

McGILL UNIVERSITY

REPORT ON ENDOWMENT PERFORMANCE 2013-14

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 (“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.

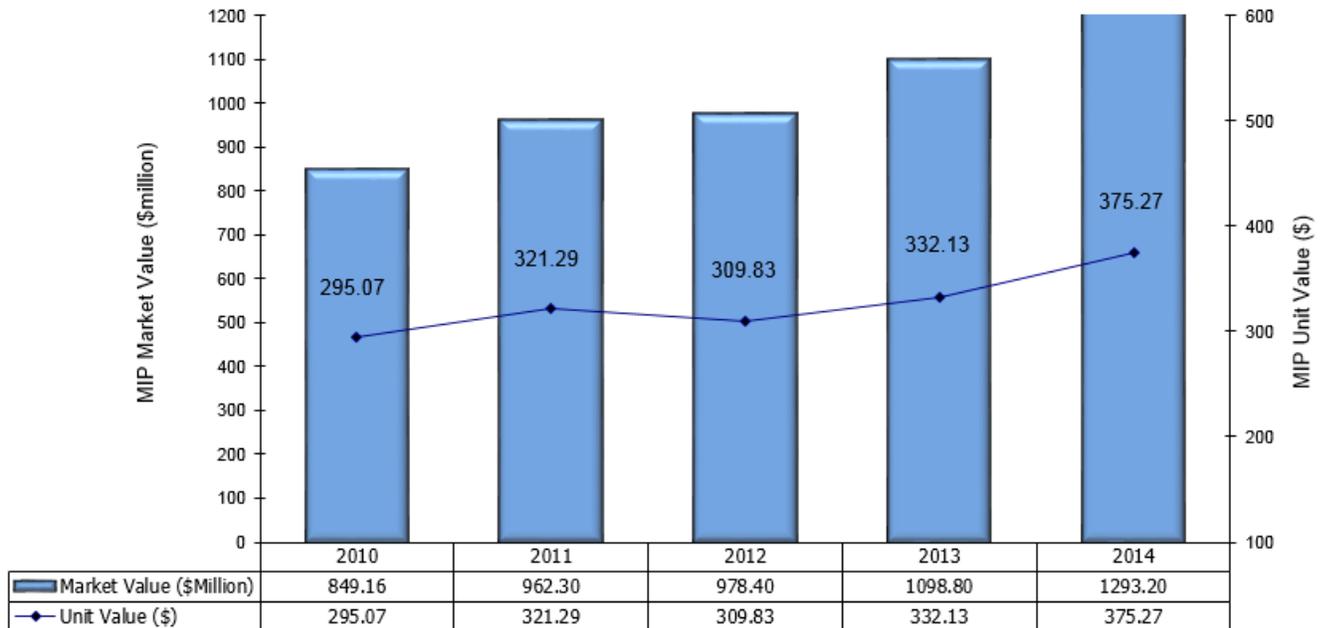
The endowment fund is managed as the MIP which was formed in 1970. The use of a unitized pool allows for the investment of a critical mass of assets thus providing for broad diversification and economies of scale that have over the years resulted in positive performance, reduced volatility and low investment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

At April 30, 2014, the end of the University’s fiscal period, the MIP, with a market value of \$1.3 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, 2010 and April 30, 2011 to April 30, 2014, are shown below:

MIP Market Value and Unit Value Change (May 31, 2010 & April 30, 2011 to 2014)



MIP Growth

Table 1: Change in market value for the year ended April 30, 2014

		(000's)
Market value of the MIP, beginning of the year		1,098,794
Unrealized market gain	119,093	
Gain on sale of investments	62,129	
Investment income	26,196	
Foreign exchange loss	<u>(7,904)</u>	
Total MIP earnings		199,514
Endowment income distribution and management fee		(52,663)
Gifts/bequests	40,443	
Capitalization of income distributed	5,760	
Net other transfers	<u>1,355</u>	
Total net capital contributions		<u>47,558</u>
Net change in market value during the year		<u>194,409</u>
Market value of the MIP, end of the year		<u>1,293,203</u>

Income Distribution and Management Fee

The 2013-14 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 2014-15 fiscal year the distribution rate per unit will be based on the average market value of the previous three fiscal periods ended April 30, 2013, April 30, 2012 and April 30, 2011 as approved by the Board of Governors.

For the year ended April 30, 2014, \$44.3 million in income was distributed to the University's endowment beneficiaries based on an annual distribution rate of \$13.12 per unit. For fiscal 2014-2015 the annual income distribution amount per unit will be \$13.65.

For 2013-14, the management fee of .90% of the average market value of the previous three years amounted to \$8.4 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 2014-15 fiscal year, in that it will be based on the average market value of the previous three fiscal periods ended April 30, 2013, April 30, 2012 and April 30, 2011.

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, 2014 consisted of Joel Raby (Montreal), Chair; Suzanne Fortier (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), serves as Special Advisor. 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 five times during the fiscal year ended April 30, 2014. Overall attendance averaged 72%.

Decisions related to manager changes for the period ended April 30, 2014

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

The funds' hedge fund diversification, which began in 2012, was completed during the year with new allocations to the following four hedge fund managers and strategies: Lodge Hill Fund, Ltd. (US \$10 million), hedged equity; Tiger Ratan Capital Fund (Cayman) Ltd. (USD \$8 million), hedged equity; Cooper Square Offshore Fund Ltd. (US \$8 million), non-U.S. hedged equity and Nipun Asia Total Return Offshore Fund, Ltd. (US \$8 million), Asian markets hedged equity. Offsetting these additions was the sale during the year of the remaining investment in Communfund Hedge Fund Series 1.

New real estate investment agreements were entered into with Forgestone Capital Fund no. 1 L.P. ("Forgestone") and AEW Partners VII, L.P. ("AEW"). The Forgestone commitment (\$15 million) is to a fund that develops properties throughout Canada. The AEW commitment (US \$15 million) is to a fund that invests opportunistically, primarily in the United States.

A new private equity investment agreement was entered into with Angelo Gordon Capital Recovery Partners VIII, L.P. ("AG Capital"). The AG Capital commitment (US \$ 15 million) is to a fund investing in a diversified portfolio of corporate debt, primarily in the U.S.

In addition to the above, a new investment management mandate was granted during the year to Comgest Asset Management International Limited for an investment in their Comgest Growth Europe fund which invests primarily in the equity of European companies.

As at June 30, 2014, approximately 86% 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** (one emerging markets equity mandate and one European equity mandate)
- **TD Asset Management** (Canadian bond fund, Government of Canada T-bills and a passive currency hedging program)
- **Phillips, Hager & North** (Canadian fixed income)
- **Neuberger Berman** (U.S. high yield bonds)
- **Van Berkomp** (one U.S. and one Canadian small-cap equity mandate)
- **Hedge Funds** (Eleven Hedge Funds in total: one fund of funds, primarily invested in long/short equity and ten 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, two Canadian venture capital funds, and one fund investing primarily in U.S. corporate debt)
- **Commodities** (two North American natural resources funds of funds and three Canadian oil and gas funds)
- **Real estate** (five funds investing in Canadian real estate and one investing in U.S. real estate)

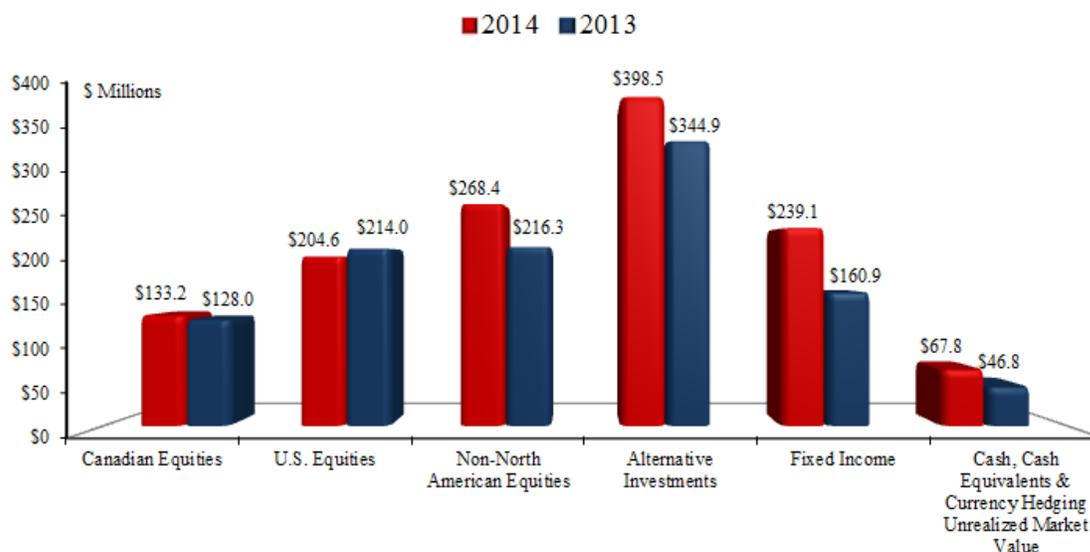
In addition to the above, two investment management mandates granted to Desautels Capital Management Inc., for global equity and for global fixed income, are managed by students in McGill University's Desautels Faculty of Management.

The Office of Investments manages approximately 14% of the MIP internally. It mostly holds exchange-traded funds.

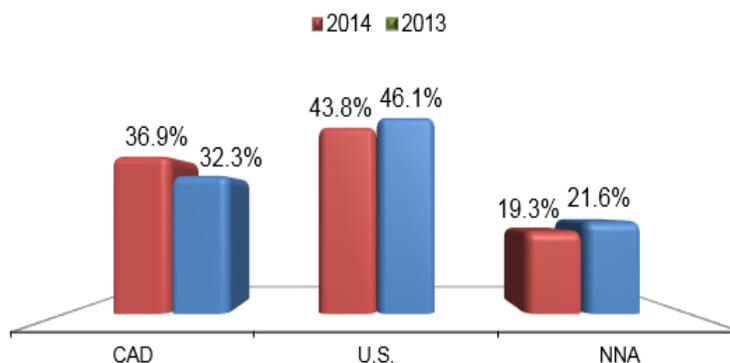
Asset Distribution

The asset allocation of the MIP portfolio by asset class at June 30, 2014 and at June 30, 2013 is shown below:

MIP Asset Distribution by Asset Class as at June 30 (2014 - \$1,311.6 M; 2013 - \$1,110.9 M)



MIP Asset Allocation by Currency as at June 30



The currency allocation for total investments at June 30 is shown in the above chart.

Performance Measurement 2013-2014

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 Canadian Foundations and Endowments Universe, a composite of the returns of five comparable Canadian university endowment funds, the absolute return objective and the MIP's composite benchmark over a range of periods ended June 30, 2014:

	Annualized Returns			
	1 year	3 years	5 years	10 years
McGill Investment Pool	19.2%	11.7%	11.7%	6.2%
Absolute Return Objective	7.5%	6.8%	7.1%	7.4%
Composite benchmark (policy weights times related index returns)	16.9%	10.1%	10.3%	6.0%
Median – BNY Mellon Canadian Master Trust Universe	17.7%	10.2%	10.5%	7.1%
Median – BNY Mellon Canadian Foundations & Endowments Universe	16.6%	10.3%	11.0%	6.4%
Composite of the returns of five comparable Canadian university endowment funds	18.1%	10.8%	10.9%	6.1%