



To: WSLCA Executive Committee
WSLCA Delegates and Affiliates
From: Tobin Follenweider, Asset Management Committee Chair
Date: Tuesday, January 6, 2015
Re: Asset Management Committee Report - January 2015

Committee Meeting Date: January 6
Time: 10:15 am to 11:45 am
Attendance: 21

WSLCA ASSET MANAGEMENT COMMITTEE TOPICS AREAS

1. Portfolio wide - CAP #1 (Active)
2. Operations - CAP #2 (On hold)

CAP #1 - PORTFOLIO MANAGEMENT PRINCIPLES

Presenter - *Bill Jarvis, CommonFund Institute*

Three important questions:

- How should we conceptualize, analyze and measure a portfolio that is composed of resource-productive land, commercially-productive land, other types of land, and financial assets?
- What sustainable rate of return can we reasonably expect from such a portfolio over a perpetual time frame?
- How can such a portfolio be responsibly and transparently governed?

How different are we from educational and private endowment/foundation investments?

- US
 - Colleges 8% in Real Estate
 - Foundations 4% in Real Estate
 - Trinity Wall Street (NY) \$2 to \$3 billion in RE
 - Kamehameha (Hawaii) >\$9 billion in Real Estate
- UK
 - 75% of "Oxbridge" schools own an average of 30% real estate
 - Real Estate viewed as a Bond substitute

Committee Meeting Date: January 6

Time: 10:15 am to 11:45 am

Attendance: 21

What are asset categories?

- Asset Categories
 - Growth (Equities)
 - “Equity Risk Premium” 6% (2% dividends, 4% expansion)
 - Inflation Hedge (Land, Real Estate, Commodities, etc)
 - Commodities are not a great hedge against inflation (Great Depression).
 - Deflation Hedge (Bonds)
 - Diversifiers (Hedge Funds)
- Liabilities
 - Beneficiary revenues, “Payout”
 - Cost increases, Inflation
- Modeling
 - Risk factor analysis
 - Monte Carlo simulation
 - Volatility

What are the funds for?

- Beneficiaries
 - Urgent needs of today tend to trump future needs
 - “Intergenerational Equity”
 - Purchasing power should be maintained as measured by some index
- Sustainable Return
 - 4.5% to 5.0% spending + 3% equity (appreciation) + 1% operations = 8.5% to 9.5%
 - 3 year moving average
 - Inflation methodologies - needs floor and ceiling
 - Need to consider the exhaustion of extractive assets
- Role of Land
- Payout Policy
- Earning Reserve

How to Make Decisions (Governance)?

- Transparency
- Legacy
- Beneficiary
- Governance, not management
- Committees
 - Investment committees/ Investment Strategies Committee of the Board”
 - Governance Manual
 - Training

Committee Meeting Date: January 6

Time: 10:15 am to 11:45 am

Attendance: 21

UPMIFA - Uniform Prudent Management Institutional Funds Act

- For donor restricted funds but applicable to endowment investment management
- Enacted in 49 states in 2006
- Creates "Safe Harbor"
- Sets Standards for:
 - Investment
 - Spending(appropriation)
 - Delegation
- Affirmative duty to diversify

Committee Participant Questions

- Are we gaining anything if we only diversify with real estate?
- Emotional tie to land?
- Invest wisely?
- Avoid fund raids
- How do we institute governance change with bosses and elected officials?

Next Steps

- Draft documents
- Interim conference call - April/May 2015
- CommonFund Endowment Institute - July 12-16
- Send out documents

Asset Management Committee



22 attendees

Asset Management Committee Meeting
Phoenix, Arizona
Tuesday, January 6, 2015
10:15am-11:50am

Sign In

1. Robin Follenweider Colorado State Land Board
 2. RENE TRUAN rene.truan@ag.texas.gov TX
 3. MIKE MURPHY IDAHO mmurphy@id.gov
 4. Mia Stier Sonoran Institute mstier@sonoraninsti.tute
 5. GINO DI BETTIN AK-TRUST LAND OFFICE gdi@alaska.gov
 6. Tim Donaldson UT State Dept of Education tim.donaldson@schools.utah.gov
 7. RON CARLSON SITLA RCARLSON@UTAH.GOV
 8. Kim Christy SITLA kimchristy@utah.gov
 9. Bill Evert Co. bevert@heincpa.com
 10. Laena Bartlett BOK Financial l.Bartlett@BOKF.com
 11. Keith Kuhlman Oklahoma Keith.Kuhlman@CLO.ok.gov
 12. Jeff Engleson ND jengleson@nd.gov
 13. Dave Shripman OK Dave.Shripman@CLO.ok.gov
 14. James Spurgeon OK James.Spurgeon@CLO.ok.gov
 15. Denise Nechvatal WI denise.nechvatal@wisconsin.gov
- Lisa Schneider UT lisa.schneider@utah.gov
Katmy Orr ED/ID

16. John Andrews UT

17. Paula Plant Mt. State Bd of Education

18. Mary Abrams OR

19. Tina Nelson WI

20. Harry Bordwell OK

21. _____

22. _____

23. _____

24. _____

25. _____

26. _____

27. _____

28. _____

29. _____

30. _____

31. _____

32. _____

33. _____

34. _____

35. _____

WSLCA Asset Management Committee Agenda

January 6, 2015

8:30 am - 10:00 am

- I. Introductions (10 mins)
- II. Priority Strategy #1 - Portfolio Management Principles and Strategies (70 mins)
 1. Portfolio Governance
 2. Portfolio Goals
 3. Portfolio Model
- III. New Affiliate Member List Recommendations (5 mins)
- IV. Future Committee Schedule (5 mins)
 - a. Priority Strategy #1 - Portfolio Management Principles - Draft Principles
 - b. Priority Strategy #2 - IT Best Management Practices - Interim Meeting



To: WSLCA Asset Management Committee
Other Interested Parties
From: Tobin Follenweider, Colorado State Board of Land Commissioners
Date: Thursday, December 11, 2014
Re: WSLCA Asset Management Committee Priority Strategy #1 - January 2015

This document introduces and outlines the discussion on WSLCA Asset Management Committee's Priority Strategy #1 to develop portfolio management strategies and principles appropriate to WSLCA member state assets.

Once these portfolio management principles are complete, WSLCA members will be able determine where to focus their portfolio management efforts. Some strategies and principles may not be immediately relevant to WSLCA members and will take time to implement. We will also identify areas for further discussion and study and make adjustments to the principles along the way. However, I believe that developing portfolio management principles that are suitable to state trust asset portfolios will be valuable for the WSLCA members and our beneficiaries.

The formation of WSLCA's portfolio management principles involves consideration of three important questions:

- How should we conceptualize, analyze and measure a portfolio that is composed of resource-productive land, commercially-productive land, other types of land, and financial assets?
- What sustainable rate of return can we reasonably expect from such a portfolio over a perpetual time frame?
- How can such a portfolio be responsibly and transparently governed?

I would like to thank Bill Jarvis of the Common Fund for his assistance and continued support for this project.

PORTFOLIO MANAGEMENT

Portfolio management can be described as:

The art and science to making decisions about investment mix and policy, matching investments to objectives, asset allocation for individuals and institutions, and balancing risk against performance <http://www.investopedia.com>

Many are familiar with the various portfolio management concepts particularly anyone who has met with a financial advisor. Portfolio management concepts include diversification, risk management, income distribution, hedging strategies, asset mix, investment horizon, etc.

While I believe these portfolio management concepts apply to state trust asset management, it has been difficult to implement these due to the political, legal, and physical circumstances of state trust asset management:

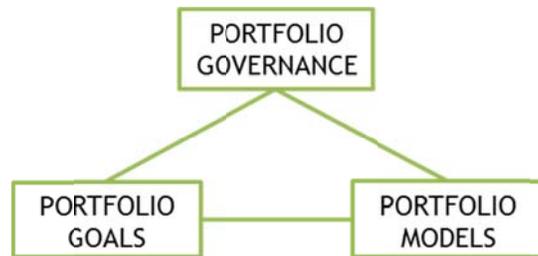
- Portfolio management is usually presented in the context of cash investments (bonds and securities) whereas state trust assets are generally dominated by real property holdings (land, buildings, and minerals).
- Portfolio management concepts tend to focus on standard market valuation methods whereas some state trust assets cannot be valued (at least not valued using standard valuation models) and/or some of assets cannot be legally sold. State trust managers also have limited resources to value their portfolios.
- Portfolio management concepts tend to focus on independent and flexible governance models whereas state trust assets are subject to considerable political and legal oversight as well as public expectations.

Despite these constraints and differences, I believe that portfolio management concepts can adapted to state trust asset management.

DISCUSSION

As identified in the three important questions above, WSCLA portfolio management principles would have three focus areas: portfolio governance, portfolio goals, and portfolio models.

Figure 1: Portfolio Management Principles



PORTFOLIO GOVERNANCE - *How to establish legitimacy and confidence?*

Any portfolio management document, particularly one geared toward multi-generational portfolios, need to contain governance principles. Given that WSLCA member states have more or less unique governance structures and associated decision making processes, it will be difficult to establish across-the-board governance principles. Nonetheless, I anticipate that we will be able to distill and evaluate a set of core governance principles applicable to state trust portfolio management.

Governance topics for discussion may include:

- Existing and preferred governance models
- Transparent decision-making processes
- Investment policies and criteria
- Investment committees
- Director and/or investment manager selection and evaluation

PORTFOLIO GOALS - *How to build a fair, long-term and sustainable portfolio?*

Portfolio management principles should include standard portfolio management goals. In many ways, these are easy to articulate but difficult to specify and implement.

Goals topics for discussion may include:

- Long-run diversification
- Intergenerational equity
- Income distribution policy - sustainable "payout" benchmark/requirements
- Risks - political, financial, inflation, etc.
- Risk hedging strategies (e.g. property as an inflation hedge)
- Total return targets

PORTFOLIO MODELS - *How to measure and integrate data in complex and changing world?*

Building a portfolio model involves understanding, characterizing, and ultimately valuing trust assets. While establishing a value for all assets is the ultimate goal, characterizing the state trust portfolio without full valuation can be just as important.

Model topics for discussion may include:

- Total trust model - cash and property
- Link to portfolio goals.
- Building an asset characterization model
 - What, where, and when
 - What do you have a lot of?
 - What do you have a little of?
 - Revenues by asset

- Building as asset valuation model
 - Consistent
 - Repeatable
 - Explainable
 - Realistic - "Meets the straight face test"
 - Dynamic
 - Assumptions
 - Testing the model
 - Sensitivity analysis
 - Scenario building
 - Measure total return - 3 year moving average
 - Income
 - Appreciation

BACKGROUND REFERENCE¹

The following is by no means an exhaustive list of reference material and I would encourage the addition of more documents by WSLCA members before, during, and after the January 2015 meeting. Please review the Common Fund principles document because I believe it provides a good model for the WSLCA investment management principles document.

- "Principals of Investment Management for Long Term Funds " Common Fund November 2014
- "Strive for the Best: Building and Maintaining an Excellent Board" Common Fund May 2014
- "Asset Allocation and Governance Review Idaho Board of Land Commissioners - Executive Summary" Janet Becker-Wold, CFA, Sally Haskins James Van Heuit, November 24, 2014
- "Portfolio Goals and Analysis" Colorado State Board of Land Commissioners, October 2014
- "Chapter 15 Concluding Observations" Endowment Asset Management, Acharka and Dimson 2007
- "Trust Lands and Education Funding" Sonoran Institute 2007

¹ Please send me an email you want the background reference materials (tobin.follenweider@state.co.us)