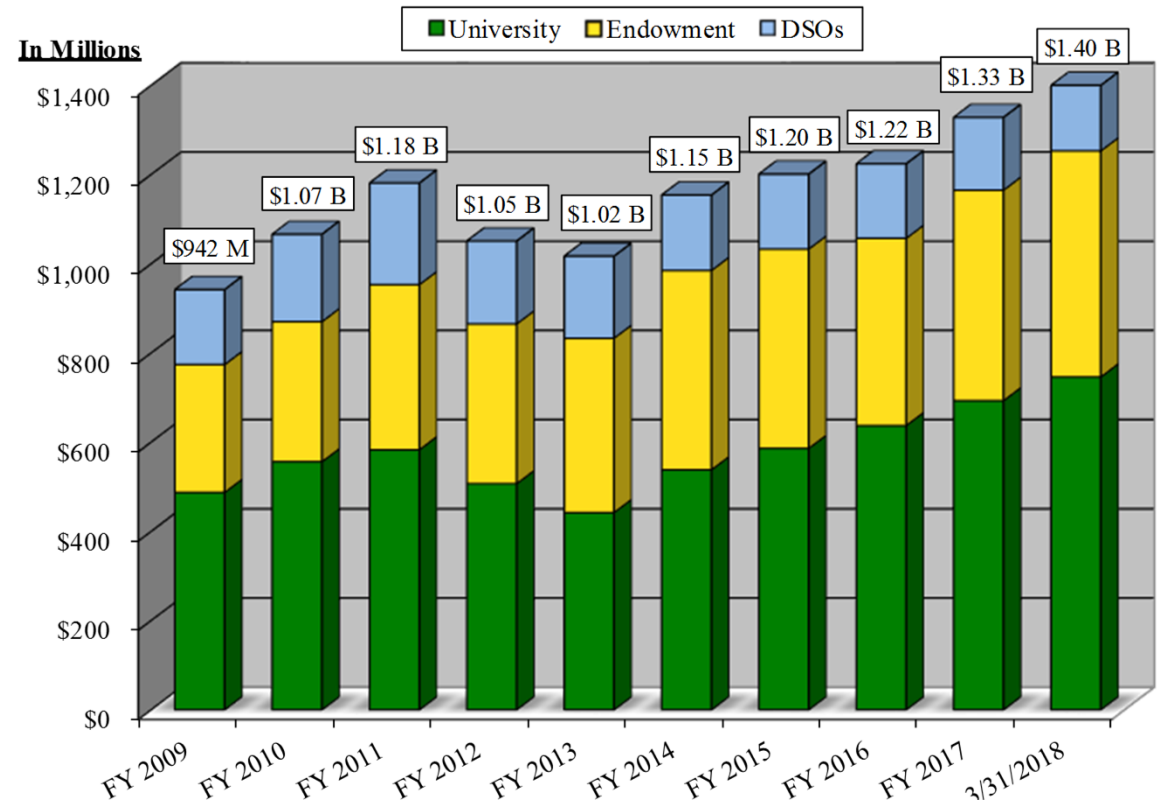
Annual Investment Report

INVESTMENT OBJECTIVE – STRENGTHEN BALANCE SHEET

- **Prudent Governance and Oversight – USF / DSO Portfolios**
 - Effective Policies, Principles, and Management Practices
 - Effective Boards / Investment Committees
 - Expert Management Teams / Investment Consultants / Investment Managers
 - Prudent Allocation of Portfolios to Asset Classes / Diversification by Investment

- **Combined USF / DSO Portfolios – \$1.4 Billion, Up \$116 Million over 2017**

All Portfolios in Compliance with BOT Investment Policy



**Asset Allocations
within Policy Limits**

USF SYSTEM INVESTMENTS – 10 PORTFOLIOS – Balances as of 3/31/18

(In Thousands)

ASSET CLASS	Combined ¹	Endowment	Operating Funds							
	USF TOTAL INVESTMENTS	FOUNDATION	UNIVERSITY	FINANCING	FOUNDATION	UMSA/MSSC	HPCC	RESEARCH	ALUMNI	SUNDOME
Cash and Equivalents (< 180 days)	\$174,955		\$96,200	\$34,923	\$27,800	\$10,700	\$1,750	\$2,800	\$205	\$772
SHORT TERM INVESTMENTS										
Fixed Income - Domestic (+ 180 days)	\$526,100		\$462,100		\$58,800	\$700		\$4,500	\$412	
TOTAL SHORT TERM INVESTMENTS	\$526,100	\$0	\$462,100	\$0	\$58,800	\$700	\$0	\$4,500	\$412	\$0
LONG TERM INVESTMENTS										
Fixed Income - Domestic	\$131,947	\$98,447	\$31,500		\$2,929	\$0		\$6,800	\$1,372	
Fixed Income - Foreign										
Equity - Domestic	\$272,461	\$182,161	\$87,000		\$5,420	\$200		\$11,900	\$2,539	
Equity - Foreign	\$190,750	\$137,350	\$50,900		\$4,087	\$1,200		\$8,000	\$1,914	
Real Assets	\$63,703	\$51,803	\$11,300		\$1,541	\$600		\$2,500	\$722	
Alternative Investments	\$44,525	\$37,725	\$6,800		\$1,122	\$0		\$1,800	\$526	
TOTAL LONG TERM INVESTMENTS	\$703,386	\$507,486	\$187,500	\$0	\$15,100	\$2,000	\$0	\$31,000	\$7,073	\$0
TOTAL CASH and INVESTMENTS as of 3/31/2018	\$1,404,441	\$507,486	\$745,800	\$34,923	\$101,700	\$13,400	\$1,750	\$38,300	\$7,690	\$772

1 FOUNDATION Operating Funds totaling \$15,100,000 invested in the ENDOWMENT Fund are eliminated in the Combined Investment balances.
 RESEARCH FOUNDATION Operating Funds totaling \$24,600,000 invested in the ENDOWMENT Fund are eliminated in the Combined Investment balances.
 ALUMNI ASSOCIATION Operating Funds totaling \$7,680,000 invested in the Foundation OPERATING and ENDOWMENT Funds are eliminated in the Combined Investment balances.

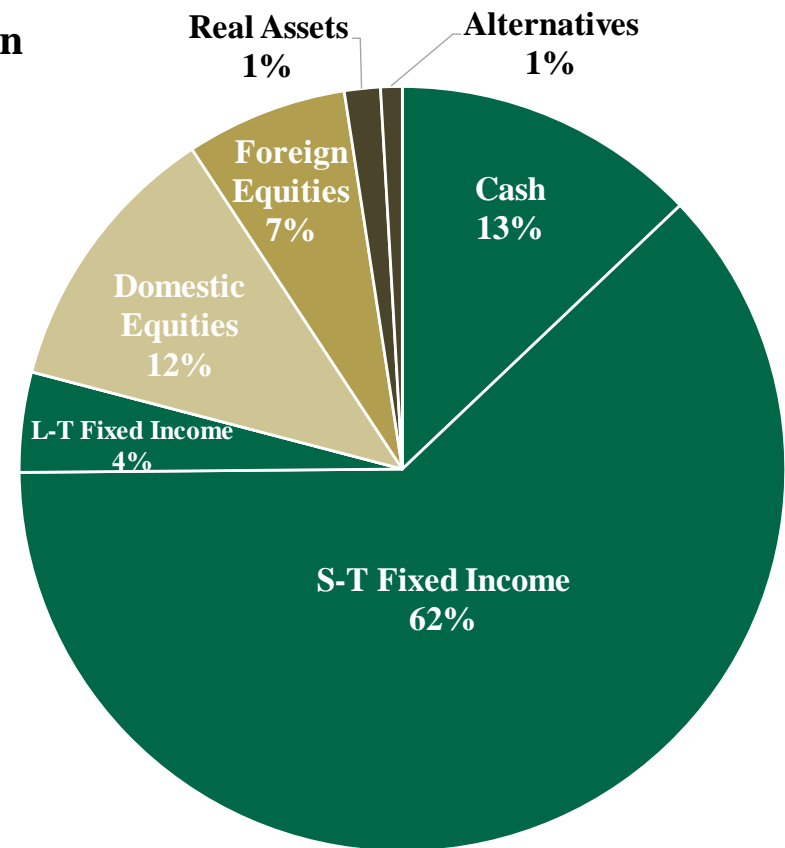
UNIVERSITY OPERATING PORTFOLIO – OBJECTIVES

- **Provide Liquidity to Fund University Operations**
 - 75% of the Portfolio is held as cash, cash equivalents, and high-quality short-term bonds
 - 25% of the Portfolio is prudently invested in risk assets with a long-term horizon

- **Preserve Capital and Provide Reasonable Returns on Invested State Funds and Reserves**
 - Focus on Diversification and Asset Allocation
 - Don't Speculate on Markets, Currencies or Interest Rates

- **Achieve Positive Absolute Return in All Market Conditions – Balance Risk and Return**
 - 0.13% Weighted Average Expense Ratio Due to Primary Use of Low-Cost Passive Index Funds

- **Provide Support for Moody's and Standard & Poor's Ratings**
 - Liquidity and Reserves



UNIVERSITY OPERATING PORTFOLIO – FY 2018 PERFORMANCE

As of June 30, 2018

Asset Class	Market Value	1-Yr	3-Yr	5-Yr	Since Inception
Total Assets	\$760.8 M	2.4%	2.3%	2.5%	2.9%
Total Assets Benchmark		2.5%	2.3%	2.5%	2.6%
Value Add		(0.1%)	0.0%	0.0%	0.3%
Total Assets ex Cash	\$652.9 M	2.6%	2.7%	3.1%	3.5%
Total Long-Term Pool	\$157.9 M	9.0%	6.7%	7.5%	7.7%
Long-Term Benchmark		9.3%	6.7%	7.7%	6.6%
Value Add		(0.3%)	0.0%	(0.2%)	1.1%
Domestic Equity	\$89.9 M	14.3%	12.1%	12.9%	15.9%
International Equity	\$33.3 M	5.9%	5.2%	6.7%	6.2%
Emerging Markets	\$15.7 M	6.3%	3.6%	3.5%	3.0%
Real Assets	\$12.8 M	14.6%	4.3%	3.5%	2.6%
Alternatives	\$6.2 M	1.7%	1.5%	3.3%	4.8%
Total Intermediate Pool	\$495.0 M	0.0%	1.3%	1.6%	2.5%
Intermediate Benchmark		(0.2%)	0.8%	1.1%	2.1%
Value Add		0.2%	0.5%	0.5%	0.4%
Fixed Income - Government	\$163.2 M	(0.2%)	0.8%	1.1%	2.0%
Fixed Income - Corporate	\$331.8 M	0.1%	1.6%	1.9%	2.6%
Cash and Equivalents	\$107.9 M	1.0%	0.6%	0.4%	0.5%

UNIVERSITY OPERATING PORTFOLIO – 10-YEAR MANAGEMENT

- **University Investment Returns have been Stable and Positive in Each of the Past 10 Years, Despite Market Volatility.**
- **University Approved 20 New Investment Managers and Terminated 8 in the Past 10 Years**
 - New Investment Managers: Recommended by Consultant and Investment Committee; Due Diligence by Management
 - Termination Criteria: Underperformance and/or Organizational Issues

5-Year Risk Adjusted Returns			
	<u>Return</u>	<u>Std Dev</u>	<u>Sharpe</u>
▪ USF Portfolio –	2.4%	2.0%	1.05%
▪ S&P 500 Index –	13.4%	9.8%	1.30%
▪ Barclay’s Agg –	2.3%	2.7%	0.69%

12-Month Performance	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018 (Preliminary)
<u>UNIVERSITY PORTFOLIO</u>										
Annual Investment Income (Loss)	\$23 M	\$27 M	\$21 M	\$10 M	\$14 M	\$27 M	\$6 M	\$10 M	\$25 M	\$18 M

Annualized Return - Equities	4.7%	4.3%	19.1%	(4.7%)	13.1%	18.3%	(0.1%)	(2.6%)	14.5%	9.0%
Annualized Return - Fixed Income	5.7%	9.7%	2.4%	2.3%	0.8%	1.1%	0.9%	2.4%	0.9%	0.0%
Total Annualized Return	4.8%	4.8%	3.3%	1.6%	2.7%	2.1%	0.7%	1.1%	3.5%	2.4%

UNIVERSITY OPERATING PORTFOLIO – NEAR-TERM INITIATIVES

- **Ongoing Assessment of Portfolio Exposure to Interest Rate Risk – Well Positioned in Short-Term, High Quality Fixed Income**
- **Maintain Liquidity in Diversified, Well-Managed Mutual Funds – Next Day Availability**
- **Continue Investment of Positive Net Cash Flow Into Balanced Portfolio Structure**
- **Monitor Investment Managers for Performance and/or Organizational Issues**

Annual Debt Management Report

DEBT MANAGEMENT OBJECTIVE – STRENGTHEN BALANCE SHEET

- **Prudent Governance – USF / USF Financing Corporation**

- Effective Policies and Management Practices
- Effective Boards
- Expert Management Teams

**Active Management:
Recent Example – Reduction
in Corporate Tax Rate**

Managing Compliance with USF BOT Debt Management Policy, BOG Regulations, State Statute, Federal SEC / IRS Laws, Covenant Requirements, Continuing Disclosure Requirements.

- **Maintain Strong Moody’s and Standard & Poor’s Credit Ratings**

- Access Capital on Attractive Terms

- **Effective Use of USF Debt Capacity**

- Strategic Prioritization of Projects
- Determination of Direct Debt or Public Private Partnerships

- **Manage Long-Term Cost of Capital and Risk**

- Capitalize on Market Opportunities to Achieve Low Cost, Low Risk, Long-Term Financing

UNIVERSITY DEBT PORTFOLIO – FY 2018

- **Transactions Closed in FY 2018 – \$229 Million**
 - \$59 M Series 2012B Housing Direct Placement Bonds – Extended Maturing Credit Facility
 - \$18 M Series 2013B Health Bonds Converted – Variable to Fixed Rate; Swap Expired 7/1/18
 - \$152 M – 8 Series of Housing, Health, Athletic and Research Bonds Amended to:
 - Eliminate Subjective Acceleration Clauses and Other Bank-Favorable Covenants; and
 - Reduce the Effect of the Reduction in Corporate Tax Rate to 21%

As of June 30, 2018

Program	Current Ratings Moody's / S&P	Debt Structure			Interest Rate	Total Outstanding
		Public / Private	Fixed / Variable	Taxable / Tax Exempt		
Parking	Aa3 / AA-	Public	Fixed Rate	Tax Exempt	2.20%	\$17.5 M
Housing	A1 / A+	Public / Private	Fixed / Variable w/ Swap	Tax Exempt	3.98%	\$179.5 M
Health	Not Rated	Private	Fixed Rate	Tax Exempt	3.07%	\$70.5 M
Athletics	Not Rated	Private	Fixed Rate	Taxable / Tax Exempt	4.08%	\$40.3 M
Marshall Center	Aa3 / AA-	Public	Fixed Rate	Tax Exempt	3.43%	\$32.5 M
Research	Not Rated	Private	Fixed / Variable w/ Swap	Taxable / Tax Exempt	4.05%	\$18.9 M
TOTAL USF & DSO DEBT		53% Private 47% Public	83% Fixed Rate 17% Variable w/ Swap	90% Tax Exempt 10% Taxable	3.68%	\$359.2 M

UNIVERSITY DEBT PORTFOLIO – 10-YEAR MANAGEMENT

- **10 Ratings Upgrades (plus recent *Positive Outlook* on all rated series by S&P)**

- **45+ Transactions Closed Over 13 Years – Exceeds \$1.8 Billion**
 - Issued only \$82 M of New Debt Over 10 Years
 - Total Debt at 6/30/18 – \$359M, Down from Peak of \$454 M in 2011
 - Low Cost of Capital – 3.68%, Down from Peak of 4.28% in 2014
 - NPV Savings on Refundings / Conversions – +\$25 M

- **Debt Structure Managed to Reduce Risk and/or Capitalize on Market Opportunities**
 - Mix of Debt – Private (53%), Public (47%) – Changed from 100% Public Debt in 2009
 - Variable Rate Debt – 17% of Total Debt, Down from Peak of 65% in 2009
 - Interest Rate Swaps – \$62M, Down from Peak of \$278 M in 2008

**Managed Debt Consistent with Market
Trends. Create Opportunities for USF.**

USF POLICY PERFORMANCE MEASURES – 10 Year Trend

(In Millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	Moody's Aa2 Medians FY 2017
NEW DEBT		\$10	\$52			\$20					
TOTAL DEBT	\$445	\$415	\$454	\$445	\$431	\$435	\$421	\$413	\$377	\$359	\$991
LONG-TERM RATE	3.93%	3.96%	4.01%	4.00%	4.13%	4.28%	3.99%	3.91%	3.64%	3.68%	

POLICY MEASURES	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	Moody's Aa2 Medians FY 2017
<u>OPERATIONS</u>											
Operating Cash Flow Margin (↑)	11.3%	7.1%	6.5%	1.1%	3.9%	10.2%	7.4%	7.3%	9.1%		11.4%
Operating Margin (↑)	5.1%	0.6%	0.3%	-6.9%	-4.7%	2.4%	0.1%	0.0%	2.0%		2.6%
<u>LIQUIDITY</u>											
Cash & Investments / Operating Exp (↑)	0.67x	0.72x	0.77x	0.62x	0.58x	0.65x	0.64x	0.64x	0.67x		0.68x
Monthly Days Cash on Hand (↑)	177 days	195 days	204 days	173 days	167 days	202 days	197 days	200 days	213 days		164 days
<u>LEVERAGE</u>											
Cash & Investments / Debt (↑)	1.3x	1.6x	1.7x	1.5x	1.4x	1.6x	1.8x	1.9x	2.3x		1.2x
Debt Service Coverage (↑)	5.2x	3.8x	3.3x	-0.1x	1.1x	4.0x	2.7x	4.1x	4.8x		3.1x
Debt Service / Operating Exp (↓)	2.1%	1.9%	2.0%	2.0%	2.2%	2.2%	2.2%	1.5%	1.7%		4.2%

UNIVERSITY DEBT PORTFOLIO – NEAR-TERM INITIATIVES

- **USF St. Petersburg Housing and Dining Project – \$33 M**
 - Meets the BOT-Required 1.30x Debt Service Coverage (exceeds BOG 1.20x Requirement)
 - Approved by DSO and BOT
 - Scheduled for Approval by BOG in November

- **USF Research Park Building – TBD; in Development**

- **USF Sarasota-Manatee Student Housing Project – TBD; in Development**

Annual Derivatives Report

DERIVATIVES POLICY – STRENGTHEN BALANCE SHEET

- **Prudent Governance – USF / USF Financing Corporation**
 - Effective Policies and Management Practices

- **Manage Long-Term Cost of Capital and Risk**
 - Hedged Variable Rate Bonds – Provides a Lower Cost of Capital – Requires Active Management
 - Matched Maturities of Bonds to Coincide with Maturing Swaps
 - \$179 M reduction in swaps over 4 years
 - Winding Down Swap Portfolio – No New Swaps Since 2007
 - 2 Swaps Currently Outstanding – \$62 M
 - 1 Swap will Expire in December 2019

As of July 1, 2018

Program	Swap Counterparty	Expiration Date	USF Optional Termination Rights	Collateral Posted	Fixed Swap Rate	Total Outstanding
Housing	Royal Bank of Canada	7/1/2037	Yes	\$0	3.94%	\$60 M
Research	Bank of America	12/1/2019	Yes	\$0	5.70%	\$2 M
TOTAL USF DSO SWAPS				\$0	4.00%	\$62 M

USF SYSTEM DERIVATIVES PORTFOLIO – 10-Year Management

- USF System Derivatives – \$62 Million (7/1/18)

Market is Not Favorable to Swaps – Looking to Exit Remaining Swap

Outstanding Derivatives - DSO Issued

