Fiscal Year 2013 Highlights

Miami’s investment portfolios produced solid results for the fiscal year ended June 30, 2013. The combined university and foundation managed pool posted a gain of 11.20 percent, a notable improvement over the previous year’s decline of 3.27 percent. Meanwhile, the non-endowment pool produced a return of 3.47 percent after earning 1.86 percent in the previous year.

Investment Pools

As of June 30, 2013, total investments held by Miami University and the Miami University Foundation approached $800 million, up from just shy of $700 million at the previous year-end. This increase is attributable to improved University operating cash flow, sound investment performance, and sustained giving levels.

The Miami University Foundation’s investment committee provides governance oversight to one unified endowment investment pool for the University and Foundation, while the University maintains oversight of the non-endowment pool. The fiscal year-end asset values among the pools are as follows:

<table>
<thead>
<tr>
<th>Pool</th>
<th>Type of Funds</th>
<th>Invested as of June 30, 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>University non-endowment</td>
<td>Working capital and cash reserves to support operating activities</td>
<td>$349,486,000</td>
</tr>
<tr>
<td>University endowment &amp; foundation</td>
<td>Funds donated to the university and the foundation to establish endowments in perpetuity</td>
<td>$416,658,000</td>
</tr>
<tr>
<td>Trusts, annuities, and separately invested assets</td>
<td>Gifts managed independently of the pooled funds</td>
<td>$25,124,000</td>
</tr>
<tr>
<td>Total Investments</td>
<td></td>
<td>$791,268,000</td>
</tr>
</tbody>
</table>

The university non-endowment pool holds the working capital and cash reserves that fund the university’s operating activities. Its balance fluctuates significantly during the course of a year based on the university’s cash flow cycle of receipts and expenditures. June 30 typically marks the low point of this annual cycle.

The combined endowment pool invests endowed gifts from donors. The pool operates under the philosophy that the funds are invested in perpetuity to provide benefits to today’s students as well as to the many generations of Miami students yet to come. Miami invests the funds with the confidence that economic cycles will rise and fall but that a well diversified portfolio will provide the long-term growth necessary to preserve the value of the endowment across the generations. The investment policy governing the endowment pool recognizes that the portfolio can tolerate year-to-year fluctuations in return because of its infinite time horizon, and looks beyond short-term fluctuations toward an investment philosophy that provides the best total return over very long time periods.

The university and foundation also hold assets given by donors in the form of trusts, annuities, insurance policies, and similar assets. These funds are managed separately from the endowment pool.

Over the last decade, the value of the combined endowment pools has increased by 71 percent through a combination of generous support from our donors and solid investment earnings. We appreciate the enduring generosity of our alumni and friends, along with the dedicated leadership of our investment committee, as we continue to navigate the extraordinary challenges present throughout the global capital markets.
**Asset Allocation**

The non-endowment pool has three components. Operating cash represents the University's working capital and is invested in short-term cash equivalents, with a target balance of two to six months of average cash needs. Core cash represents short-term reserves and is invested in high quality short-term and intermediate-term fixed income investments, also with the target balance of two to six months of average cash needs. Long-term capital consists of longer-term reserves and represents the remainder of the pool. It is invested in a mix of longer maturity bonds and absolute return hedged strategies.

During the year, cash flow generation was again very strong due to sustained improvements in University operating efficiency. This growth in cash continues to present a major challenge, however, as short-term interest rates enter their fifth year near zero. Several rebalancing actions were taken during the year to reduce operating cash balances in order to increase the pool's earnings potential. The result was one new strategy in core cash, three new strategies in the long-term capital portion, and one liquidated absolute return manager. These moves shifted the allocations lower in operating cash (from 21 percent to 14 percent) and higher in the other two categories versus last year. The potential for increases in interest rates have prompted a bias toward absolute return strategies versus traditional bond strategies.

The endowment pool’s primary asset allocation strategy uses three asset categories: equity, debt, and real assets. Within each category, we can gain exposure through three types of strategies: long-only public, hedged, or private. We employ managers that have broad, unconstrained mandates, allowing them great flexibility to pursue opportunities. Most of our managers have a global mandate.

At fiscal year-end, total equity related strategies represented about 53 percent of the combined portfolio, down by about six percentage points during the year, but with the dollar amount nearly the same as last year. This decline represents reduced exposure to both hedged equity and public equity strategies. Elsewhere, hedged debt strategies increased by nearly three percentage points and public real assets exposure nearly doubled. The investment committee slightly adjusted
the strategic asset allocation policy ranges by increasing the upper limits on public, hedged, and total debt exposure and lowering the minimums for public and total equity. Over the last few years, the asset allocation has evolved to reflect a shift away from the highly volatile public equity space and toward various credit and real asset strategies.

Another way we consider the endowment’s asset allocation is through geographic diversity. The portfolio emphasizes managers that invest globally, usually allowing the manager to determine the best places in the world to allocate our capital. The concept of geography is often difficult to quantify, since a company we invest in might be domiciled in one country, trade in another, derive its current revenue globally, and perceive its future earnings growth to be in places it does not yet conduct business. The following chart depicts the total endowment’s exposure over the last few years by broad geographic region.

The third measure of the endowment’s asset allocation is liquidity, or how quickly the exposure to a particular manager can be redeemed and turned into cash. Approximately 32% of the portfolio could be converted to cash within seven days, while about 23% is in various limited partnerships that are considered to be illiquid.

Miami treats each investment manager relationship like a partnership and, along with its external advisors, expends considerable effort on the due diligence process. The investment consultants focus on manager research, including back office due diligence, and conduct regular statistical reviews to examine the role each manager is playing in the portfolio. Staff has regular quarterly conversations with each manager to understand their strategic thinking and to monitor their activities. Ongoing oversight activities include making manager site visits, attending investor conferences, reading trade publications, tracking government filings, and monitoring the managers’ service providers.

In total, the endowment employs 24 external managers, some with multiple mandates. During the year, new relationships were established with two global credit managers, a global public equity manager, and a global public real assets manager. Two long/short equity managers and a global long only equity manager were terminated. In addition, the exposure levels to several managers were adjusted.

**Investment Returns**

The university’s non-endowment pool earned 3.47 percent for the fiscal year ended June 30, 2013. Annualized performance for the trailing ten years was 3.30 percent, providing annualized added return versus the 90-day Treasury bill over that period of 1.7 percentage points. The recent results were achieved in spite of sustained near zero short-term interest rates that significantly limit the earnings potential of the majority of this pool. The absolute return strategies in the long-term capital portion of the pool produced returns in excess of 11.3 percent for the year.

The endowment pools earned 11.20 percent for the fiscal year, rebounding from the negative return from the previous fiscal year. Three of the last four fiscal years and seven of the last ten have realized positive double digit returns. Annualized performance for the trailing ten years was 7.47 percent. All investment strategies reported positive returns for the year, with public real assets setting the pace with returns of nearly 35 percent.
Program Support

Endowments provide a lasting legacy for Miami because their principal is invested in perpetuity, and an annual distribution is made to support a variety of activities of the university. The spending policies of the university and foundation are intended to achieve a balance between the need to preserve the purchasing power of the endowment principal in perpetuity and the need to maximize the current distribution of endowment earnings. Fulfilling these dual objectives is often referred to as achieving “intergenerational equity,” in which no generation of college students is advantaged or disadvantaged in relation to other generations.

The formula under which spending distributions are calculated is a blend of two elements: an inflation component (70 percent of the formula) that increases the prior year’s distribution by the rate of inflation, and a market factor (30 percent of the formula) that ties the distribution to the market value of the investments. This formula was adopted in fiscal year 2004 and is intended to reduce volatility caused by various market conditions, while maintaining intergenerational equity and preserving the purchasing power of the endowed principal.

The combined distribution for fiscal year 2013 was about $17.8 million. This amount is nearly $2 million greater than the previous year, represents the largest distribution ever for Miami, and is more than double the amount distributed in 2004. Over the last ten years, the cumulative distributions have totaled over $136.7 million and have provided an important source of funding to help offset reductions in state support. The following chart shows the proportion of programs supported by the 2013 distributions.

The For Love and Honor capital campaign surpassed its $500 million goal during the fiscal year. This milestone represented the third goal of a campaign that was by far the most successful fundraising effort in Miami’s history. This generous support has been transformational, allowing more students to receive scholarships, professors to receive support, and buildings to be built or renovated. Looking ahead, improved financial aid resources remain our primary fundraising priority. These impactful gifts provide the resources to enhance student recruitment, moderate tuition increases, and alleviate the effect of sustained lower state subsidies. As the campus community embarks on its strategic Miami 2020 plan, your continued commitment to Miami is appreciated and will continue to be vital to shaping Miami’s vibrant future.