
Endowment Fund Overview

Natural Resources Interim
Committee

August 30, 2011



Trust Assets Overseen by the Investment Board

Funds Under Management *As of June 2011*

	<u>Assets</u> <u>(\$millions)</u>	<u>% of</u> <u>Total</u>
Endowment Fund	1,267.8	66%
State Insurance Fund	574.7	30%
Judges' Retirement Fund	62.9	3%
Parks & Rec Endowments	<u>3.4</u>	<u>0.2%</u>
TOTAL	<u><u>1,908.8</u></u>	<u><u>100%</u></u>

Mission

Endowment Fund Investment Board

Provide professional investment management services to our stakeholders consistent with our constitutional and statutory mandates.

Who is the Endowment Fund Investment Board?

- Nine members, appointed by the Governor, confirmed by the Senate
 - One Senator, one representative
 - One professional educator
 - Six members of the public familiar with financial matters
- Meets at least quarterly
- Full-time staff of four

Basic guidelines for fund management are in the Land Board's Asset Management Plan



Idaho State
Board of Land Commissioners

State Trust Lands
Asset Management Plan

December 20, 2007

Fund Investment Management

Philosophy (page 1)

As perpetual funds, per state Constitution and statute, the endowment funds have a long-term investment horizon. All of the portfolios managed by the EFIB are subject to the variability of the financial markets and to the threat of eroding purchasing power due to inflation. The EFIB will mitigate some of the market risk by investing in diversified portfolios of assets so that the expected variation in the whole portfolio is less than the sum of the variations of each part.

Fund Investment Management Philosophy (page 2)

With a citizen board and small staff, the EFIB will make strategic allocations and generally avoid making tactical calls, maintaining an asset mix that is expected to have reasonable performance over a market cycle. The asset mix of the fund takes into account the entire endowment portfolio – i.e. the fact that the revenues of the endowment lands, net of IDL expenses, will be contributed to the endowment funds.

Five Elements of Fund Diversification

- 1. Risk of return: equity vs. fixed income**
 - *Endowment: 70% stocks, 30% bonds*
- 2. Region: U.S. vs. International**
 - *Endowment: 79% U.S., 21% International (Equity 70%/30%)*
- 3. Investment Style: Value vs. Growth**
 - *Endowment: Evenly balanced*
- 4. Size: Large, medium and small companies**
 - *Endowment: Slight overweight to mid-size*
- 5. Active vs. Passive security and industry selection**
 - *Endowment: Passive for 100% of bonds, 14% of equities*

Elements 1 thru 5 correspond with the numbers in boxes on the fund map on the next page

Endowment Fund Asset Diversification Map

Region ²	Size ⁴	Investment Style ³			Total	Return Risk ¹
		Value	Core	Growth		
S C	Large Cap	10%	10% 4%	10%	35%	S t o c k s
	Mid Cap	5%		5%	9%	
	Small Cap	3%		3%	5%	
	International	7%	7%	7%	21%	B o n d s
S C	Bonds		26% 5%		30%	
		<i>Infl. Index</i>				
	<i>Total</i>	24%	51%	24%	100%	

⁵ Active or Passive (securities, sectors)

Passive/index approach (remainder take an active approach to securities and sectors within their area of expertise)

Totals may not add due to rounding

Expected Return

	<u><i>Return</i></u>	<u><i>Mix</i></u>
Equities	8.1%	70%
Bonds	3.7%	30%
Total	<u>7.2%</u>	<u>100%</u>

Returns are before investment management and EFIB oversight fees of approximately 0.4% and assume no gain or loss from active management vs. the index

Source: EFIB estimates, Callan Associates (1/11)

Allocation of Expected Return

Expected gross index return*	7.2%
Gain from active management	?
Investment management costs	0.4%
Expected net return	<u>6.8%</u>
Retain in corpus for inflation	2.8%
Expected real net return	<u>4.0%</u>

*As of 1/11

Returns over the last ten years are well below long-term, 30-year expectations

Expected Return Variation

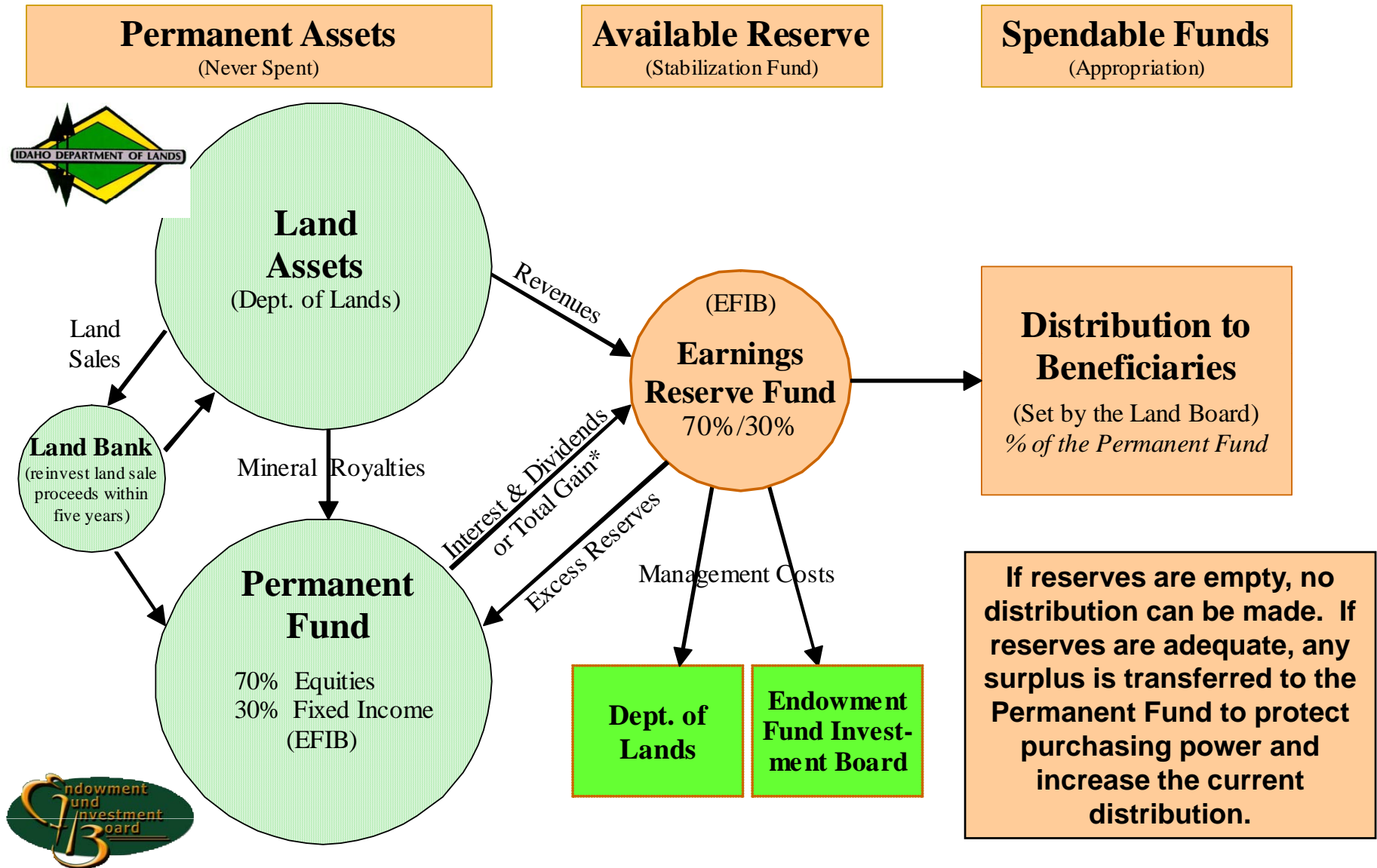
<u>Probability</u>	<u>Annual Return Over</u>	
	<u>3 Years</u>	<u>7 Years</u>
	Of returns greater than:	
10%	17.6%	14.1%
25%	12.6%	10.7%
50%	7.2%	7.2%
	Of returns less than:	
25%	2.1%	3.8%
10%	-2.5%	0.8%

Returns are before investment management and EFIB oversight fees of approximately 0.4% and assume no gain or loss from active management vs. the index

Source: EFIB estimates, Callan Associates (1/11)

Potential variation is large, but declines over time

STRUCTURE OF IDAHO'S ENDOWMENT ASSETS

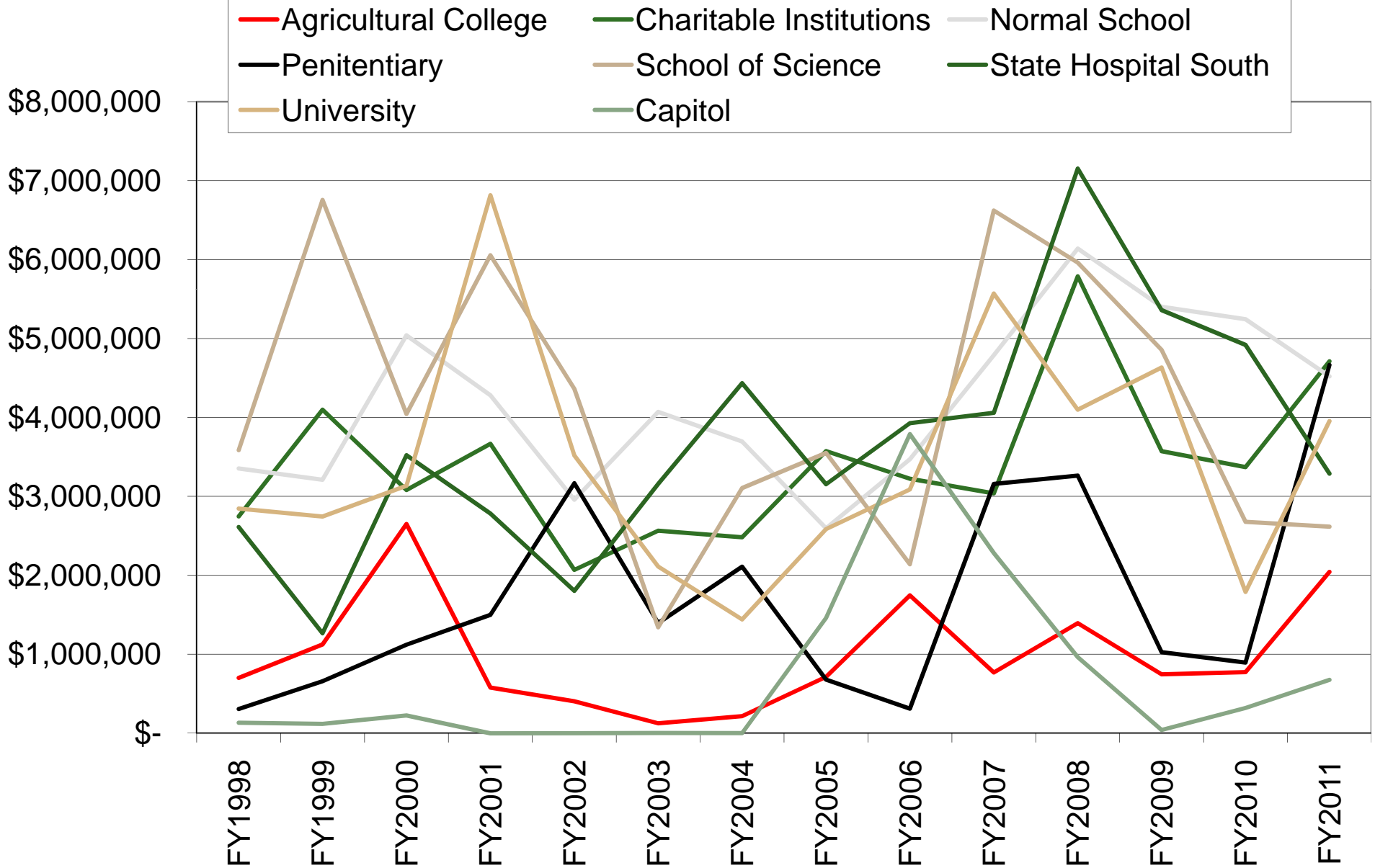


* When the Permanent Fund, adjusted for inflation, exceeds its June 2000 level, only total gain over inflation will be distributed to Earnings Reserve.

There are nine different land grant endowments



Revenue Volatility – Small Endowments



Volatility of Land Revenues 2001-2011

	<i>Average Annual Revenues (\$ million)</i>	<i>11-Year Standard Deviation (% of Ave.)</i>
Public School	37.8	15%
Normal School	4.1	23%
Charitable Institutions	3.4	29%
State Hospital South	4.0	32%
University of Idaho	3.6	40%
School of Science	3.9	41%
Penitentiary	2.0	66%
Agricultural College	0.9	69%
	<hr/> 59.7 <hr/>	<hr/> 13% <hr/>

2/3^{rds} of the time, land revenues will be within plus or minus this percent of the average – 1/3rd of the time, revenues will vary outside this range

Smaller endowments have more variation

Objectives for determining distributions (in priority order)

1. Avoid reductions in total endowment distributions
2. Maintain adequate Earnings Reserves to protect distributions from temporary income shortfalls
3. Grow distributions and permanent corpus faster than inflation and population growth

Endowment Distributions

- Current distributions are 4-5% of each endowment fund
- These rates are based on:
 - Expected sustainable income
 - From the fund
 - From the land
 - Expected rate of inflation
 - Expected growth in population
 - Adequacy of Earnings Reserve

Endowment Distributions

FY 2012 and FY 2013

Endowment Beneficiary	FY 2012 Approp.	Change	FY 2013 Approv. Dist.	% Change
Public Schools	31,292	-	31,292	0.0%
All University Endowments	\$ 9,616	\$ 311	\$ 9,927	3.2%
State Hospital South	2,302	566	2,868	24.6%
Penitentiary	1,040	206	1,247	19.8%
Juvenile Corrections	790	0	791	0.0%
State Hospital North	790	0	791	0.0%
Veterans Home	494	0	494	0.0%
School for the Deaf and Blind	99	0	99	0.0%
Grand Total	46,424	1,084	47,509	2.3%

All amounts in thousands of dollars

Conclusions -- Endowment Investments and Distributions

- In support of each endowment's goal of providing perpetual distributions to its beneficiaries, the EFIB manages a diversified portfolio of securities to obtain a reasonable long-term rate of return
- Today's distributions must be balanced with the need to retain funds for future beneficiaries
- The amount of distributions is driven by both the expected level and the expected volatility of both fund returns and land revenues
- Efforts to improve fund and land returns and reduce their volatility will result in higher distributions

Appendix

Idaho Land Grant Endowment Fund Assets

(Amounts in millions)

	<i>Fiscal Year End</i>				
	<u>1966</u>	<u>2000*</u>	<u>2011</u>		
			<u>Total</u>	<u>Permanent Fund**</u>	<u>Earnings Reserve**</u>
Public School	45.7	556.0	808.2	714.7	93.5
Agricultural College	2.6	14.8	25.9	20.2	5.7
Charitable Institutions	4.4	54.5	83.4	68.6	14.8
Normal School	4.2	47.3	76.1	62.8	13.4
Penitentiary	2.6	18.3	34.8	28.6	6.2
School of Science	4.3	54.8	85.1	70.1	15.0
State Hospital South	2.0	23.4	60.2	45.9	14.3
University	3.2	42.4	72.2	59.4	12.8
	69.0	811.5	1,245.9	1,070.2	175.6
Capitol Permanent***	<i>not avail.</i>	<i>not avail.</i>	21.9	<i>not applicable</i>	

* Excludes approximately \$25 million of endowment-related funds held by the IDL which were transferred to the EFIB in July 2000 to become the beginning balance of Earnings Reserves.

** Reflects \$28.6 million of approved transfers from Reserves to Permanent effective 9/1/2011.

*** The Capitol Permanent Fund was managed separately from the other endowments until 2004.

Endowment Fund Investment Board members

Dean Buffington

**Partner,
investment firm,
attorney**



Gavin Gee

**Director, Dept.
of Finance,
attorney**

Max Black

**Retired
insurance
agent,
legislator**



Endowment Fund Investment Board members (page 2)

Vaughn Heinrich

**Retired Supt. Of
Vallivue School
District**



**Tom
Kealey**

**Business-
man, inves-
tor, former
MK CFO**

**Sue
Simmons**

**Dept. of Labor
Project
Manager, CPA**



Endowment Fund Investment Board members (page 3)

**Richelle
Sugiyama**

**Investment
Officer, PERSI**



**John
Taylor**

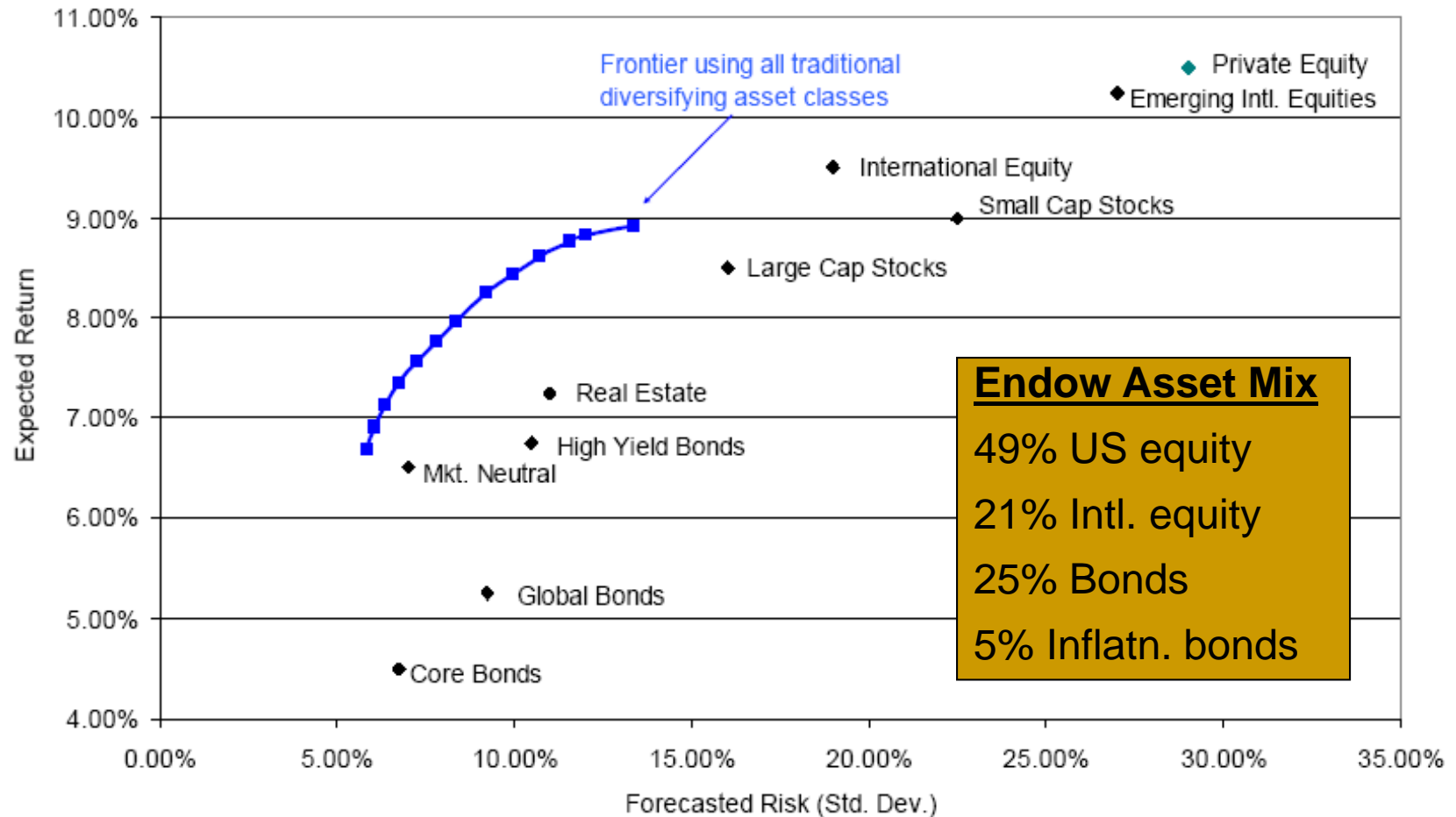
**Insurance
company
executive**

**Chuck
Winder**

**Senator, real
estate broker**



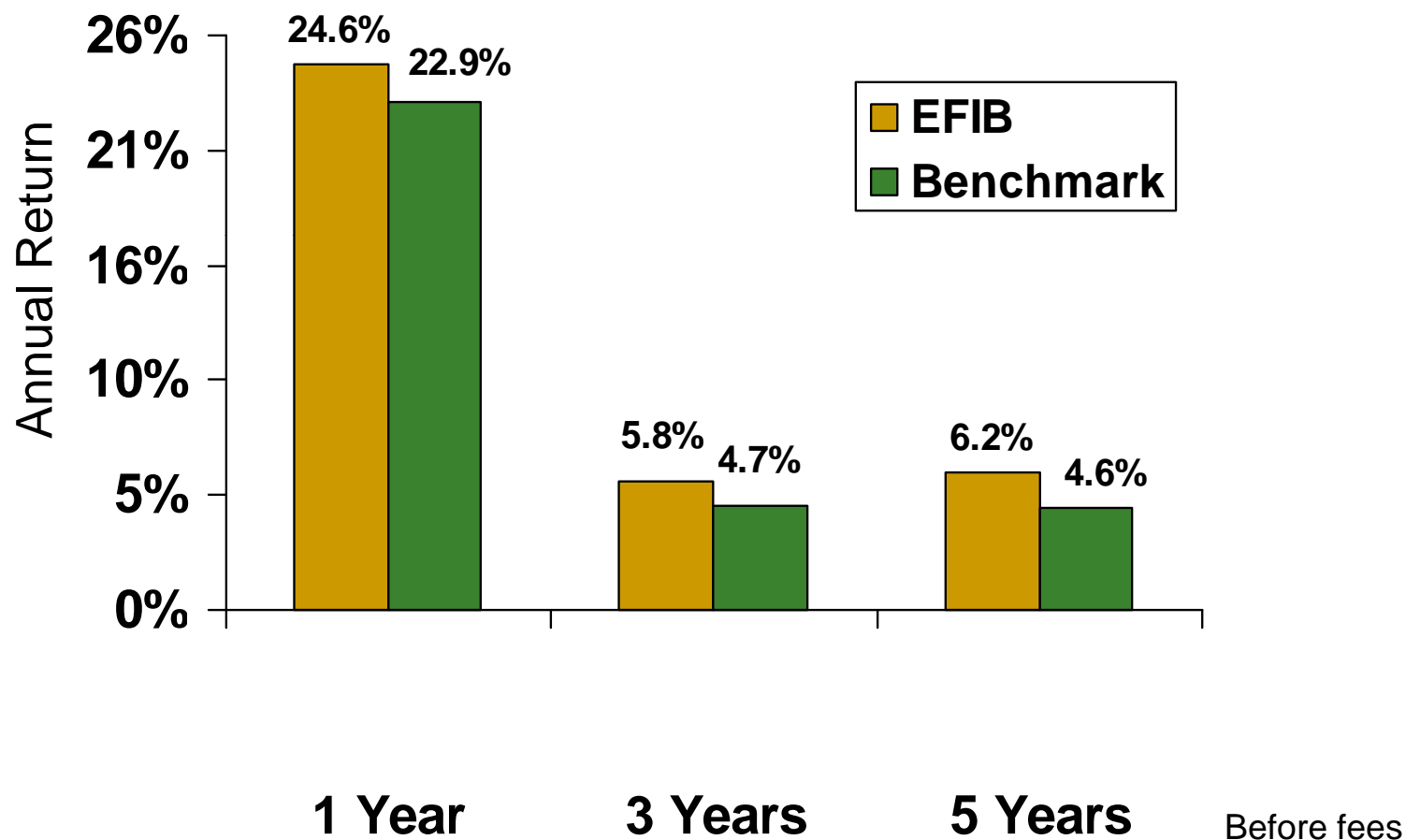
Efficient Frontier



A diversified mix has better risk/return

Endowment Fund Performance

(For periods ended June, 2011)



Relative performance at 6/11 was 17th percentile for 1 year, 9th for 5 years

Vs. Callan Public Funds

Beneficiaries, Endowments, Budget Responsibility

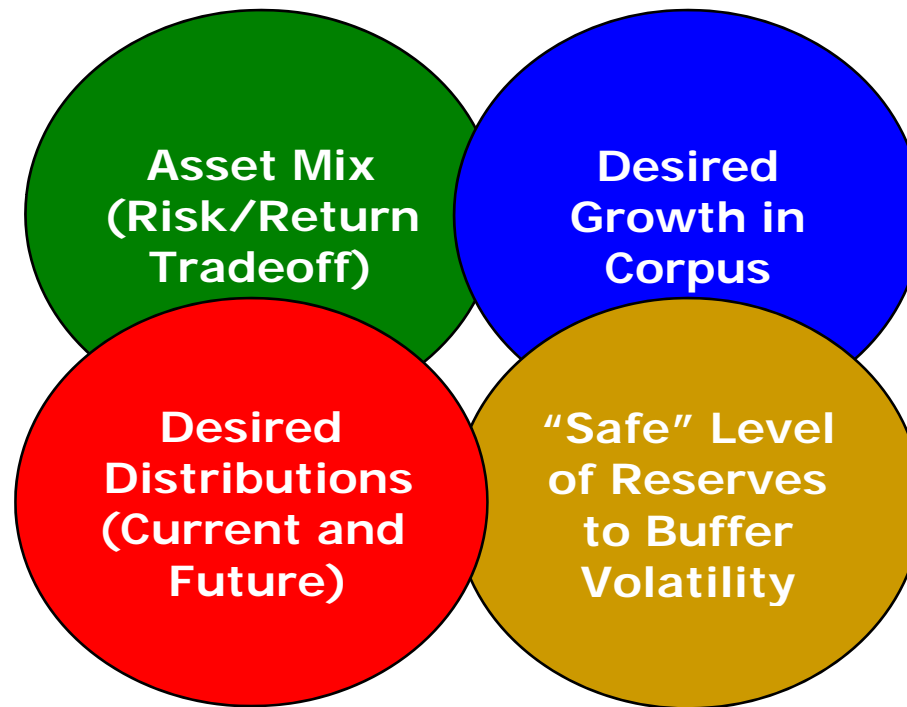
Idaho Land Grant Endowments

<i>Fourteen Legal Beneficiaries</i>	<i>Nine Endowment Funds</i>	<i>Nine Areas Of Budgetary Responsibility</i>
Public Schools	<i>Public School</i>	Public Schools
U of I Agricultural College	<i>Agricultural College</i>	} Higher Education
U of I School of Science	<i>School of Science</i>	
University of Idaho	<i>University</i>	
ISU Education Department	} <i>Normal School</i>	
Lewis-Clark State		
Idaho State University	} <i>Charitable Institutions</i>	Juvenile Corrections Center
Juvenile Corrections Center		State Hospital North
State Hospital North		Veterans Home
Veterans Home		School for the Deaf and Blind
School for the Deaf and Blind		<i>State Hospital South</i>
State Hospital South	<i>Penitentiary</i>	Penitentiary
Penitentiary	<i>Capitol Permanent</i>	Capitol Commission
Capitol Commission		

Fiduciary tradeoffs make defining and managing Distribution Policy challenging

Evaluate the interaction of four policy drivers in order to balance asset mix, current & future distributions, and levels of reserves

- Higher long-term return means more potential short-term volatility
- How much downside variation can the fund endure?



- How fast should the fund grow over time? With inflation? Faster than inflation?
- How much risk of a cut in distributions should beneficiaries face?

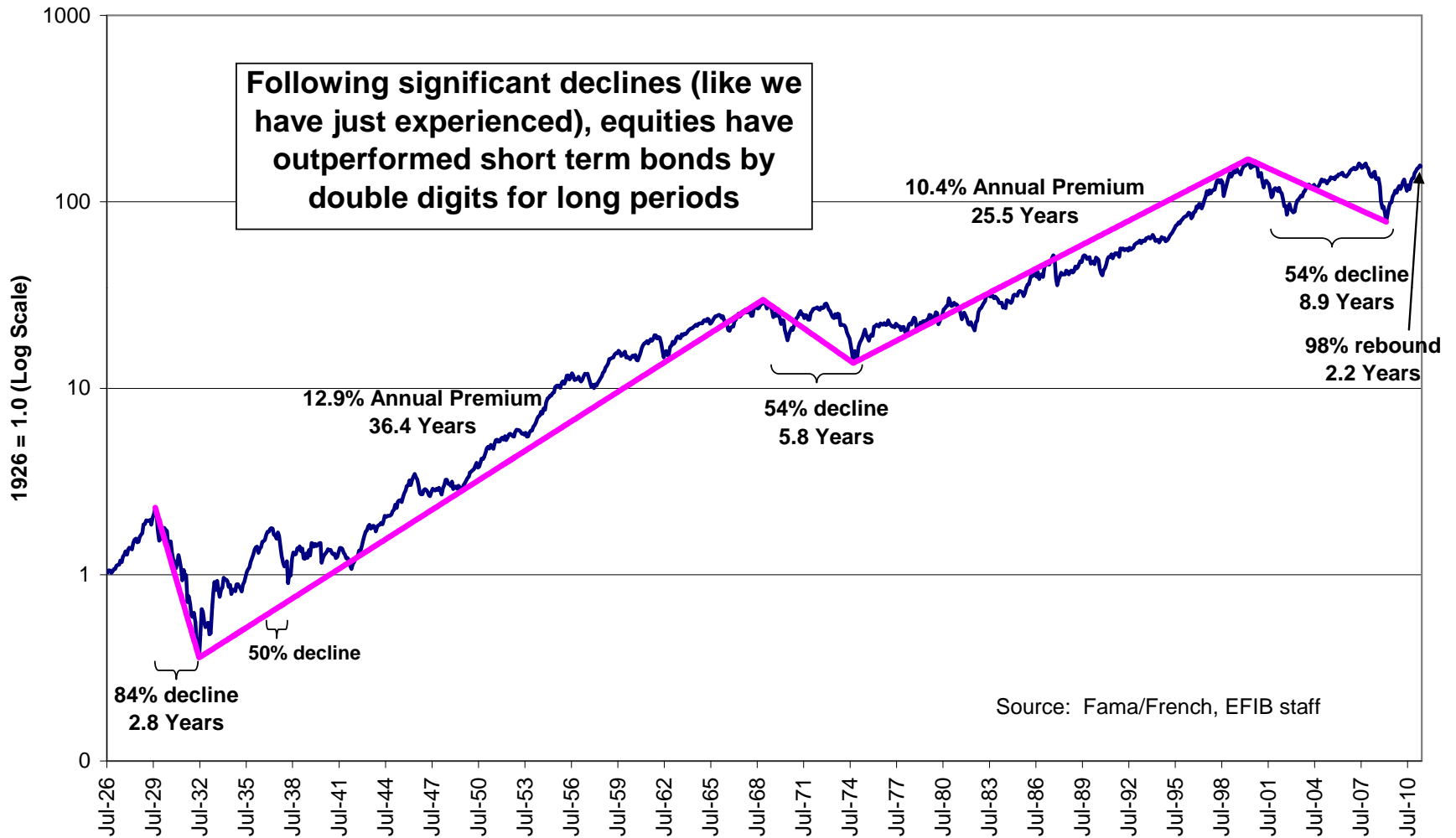
- What rate is sustainable?
- Spend a lot, save a little or spend little now and more later

These tradeoffs must be determined by the Land Board within limits prescribed by state statute, the state constitution, and federal statutes

Cumulative Equity Risk Premium

U.S. Equity Return Minus One Month T-Bill Rate

1926 Thru May 2011



Cumulative Equity Risk Premium

U.S. Equity Return Minus One Month T-Bill Rate
7, 15 and 30-Year Rolling Periods Thru May 2011

