

## McGILL UNIVERSITY

### REPORT ON ENDOWMENT PERFORMANCE 2012-13

The McGill endowment is comprised of (i) bequests and donations received by the University, for the most part with specific designations, and to be held in perpetuity (ii) those assets designated by the Board of Governors to be endowed and (iii) those assets of certain McGill units and affiliated entities which have been allocated to the McGill Investment Pool (“MIP”) as an investment vehicle. The endowment is managed by the McGill Office of Investments under the direction of the Investment Committee.

The overall objective of the endowment is to obtain a total return (yield plus capital appreciation) necessary to provide a dependable and optimal source of income for endowment beneficiaries, to cover the annual operating costs of the endowment and to preserve (in real dollar terms) the capital of the endowment within the social and ethical norms of the University.

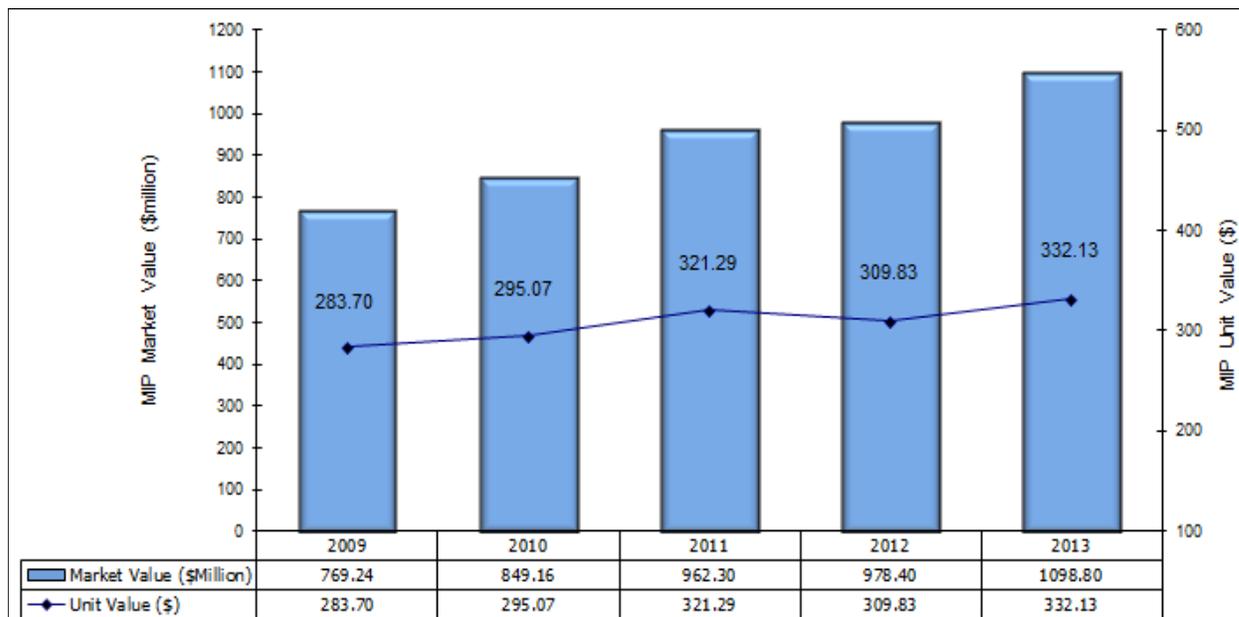
The endowment fund is managed as the MIP which was formed in 1970. The use of a unitized pool allows for the investment of a critical mass of assets thus providing for broad diversification and economies of scale that have over the years resulted in positive performance, reduced volatility and low investment management fees.

At April 30, 2013, the end of the University’s fiscal period, the MIP, with a market value of \$1.1 billion, consisted of investments for the McGill endowments and accounts managed on behalf of McGill units and affiliated entities.

#### **MIP Market and Unit Value**

The MIP market and unit value changes, over the fiscal periods ended May 31, 2009 and May 31, 2010 and April 30, 2011 to April 30, 2013, are shown below:

**MIP Market Value and Unit Value Change (May 31, 2009-2010 & April 30, 2011 to 2013)**



#### **MIP Growth**

**Table 1: Change in market value for the year ended April 30, 2013**

		(000's)
Market value of the MIP, beginning of the year		978,372
Unrealized market gain	42,826	
Gain on sale of investments	55,600	
Investment income	25,904	
Foreign exchange loss	<u>(2,188)</u>	
Total MIP earnings		122,142
Endowment income distribution and management fee		(48,568)
Gifts/bequests	38,466	
Capitalization of income distributed	6,323	
Net other transfers	<u>2,059</u>	
Total net capital contributions	-	<u>46,848</u>
Net change in market value during the year		<u>120,422</u>
Market value of the MIP, end of the year		<u><u>1,098,794</u></u>

### **Income Distribution and Management Fee**

The 2012-13 distribution rate per unit was based on 4.25% of the average market value of the MIP at the end of each of the previous three fiscal periods. This practice is used to minimize the impact of market fluctuations on the endowment fund and is consistent with practices adopted at other leading North American universities. It is based on the distribution of an appropriate and prudent level of income to all unit holders. For the 2013-14 fiscal year the distribution rate per unit will be based on the average market value of the previous three fiscal periods ended April 30, 2012, April 30, 2011 and May 31, 2010 as approved by the Board of Governors.

For the year ended April 30, 2013, \$40.8 million in income was distributed to the University's endowment beneficiaries based on an annual distribution rate of \$12.75 per unit. For fiscal 2013-2014 the annual income distribution amount per unit will be \$13.12.

For 2012-13, the management fee of .90% of the average market value of the previous three years amounted to \$7.7 million. The management fee covers the endowment fund's administrative costs, investment management fees, custodial expenses and the cost of other service providers as well as a contribution to the University's indirect costs. The management fee will be calculated in the same manner for the 2013-14 fiscal year, in that it will be based on the average market value of the previous three fiscal periods ended April 30, 2012, April 30, 2011 and May 31, 2010.

### **Governance and Investment Management**

The Investment Committee, a committee of the Board of Governors ("Board"), oversees the investment of the MIP assets. The Office of Investments is responsible for implementing the Investment Committee's decisions.

The Investment Committee is comprised of 10 members who, as at June 30, 2013 consisted of Joel Raby (Montreal), Chair; Heather Munroe-Blum (Montreal), Principal and Vice-Chancellor, ex-officio; Robert Rabinovitch (Montreal), Nathalie Bernier (Montreal), Kathy Fazel (Montreal), Mark Hantho (New York), Gerald Sheff (Toronto), Arnold Steinberg (Montreal), Danny Ritter (Montreal) and Stuart Cobbett (Montreal), Chair of the Board, ex-officio. Marc Weinstein (Montreal), Vice-Principal (Development and Alumni Relations) and Anthony Campbell (New York), serve as Special Advisors. Members are appointed on the basis of their expertise and interest in investment, business and economics.

Pursuant to its Terms of Reference, the Committee is responsible for overseeing the management of the University's investments in accordance with the Statement of Investment Policy. Included in the Committee's functions are (i) providing advice to the Board in establishing policies related to investments and making recommendations thereon to the Board for approval, (ii) reviewing annually the appropriateness of the Statement of Investment Policy and making recommendations on proposed modifications to the Board (iii) recommending to the Board policies on the annual distribution rate for the income from the University's endowment (iv) reviewing and approving the appointment and termination of investment managers and service providers, investment manager mandates and the performance of each fund manager and (v) monitoring compliance with the Statement of Investment Policy.

The Committee met four times during the fiscal year ended April 30, 2013. Overall attendance averaged 75%.

**Decisions related to manager changes for the period ended April 30, 2013 are noted below:**

During the year, a number of investment manager changes were undertaken under the direction of the Committee.

Further diversification of the MIP's hedge fund portfolio away from funds of funds and predominantly hedged equity exposure as approved by the Investment Committee in April 2012 continued during the fiscal year ended April 30, 2013. In addition to hedged equity, allocations to the following strategies have been approved: (i) credit/distressed, (ii) event-driven, (iii) relative value and (iv) CTA/global macro.

The portfolio diversification was further implemented through the allocation to the following three new managers and strategies in November and December 2012: Silver Point Capital Offshore, Ltd., (US \$20 million), credit/distressed; Winton Futures Fund Ltd., (US \$20 million), CTA/global macro and AllBlue Ltd., (US \$15 million), relative value.

In November 2012, the Investment Committee approved an allocation of \$40 million to five early-stage hedged equity managers. Funding of the early-stage hedged equity manager mandate is expected to be completed during the 2013-2014 fiscal year.

In addition to the above, new investment agreements were entered with Catalyst Fund Ltd. Partnership IV ("Catalyst") and JOG Ltd. Partners No. VI ("JOG VI"). The Catalyst IV commitment (US \$20 million) is to a Canadian fund investing in securities of distressed and undervalued Canadian companies. The commitment to JOG VI (\$15 million) is to a Canadian early stage oil and gas fund.

Three new investment manager mandates were granted during the year and one investment manager was terminated. Van Berkomp and Associates was hired to manage an actively managed Canadian small-cap mandate as well as an actively managed U.S. small-cap mandate. Jarislowsky Fraser's Canadian equity mandate was terminated during the year. In addition, the U.S. high yield bond exchange traded fund was sold during the year and Neuberger Berman Fixed Income LLC was hired to manage a U.S. high yield bond fund.

As at June 30, 2013, approximately 80% of the University's endowment investments were managed by external investment managers. These managers and their respective mandates were:

- **Pyramis Global Advisors**, a Fidelity Investments Company (Canadian equity)

- **LSV Asset Management** (U.S. small/mid-cap equity)
- **Aberdeen Asset management** (emerging markets equity)
- **William Blair & Company** (non-North American equity for both developed and emerging markets)
- **Hexavest Inc.** (non-North American equity)
- **Comgest Asset Management** (emerging markets equity)
- **TD Asset Management** (Canadian bond index, Government of Canada T-bills and a passive currency hedging program)
- **Phillips, Hager & North** (fixed income)
- **Neuberger Berman** (U.S. high yield bonds)
- **Van Berkom** (one U.S. and one Canadian small-cap equity)
- **Hedge Funds** (two funds of funds, primarily invested in long/short equity and six direct funds investing in various strategies)
- **Private equity** (six private equity funds of funds, investing on a combined basis in North American and European buyout, venture capital and global secondary funds, two Canadian funds investing in securities of distressed and under-valued Canadian companies and two Canadian venture capital limited partnerships)
- **Commodities** (two North American natural resources funds of funds, three Canadian oil and gas funds)
- **Real estate** (four limited partnerships investing in Canadian real estate and one U.S. open-ended real estate fund)

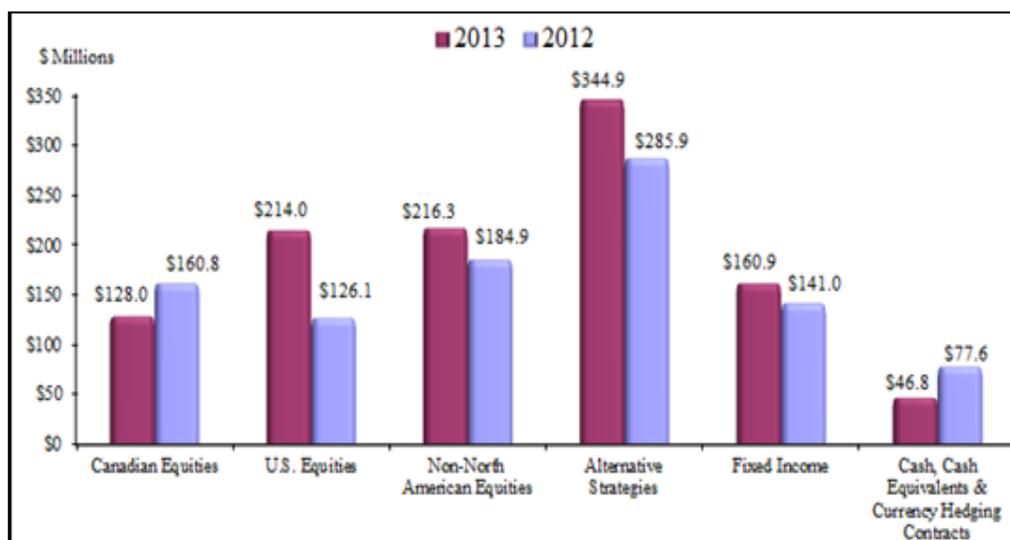
In addition to the above, two investment management mandates granted to Desautels Capital Management Inc., for global equity and for global fixed income, are managed by students in McGill University's Desautels Faculty of Management.

The Office of Investments manages approximately 20% of the MIP internally. It holds securities in an account pending liquidation or allocation to an external investment manager, in addition to managing cash and cash equivalents and exchange-traded funds.

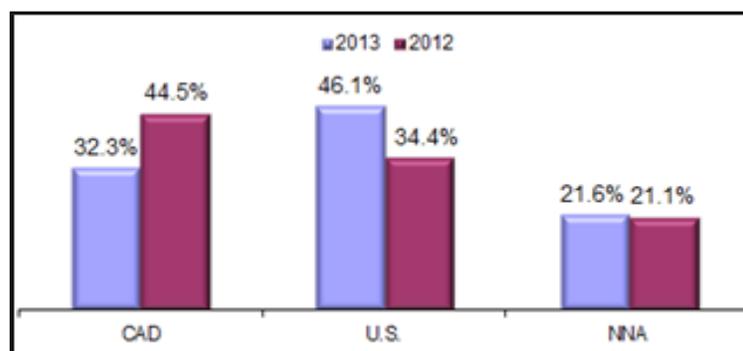
## Asset Distribution

The asset allocation of the MIP portfolio by asset class at June 30, 2013 and at June 30, 2012 is shown below:

MIP Asset Distribution by Asset Class as at June 30 (2013 - \$1,110.9 M; 2012 - \$976.3 M)



### MIP Asset Allocation by Currency as at June 30, 2013



The currency allocation for total investments at June 30 is shown in the above chart. The 12.2 percentage point decrease in Canadian exposure and the increase in U.S. exposure reflect primarily rebalancing activities.

### Performance Measurement 2012-2013

Performance measurement of the MIP is carried out quarterly on a calendar year basis by an independent performance measurement service. Investment rates of return are stated on a total return basis which is capital appreciation, both realized and unrealized, plus income received and accrued. The following table indicates the performance of the MIP as well as the median returns of the BNY Mellon Canadian Master Trust Universe and the BNY Mellon Foundations and Endowments Universe, a composite of the returns of four comparable Canadian university endowment funds, the absolute return objective and the MIP's composite benchmark over a range of periods ended June 30, 2013:

	Annualized Returns			
	<u>1 year</u>	<u>3 years</u>	<u>5 years</u>	<u>10 years</u>
Total MIP	14.4%	10.7%	4.5%	5.9%
Absolute Return Objective	6.3%	7.1%	6.7%	7.5%
Composite benchmark (policy weights times related index returns)	11.8%	9.7%	4.6%	5.8%
Median – BNY Mellon Canadian Master Trust Universe	10.6%	9.1%	4.8%	6.9%
Median – BNY Mellon Foundations & Endowments Universe	11.4%	9.1%	5.0%	6.4%
Composite of the returns of four comparable Canadian university endowment funds	14.7%	10.2%	3.5%	6.2%

Prepared by: Office of Investments