

MCGILL UNIVERSITY

REPORT ON ENDOWMENT PERFORMANCE 2015-16

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

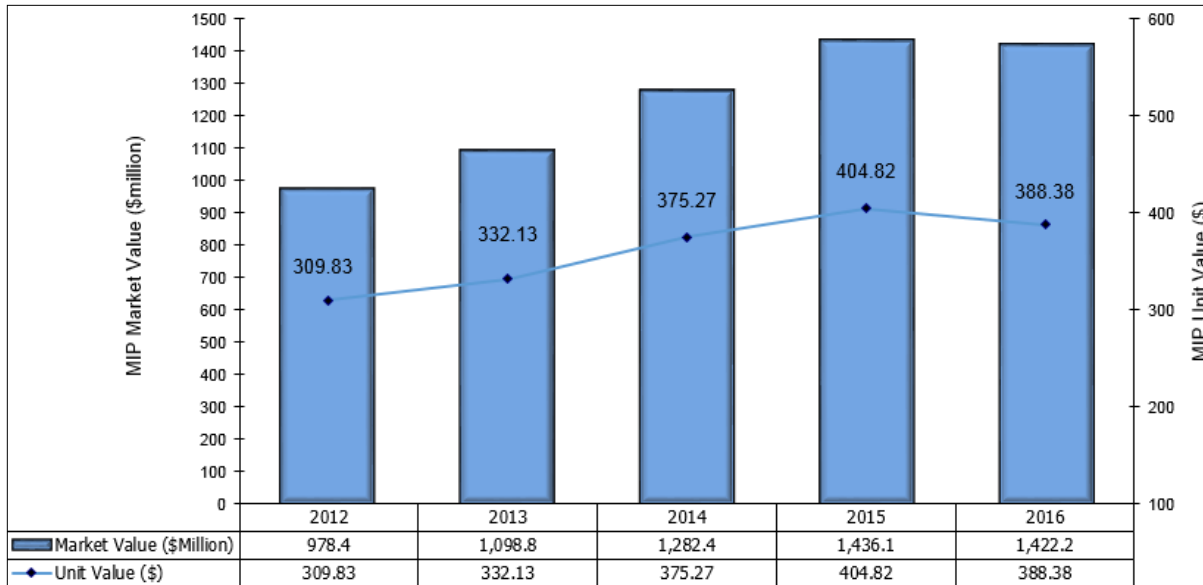
The endowment fund is managed as the MIP which was formed in 1970. The use of a unitized pool allows for the investment of a critical mass of assets thus providing for broad diversification and economies of scale that have over the years resulted in positive performance, reduced volatility and low investment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

At April 30, 2016, the end of the University’s fiscal period, the MIP, with a market value of \$1.4 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 April 30, 2012 to April 30, 2016, are shown below:

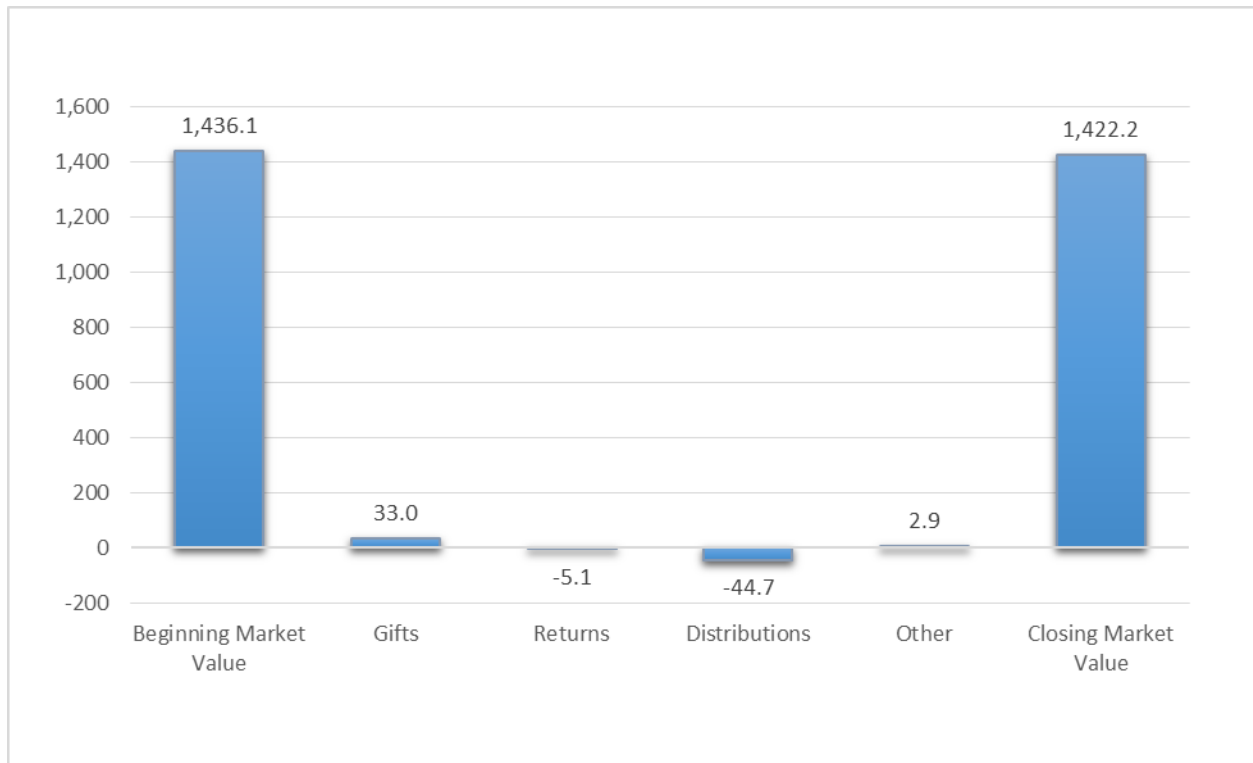
Graph 1: MIP Market Value and Unit Value Change (April 30, 2012 to April 30, 2016)



The unit value for the 12 months ended April 30, 2016 decreased by -4.1% compared to an increase of inflation of 1.7% for a real return of -5.8%.

MIP Growth

Graph 2: Change in market value for the year ended April 30, 2016



Income Distribution and Management Fee

The 2015-16 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 plus an additional 0.25% distribution was added. 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 2016-17, the 4.25% rate will be maintained plus an additional 0.25% distribution will be added to the income distribution rate. As in previous years, distribution rate per unit will be based on the average market value of the previous three fiscal periods ended April 30, 2015, April 30, 2014 and April 30, 2013 as approved by the Board of Governors.

For the year ended April 30, 2016, \$44.7 million was spent as distributions to the University's endowment beneficiaries based on an annual distribution rate of \$15.26 per unit. For fiscal 2016-17 the annual income distribution amount per unit will be \$16.68.

For 2015-16, the management fee of 0.90% of the average market value of the previous three years amounted to \$10.1 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. For fiscal 2016-17, the management fee will be 1.10% and will be calculated based on the beginning market value of fiscal 2016-17.

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.

Over the course of the year, the Investment Committee was comprised of 10 members consisting of Joel Raby (Montreal), Chair; Suzanne Fortier (Montreal), Principal and Vice-Chancellor, ex-officio; Robert Rabinovitch (Montreal), Sam Altman (Montreal), Kathy Fazel (Montreal), Anik Lanthier (Montreal), Gerald Sheff (Toronto), Arnold Steinberg (Montreal) who sadly passed away in December 2015, Danny Ritter (Montreal) and Stuart Cobbett (Montreal), Chair of the Board, ex-officio. Marc Weinstein (Montreal), Vice-Principal (University Advancement), 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.

In June 2014 a Subcommittee of the Investment Committee was created with the mandate to act on issues which may arise between regular scheduled meetings. The Subcommittee is composed of the Chair of the Committee, a member of the Investment Committee, the Senior Steward and the Chief Investment Officer.

The Investment Committee and Subcommittee met six times during the fiscal year ended April 30, 2016. Overall attendance averaged 76%.

Decisions related to manager and consultant changes for the period ended April 30, 2016

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

Within the Public Equity Asset Class, a new allocation was made to ISHARES (XIU) and to SSGA S&P 500 (passive mandate) and the S&P 500 ETF mandate was terminated.

Within the Alternative Investments Asset Class, new allocations were made to Alphadyne International Master Fund (global macro strategy) and Formula Growth Alpha Fund (neutral strategy) while the mandates of AllBlue, Commonfund and Tiger Ratan were terminated. Allocation to Real Estate was increased during the year with an investment in IPSO FACTO (RPA) Limited Partnership consisting of senior retirement dwellings. Also, a new allocation to Listed Real Assets was made (Brookfield Investment Management).

Within the Fixed Income Asset Class, a new allocation was made to Municipal Bonds with the hiring of Optimum Asset Management. As a result, Phillips, Hager & North's short term mandate was terminated.

TDAM's currency hedging overlay mandate was terminated opting instead for an internally managed currency hedging overlay strategy.

As at June 30, 2016, approximately 97% of the University's endowment investments were managed by external investment managers. These managers and their respective mandates were:

Managers	Mandates
Equities and Bonds	
Fidelity Investments	Canadian equities
Van Berkomp Associates	Canadian and U.S. small-cap equities
SSGA	U.S. passive equities
LSV Asset Management	U.S. small/mid-cap equities
Hexavest	Non-North American equities
William Blair & Company	Non-North American equities (developed and emerging markets)
Aberdeen Asset Management	Emerging markets equities
Comgest Asset Management	Emerging markets equities
Phillips, Hager & North	Canadian fixed income
Optimum Gestion de Placements	Municipal bonds
Colchester Global Investors	Global Government bonds
Neuberger Berman	U.S. high yield bonds
Gestion de placements TD	Money market fund
Alternative Investments	
Hedge Funds	10 Hedge Funds investing in various strategies
Private Equity	3 secondary market funds 3 buyout funds 3 distressed funds 2 venture capital funds
Real Estate	5 Canadian funds 1 U.S. fund
Listed Real Assets	Fund investing in listed companies whose main businesses are linked to real assets
Commodities	2 North American natural resources funds of funds 3 Canadian oil and gas funds

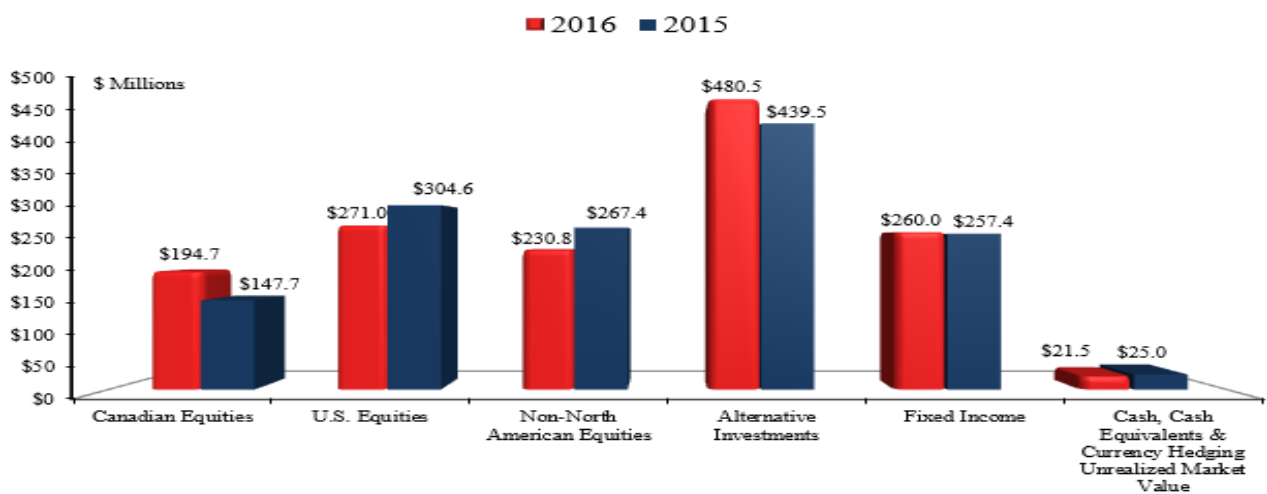
In addition to the above, two investment management mandates granted to Desautels Capital Management Inc., for global equity and for global fixed income, are managed by students in McGill University's Desautels Faculty of Management.

The Office of Investments manages approximately 3% of the MIP internally. It mostly holds iShares (XIU).

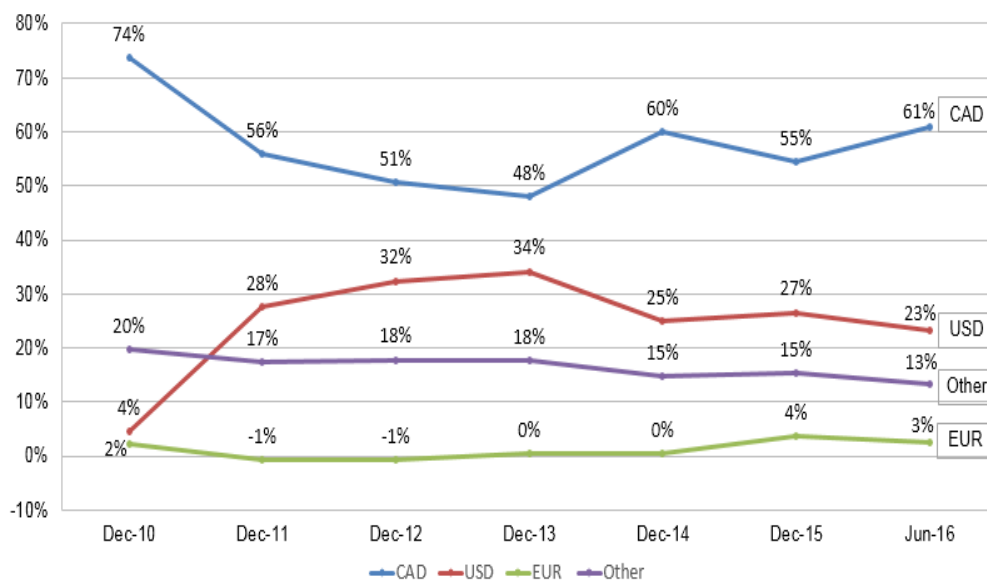
Asset Distribution

In accordance with performance measurement standards the following graph presents the asset allocation of the MIP portfolio at June 30, 2016 and at June 30, 2015:

Graph 3: MIP Asset Distribution by Asset Class as at June 30 (2016: \$1,458.4 M; 2015: \$1,441.6 M)



Graph 4: MIP Currency Exposure after hedging as at June 30



Performance Measurement 2015-16

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. For the twelve months ended June 30, 2016, the MIP had a rate of return of 2.7%, equal to that of the Canadian Foundations and Endowments Universe's median fund return of 2.7%, shown below. The following table also indicates the MIP's absolute return objective, the MIP's composite benchmark and the returns of five comparable Canadian university endowment funds over a range of periods ended June 30, 2016:

	Annualized Returns			
	1 year	3 years	5 years	10 years
Total MIP	2.7%	10.5%	9.6%	6.5%
Absolute Return Objective	6.6%	6.8%	6.7%	7.1%
Composite benchmark (policy weights times related index returns)	2.8%	10.3%	8.9%	6.4%
Median – BNY Mellon Canadian Foundations & Endowments Universe	2.7%	9.7%	9.0%	6.4%
Composite of the returns of five comparable Canadian university endowment funds	3.3%	10.4%	9.0%	5.8%

Since June 1, 2010, the Statement of Investment Policy stipulated an absolute return objective of 5.15% plus CPI measured over moving annualized five and ten-year time periods, however at their April 21, 2016 Investment Committee meeting, the Committee decided to change the absolute objective to: *“preserving (in real dollar terms) the capital of the MIP within the social and ethical norms of the University, to obtain a total return (yield plus capital appreciation) necessary to provide a dependable and optimal source of income for endowment beneficiaries and to cover the annual operating costs of the MIP”*. For the 2016-17 reporting year, the absolute objective will be based on this decision.

Prepared by: Office of Investments