Board of Trustees

Finance & Administration Committee

Friday, January 9, 2015

The Board of Trustees of Oregon State University

Regular Meeting of the Finance & Administration Committee

January 9, 2015
4:00 pm – 5:00 pm
Dial In Number: 1-855-244-8681
Meeting Number 193-048-827

AGENDA

1. **Call to Order/Roll Call/Declaration of a Quorum** (*Schueler*)

2. **Action Item**
   a. FY15 Q1 Operating Management Report (*Ford, Green*) F-2
   b. FY15 Q1 Investment Reports (*Ford, Green*)
      i. FY15 Q1 Market Background F-10
      ii. FY15 Q1 Public University Fund Investment Report F-14
      iii. FY15 Q1 Oregon State University Investment Report F-15

3. **Adjournment**

FY15 Q1 Operating Management Report

Oregon State University's 1st Quarter FY2015 Operating Management Report presents the first quarter operating results for the three operating fund groups: Education and General, Self-Support, and Restricted funds. The quarterly management report is a summary level report that compares:

- Year-to-date actual activity relative to the projected total for the year to the same relationship in prior years or to expected current year totals to provide early warning of unexpected operating trends.
- The current quarter projection for the year to the prior quarter projection to highlight mid-year changes in expected annual results.

The percentage of year-to-date actual revenue and expenditures to the total projected annual amounts is calculated to help ensure that the Board and management have an early warning regarding unanticipated operating trends in the major categories. This percentage is called the *realization rate* for revenues and the *burn rate* for expenditures. The next step is to compare the current year realization/burn rate to the seven year average of prior years' actual rates. The seven-year average is used to smooth out one-time operating changes. This method has proven to be very successful in identifying when the current year actual results are not tracking as expected, allowing management to make any necessary budgetary changes to address unanticipated results.

The low standard deviation of the actual year-to-date results for each quarter over the past seven years provides support for the predictive value of the data. The standard deviation, coupled with the materiality of the amounts provides a basis upon which we have established tolerance ranges within which the actual results should track. If the actual year-to-date amounts fall outside the established tolerances, the data is flagged for further analysis.

This approach is applied with the following tolerances:

- Tuition & Resource Fees, net of waivers – at +/- 2%
- Enrollment Fees – at +/- 2%
- Sales & Services – at +/- 5%
- Other revenue – at +/- 7%
- Federal restricted – at +/- 5%
- State restricted – at +/- 7%
- Other restricted – at +/- 6%
- Personnel Services – at +/- 2%
- Supplies & Services & Capital Outlay – at +/- 5%

To provide similar precision to the other captions in the report for which actual results do not track similarly from year to year, the expected current year results provides similar predictive value to the report. For these captions, we have established tolerance ranges based upon materiality. This approach is applied with the following tolerances:

- State General Fund – at +/- 2%
- Transfers – at +/- 10%

The breakdown and discussion of the variances in the FY2015 1st quarter report for each major operating fund type is as follows:

Education and General

The Personnel Services year-end projection has been increased approximately $9.9M primarily due to the following items:

- Additional $1.8M in faculty salaries and OPE for current and projected staffing levels.
- Additional $0.6M in classified pay and OPE for current and projected staffing levels.
- Increase of $4.3M in unclassified non-faculty salaries and OPE due to items that were not considered in the initial budget.
    - The redistribution from other funds that occurred in FY2014 4th quarter (this was a variance in Q4 report and discussed at the October meeting).
    - Some mid-year new hires in FY14, most of which were for governance functions, were not captured for the FY15 projection. Increased governance-related costs were offset by savings associated with reduced assessments paid to the Chancellor's Office.
- Other personnel services costs increased by approximately $3.2M mainly for:
    - A $1.3M update to the projection for PEBB costs.
    - A $0.6M increase to estimated compensated absences based on the FY14 liability.
    - A $1.3M increase in graduate fee remissions based on fall term experience.

The projected Ending Unrestricted Net Assets of 8.8% of operating revenues is up $1.2M, or 0.1% from the original budget.

Self-Support

As mentioned in the October 2014 meeting, the integrated planning and budgeting area is currently undergoing review and development of best practices. The newly promoted Director of Capital Budgeting and Self-Support Fund Budget and Resource Planning has performed extensive reviews of the original budget and as such there are a number of changes reflected in this quarter's projection. They are as follows:

- The Sales & Services revenue projection was increased approximately $5.3M due mainly to:
    - Reflecting where the approximately $4.8M of the University Shared Services Enterprise (USSE) revenues will be recorded (originally budgeted in Other Revenue).
    - Increase in projected revenue of approximately $0.5M in multiple other units.
- The Other Revenues projection was decreased by approximately $9.6M primarily due to:
    - Reflecting where the approximately $4.8M of USSE revenues will be recorded.

- Correcting for a budget overstatement due to duplication of approximately $4.0M of 5th Site (USSE unit providing IT services to the Technical and Regional Universities and the Chancellor's Office) revenue.
- Athletics projecting lower PAC 12 revenue of approximately $0.4M.
- $0.4M decreases in various other units.

- The Supplies & Services & Capital Outlay projection is being increased a net $5.1M due to the following increases and decreases:
  - Housing & Dining
    - $1.0M – interest expense not included in the initial budget
    - $500K – better estimate of food cost inflation
    - $200K – better estimate of one-time costs related to Tebeau Hall opening
    - $150K – unexpected vendor rate increase in garbage/recycling costs. Staff is working with the vendor to better understand the genesis of the increase and negotiate a reduced rate or a phase-in of the increase.
    - $150K – better estimates for various costs (consulting, training, repairs, etc.)

  - Student Centers
    - $3.2M – interest expense not included in the original budget
    - $675K – spending of building and equipment reserves moved after the budget was prepared. See more details regarding building and equipment reserves in discussion of transfers below.
    - $215K – a new fund, Student Media, was part of Educational Activities fund and was split off in FY15; it was not included in the initial budget

  - Athletics
    - $1.3M – increase in expenses for the University of Hawaii football game and higher food costs due the impacts of NCAA legislation

  - Parking
    - ($250K) – removed debt principal payment included in budget
    - ($740K) – removed depreciation included in budget
    - ($170K) – other various parking reductions

  - Designated Operations – USSE
    - ($1.5M) – removed duplicate 5th Site expense included in original budget
    - ($480K) – Other USSE budgets less than June estimate

  - Designated Operations
    - $325K – increase relating to INTO activity
    - $540K – various other units

Transfers In are increasing $15.1M due to moving the reserves for building repairs and equipment replacement from plant funds to operating funds. The building repair and equipment replacement reserves were moved from the plant fund group to the self-support funds in order to facilitate more complete reporting of the assets of the self-support funds. In addition, transfers from E&G are increasing $900K consisting mainly of $500K for the Student Experience Center furniture, fixtures and equipment, $190K for Ecampus support and $107K for Pre-college program moved to Designated Operations.

The projected Ending Unrestricted Net Assets of 35.1% of operating revenues is up $5.2M, or 3.5% from the original budget.

Restricted

In general, the restricted funds projections for revenues and expenditures are being adjusted upward based on the prior three year trending analysis. Specific to revenues, research awards received in FY2014 were up $20M or 11% and the current year F&A recovery rate in E&G funds is trending over budget as well.

Staff Recommendation to the Committee

Staff propose that the Board of Trustees' Finance and Administration Committee accept the FY2015 Quarterly Operating Management Report as of September 30, 2014.

Oregon State University

Quarterly Management Report

(Unaudited, For management purposes only)

As of September 30, 2014

For the Fiscal Year Ended June 30, 2015

(in thousands except enrollment)	YTD Actual			Budget & YE Projection					
	A	*B*	*C*	*D*		*E*	*F*	*G*	
	YTD	**YTD as a % of Projected**	**Prior 7 yr. avg. YTD %**	**Budget**	**Adjusted Budget 6/30/2015**	**Projected Variance from Budget**	**YE Projected 6/30/2015**	**Chg from prior qtr. projection**	**Notes**
EDUCATION & GENERAL									
State General Fund	$52,266	35%	36%	$150,328	$150,428	$100	$150,428	$100	
Tuition & Resource Fees, net of Remissions	127,023	40%	40%	314,523	317,403	2,880	317,403	2,880	
Other	14,564	19%	17%	73,888	76,737	2,849	76,737	2,849	
Total Revenues	193,853			538,739	544,568	5,829	544,568	5,829	
Personnel Services	(81,785)	19%	20%	(409,884)	(419,779)	(9,895)	(419,779)	**(9,895)**	(1)
Supplies & Services & Capital Outlay	(21,789)	19%	21%	(118,432)	(113,023)	5,409	(113,023)	5,409	
Total Expenditures	(103,574)			(528,316)	(532,802)	(4,486)	(532,802)	(4,486)	
Net from Operations	90,279			10,423	11,766	1,343	11,766	1,343	
Transfers In	93	8%	8%	1,226	1,119	(107)	1,119	(107)	
Transfers Out	(4,007)	53%	52%	(7,600)	(7,619)	(19)	(7,619)	(19)	
Fund Additions/(Deductions)	0			0	0	0	0	0	
Change in Unrestricted Net Assets	86,365			4,049	5,266	1,217	5,266	1,217	
Beginning Unrestricted Net Assets	42,693			42,693	42,693	0	42,693	0	
Ending Unrestricted Net Assets	$129,058			$46,742	$47,959	$1,217	$47,959	$1,217	
% Operating Revenues				8.7%	8.8%		8.8%		
Student FTE Enrollment-Summer and Fall terms only	10,538	40%	40%	26,064	26,564	500	26,564	500	

(1) $1.8M increase in faculty salaries and OPE for current & projected staffing levels, $600K increase in classified pay & OPE for current and projected staffing levels, increase of $4.3M in unclassified non-faculty salaries & OPE due to items that were not considered in the initial budget and $3.2M increase for new PEBB costs, estimated compensated absences and graduate fee remissions based upon fall term experience.

Oregon State University **As of September 30, 2014**

Quarterly Management Report **For the Fiscal Year Ended June 30, 2015**

(Unaudited, For management purposes only)

(in thousands except enrollment)	YTD Actual A YTD	B YTD as a % of Projected	C Prior 7 yr. avg. YTD %	Budget & YE Projection D Budget	Adjusted Budget 6/30/2015	E Projected Variance from Budget	F YE Projected 6/30/2015	G Chg from prior qtr. projection	Notes
SELF-SUPPORT - Auxiliaries, Designated Operations and Service Departments									
Enrollment Fees	$11,963	36%	38%	$33,636	$33,182	($454)	$33,182	($454)	
Sales & Services	23,077	18%	22%	122,550	127,838	5,288	127,838	**5,288**	(2)
Other	9,204	30%	27%	40,427	30,794	(9,633)	30,794	**(9,633)**	(3)
Total Revenues	44,244			196,613	191,814	(4,799)	191,814	(4,799)	
Personnel Services	(22,110)	23%	23%	(97,382)	(97,102)	280	(97,102)	280	
Supplies & Services & Capital Outlay	(17,710)	18%	20%	(93,665)	(98,807)	(5,142)	(98,807)	**(5,142)**	(4)
Total Expenditures	(39,820)			(191,047)	(195,909)	(4,862)	(195,909)	(4,862)	
Net from Operations	4,424			5,566	(4,095)	(9,661)	(4,095)	(9,661)	
Transfers In	7,081	33%	33%	5,435	21,475	16,040	21,475	**16,040**	(5)
Transfers Out	(3,248)	65%	65%	(4,575)	(5,031)	(456)	(5,031)	(456)	
Additions/(Deductions) to Unrestricted Net Assets	(700)			0	(700)	(700)	(700)	(700)	
Change in Unrestricted Net Assets	7,557			6,426	11,649	5,223	11,649	5,223	
Beginning Unrestricted Net Assets	55,648			55,648	55,648	0	55,648	0	
Ending Unrestricted Net Assets	$63,205			$62,074	$67,297	$5,223	$67,297	$5,223	
% of Operating Revenues				31.6%	35.1%		35.1%		
Total Unrestricted Net Assets				108,816	115,256		115,256		
Days of Expenditures in Total Unrestricted Funds				39	41		41		

(2) Increase due mainly to USSE budgeted initially as other revenue and will be recorded as Sales & Service revenues ($4.8M).

(3) Decrease $4.8M for USSE being reported as Sales & Services revenue, decrease $4.0M for duplicate budgeting of 5th site and lower Athletic revenue from PAC 12 of $400K.

(4) Increase due mainly to not including interest expense $4.2M not in budget, $1.0M better estimates based on current information, $675K higher spending due to plant funds moving to operating funds and increase Athletics cost for additional home game and game played in Hawaii, offset by decrease of $1.0M for items inadvertently included, duplicate USSE expense of $1.5M and better estimates based on current information totaling $740K. See docket narrative for more specifics.

(5) Increase mainly due to plant reserves moving to operating funds ($15.1M) and higher support from E&G funds ($900K).

Oregon State University

Quarterly Management Report

(Unaudited, For management purposes only)

As of September 30, 2014

For the Fiscal Year Ended June 30, 2015

(in thousands except enrollment)	YTD Actual			Budget & YE Projection					
	A	*B*	*C*	*D*		*E*	*F*	*G*	
	YTD	**YTD as a % of Projected**	**Prior 7 yr. avg. YTD %**	**Budget**	**Adjusted Budget 6/30/2015**	**Projected Variance from Budget**	**YE Projected 6/30/2015**	**Chg from prior qtr. projection**	**Notes**
RESTRICTED FUNDS									
Federal	$58,007	29%	26%	$198,975	$203,510	$4,535	$203,510	**4,535**	(6)
State	4,360	30%	26%	13,265	14,770	1,505	14,770	1,505	(6)
Other	17,349	22%	17%	75,800	79,000	3,200	79,000	**3,200**	
Total Revenues	79,716			288,040	297,280	9,240	297,280	9,240	
Personnel Services	(32,316)	27%	27%	(115,216)	(119,563)	(4,347)	(119,563)	**(4,347)**	(6)
Supplies & Services & Capital Outlay	(46,989)	26%	26%	(172,824)	(180,741)	(7,917)	(180,741)	**(7,917)**	(6)
Total Expenditures	(79,305)			(288,040)	(300,304)	(12,264)	(300,304)	(12,264)	
Net from Operations	411			0	(3,024)	(3,024)	(3,024)	(3,024)	
Transfers In	0	0%		350	30	(320)	30	(320)	
Transfers Out	(36)	31%		(1,300)	(117)	1,183	(117)	1,183	
Additions/(Deductions) to Restricted Net Assets	1			0	0	0	0	0	
Change in Restricted Net Assets	376			(950)	(3,111)	(2,161)	(3,111)	(2,161)	
Beginning Restricted Net Assets	12,546			12,546	12,546	0	12,546	0	
Ending Restricted Net Assets	$12,922			$11,596	$9,435	($2,161)	$9,435	($2,161)	
% of Operating Revenues				4.0%	3.2%		3.2%		

(6) In general, the restricted funds projection is being adjusted upward based on three year trending analysis. This is in line with the fact that research awards received in FY2014 were up $20M or 11% and the current year F&A recovery rate in E&G funds is over budget as well.

OREGON STATE UNIVERSITY **As of September, 2014**

Transfers schedule **For the Fiscal Year Ended June 30, 2015**

in 000's

			Self-Support						
		E&G	Auxiliary	Designated Operations & Service Departments.	Plant fund	Restricted	Misc.	Total
Transfers In - E&G								
			49 (d)	753 (e)	200	117		1,119
Transfers Out - E&G								
		(a)	4,549 (b)	1,796 (c)	1,274			7,619
Transfers In - Auxiliary								
	(a)	4,549		(f)	11,568			16,117
Transfers Out - Auxiliary								
		49		(g)	4,230			4,279
Transfers In - Designated Operations & Service Departments								
	(b)	1,796		(f)	3,563			5,359
Transfers Out - Designated Operations & Service Departments								
	(d)	753						753
Transfers In - Restricted								
							30	30
Transfers Out - Restricted								
		117						117

(a) mainly athletic support $4.0M

(b) transfers from E&G for supporting Designated Operations and Service Departments

(c) transfers to plant fund for remodels and space renovations

(d) mainly transfer of royalties to E&G - $653K

(e) close out plant funds

(f) moving equipment and building repair reserves from plant funds to self-support operating funds

(g) transfers from student centers to fund plant projects

FY15 Q1 Investment Reports

The Oregon State University (University) investment reports for the first quarter of FY2015 are presented in the following three sections:

- **FY15 Q1 Market Background** – This section provides a general discussion of the investment markets and related performance information during the first quarter of FY2015 (third calendar quarter of 2014).

- **FY15 Q1 Public University Fund Investment Report** – This section includes a report on the investments of the Public University Fund (P.U.F.) for the first quarter of FY2015. The P.U.F. is an investment pool that is administered by the University on behalf of all Oregon public university participants, pursuant to legislation adopted by the 2014 Legislature. The P.U.F. holds assets of all participating Oregon public universities, including Eastern Oregon University, Oregon Institute of Technology, Oregon State University, Portland State University, Southern Oregon University, and Western Oregon University, as well as the Oregon University System's Chancellor's Office.

- **FY15 Q1 Oregon State University Investment Report** – This section includes a report on the investments of the operating and endowment assets of the University. The report includes both the University's operating asset investments that are held in their entirety in the Public University Fund and the University's endowment and quasi-endowment investments, including land held as separately invested endowment funds and cash invested in a pooled endowment fund at the State Treasury.

FY15 Q1 Market Background

(Prepared by Callan Associates, Oregon Investment Council consultant)

Economic and Market Environment

Global investment markets closed the third quarter with substantial volatility, influenced in early September by the European Central Bank's (ECB's) surprise announcement of a rate cut and "Quantitative Easing (QE)", and punctuated at quarter-end by the unexpected departure of Bill Gross from PIMCO. Gross was PIMCO's Chief Investment Officer and the lead portfolio manager of the PIMCO Total Return Fund, at one point the world's largest mutual fund. While Europe just embarked on its own quantitative easing, the U.S. will see the curtain fall on QE by the end of October.

An improving U.S. economy put upward pressure on interest rates, but a significant yield advantage relative to other developed markets helped to dampen this effect. While the U.S. economy gained traction, news from Europe and Japan was far bleaker with euro zone Gross Domestic Product (GDP) barely positive in the 2nd quarter versus a U.S. reading of +4.6%. Foreign investors were lured to the relatively high yields in the U.S. market, propelling the dollar sharply higher. At quarter-end, U.S. Treasuries offered a 57 basis point premium over German bunds, a 15-year high; as investors weighed the prospects of U.S. interest rate hikes against the likelihood of more accommodative policy in the euro zone.

The ECB unexpectedly cut rates to record lows in September to spur growth and stave off deflation. Germany's economy shrank 0.2% in the 2nd quarter and euro zone inflation fell to 0.3% in September; the weakest in 5 years and well below target. Japan's economy suffered its worst contraction since 2009 with 2nd quarter GDP shrinking by an annualized 7.1% in the wake of a sales tax hike from 5% to 8%. Yields in a number of developed markets hit all-time lows with 2-year government bonds trading below 0% in eight countries after the ECB cut rates. The yield spread between U.S. Treasury and European sovereign issues are surprising with yields on both the 10-year Italian note (2.33%) and Spanish note (2.14%) below U.S. Treasuries (2.52%). The relatively attractive yields offered in the U.S. and expectations for higher rates propelled the dollar higher versus most currencies. The dollar gained 7% versus the euro and 8% versus the yen.

U.S. economic data has been quite strong of late. GDP recovered dramatically in 2Q14 after winter weather caused a 2% contraction in the 1st quarter; however, the Fed survey of real GDP growth expectations continued to trend downward toward a longer run forecast of 2%. The unemployment rate continued to decline and crept below 6% in September. Inflation readings remain benign in the U.S. with the 12 months ended in August showing a modest 1.7% rise in both headline and core Consumer Price Index (CPI). Housing was the CPI component exhibiting the most dramatic price rise (+2.6%) and accounts for more than 40% of the headline CPI calculation and more than 50% of the core CPI calculation. While CPI readings are slightly below the Fed's target of 2%, deflation risks do not appear to be a concern. Looking forward, inflation expectations dropped sharply during the quarter as evidenced by the divergence between Treasury Inflation Protected Securities (TIPS) and nominal treasuries.

Equity valuations remain moderate on a historical basis with the Standard & Poor's 500 (S&P 500) trading at 15.2x forward earnings; just below the 25 year average of 15.6X. Coincidentally, the S&P 500 peaked at 15.2x in the fall of 2007 just before the start of the Great Recession. Foreign equities appear somewhat more attractive on a valuation basis as developed markets stand at 13.9x forward earnings while emerging markets are at 10.8x.

3Q Calendar 2014 Market Performance

U.S. large caps led global equity market performance in the third quarter with declines of 1.4% in both July and September bookending a 4% rally in August that was enough to keep full quarter results positive (S&P 500 +1.1%). The strength in U.S. large cap equities masked weakness elsewhere among global equities as smaller capitalization U.S., developed foreign, and emerging markets all suffered declines in the quarter.

While local currency results showed fractional gains, major strength in the U.S. dollar relative to many foreign currencies pushed non-U.S. equity returns well into negative territory. Europe suffered big currency declines in the euro, U.K. pound, and Swiss franc. Japan also felt its currency weaken notably against the dollar as did a number of emerging market currencies.

In the U.S., large caps gained and led equity market results while midcaps drifted slightly lower (Russell Top 200: +1.7%, Russell Midcap: -1.7%). Small caps suffered acutely (Russell 2000: -7.4%) in what was the index's worst relative performance versus the S&P 500 since the late 1990's. Growth outperformed value across capitalization (Russell 1000 Growth: +1.5%, Russell 1000 Value: -0.2%, Russell Midcap Growth: -0.7%, Russell Midcap Value: -2.6%, Russell 2000 Growth: -6.1%, Russell 2000 Value: -8.6%). High quality outperformed low quality (S&P High Quality: +1.1%, S&P Low Quality: -2.0%) for the first time in over two years. Within the S&P 500, the Energy sector (-8.6%) suffered notably with falling oil and natural gas prices and gave

back most of its 2Q14 rally. Technology (+4.8%) and Health Care (+5.5%) posted the strongest gains from a sector perspective.

Developed foreign equities nearly matched the returns of U.S. large caps in local currency terms; however, significant dollar strength versus most currencies pushed returns sharply lower in U.S. dollar terms (Morgan Stanley Capital Index – Europe, Australasia, Far East (MSCI EAFE) Local: +0.9%, EAFE U.S.$: -5.9%). As in the U.S., growth outperformed value in developed markets (EAFE Growth: -5.5%, EAFE Value: -6.2%) and small caps trailed larger issues (EAFE Small Cap: -7.8%). Emerging Market (EM) equities trailed developed in local terms; however, more muted currency effects allowed EM to outperform developed in U.S. dollar terms (MSCI EM Local: +0.7%, EM U.S.$: -3.4%). On a country specific basis, Israeli equities generated the strongest returns among developed nations despite continued regional tensions (MSCI Israel: +0.2%). Portugal's equity market fell by 25% and occupied the bottom rung of the developed market performance ladder. Greece occupied the same position among emerging countries; a frequent occurrence over the past few years (MSCI Greece: -20.0%). Egypt was the best performing market globally with a 28% advance in the quarter.

Global fixed income results were mixed in the quarter. The 10-year U.S. Treasury traded in a 29 basis point range in the third quarter, hitting a low for the year (2.34%) on August 28th and an intra-quarter high of 2.63% on September 18th before closing the quarter at 2.52%. The flattening U.S. yield curve, weak foreign currencies, widening credit spreads, and falling inflation expectations led to disparate returns across bond indices.

The Barclays Aggregate Index returned 0.2% in the third quarter with U.S. Treasuries performing the best. Both corporates and mortgages underperformed like-duration Treasuries for the quarter. High yield corporate bonds sank nearly 2% as the sector endured heavy outflows amid concerns over rich valuations. Bank loans, also hit by outflows, returned -0.5% as measured by the S&P/Loan Syndications and Trading Association (LTSA) Index. TIPS underperformed nominal Treasuries by a significant margin as inflation expectations fell. The CPI dropped 0.2% in August and annual inflation has fallen short of the Fed's 2% target for 27 consecutive months. The Barclays U.S. TIPS Index fell 2.0% versus a return of +0.3% for the U.S. Treasury Index. The yield curve continued to flatten with the 30-year yield dropping 13 basis points and the 5-year yield rising 16 basis points as investors contemplated the timing of eventual rate hikes.

Hedged non-U.S. fixed income posted positive returns in the third quarter as yields dropped on anemic growth, mounting deflationary pressures and geopolitical concerns, but significant foreign currency weakness eroded returns for U.S. investors. The Barclays Global Aggregate ex-US Index returned 1.5% (hedged) while the unhedged version fell 5.4%. Emerging markets U.S. dollar-denominated debt posted small declines after rallying earlier in the year. The J.P. Morgan Emerging Market Bond Global Diversified Index returned -0.6% for the quarter. Local currency debt fell more sharply given broad-based currency weakness versus the U.S. dollar. The J.P. Morgan Global Bond Index –Emerging Market Global Diversified in local currency posted a -5.7% return for the quarter. The Russian ruble and Brazilian real fell 14% and 10%, respectively, against the dollar.

The municipal bond market posted solid returns in the third quarter, outperforming taxable bonds. The Barclays Municipal Bond Index has posted positive returns in each of the first nine months of this year, a first-time occurrence. The Barclays 1-10 Year Blend was up 0.8% (4.1% y-t-d). Lower quality again outperformed high quality for the quarter, with Baa-rated municipal

bonds up 2.2% for the quarter and 12.2% y-t-d. The most defensive sector, pre-refunded bonds, returned a meager 0.3% for the quarter and is up only 1.7% year-to-date.

Less traditional assets showed a wide dispersion of results in the third quarter. Within yield-oriented equities, Real Estate Investment Trusts (REITs) experienced a sharp slide in September that brought the quarterly return down to -3.1%. Gathering momentum from a large corporate restructuring in August, Master Limited Partnerships (MLPs) advanced 2.7% in the quarter. Commodities experienced huge volatility in the quarter and both the S&P Goldman Sachs Commodity Index (GSCI) and Bloomberg Commodities Index (BCI) fell sharply (GSCI: -12.5%, BCI: -11.8%). Grains were broadly negative with Corn (-26%) experiencing the most dramatic slide. Energy and Precious Metals also traded down sharply. Within the Hedge Fund space, early estimates indicate results around +0.5% (Hedge Fund Research Institute (HFRI) Fund Weighted Composition: +0.5%, HFRI Hedge Fund of Funds: +0.6%). Global Macro and Commodity Trading Advisors (CTAs) recovered nicely after significant weakness earlier in 2014 and posted the best results among hedge fund styles.

Closing Thoughts

As the 4th calendar quarter commences, financial markets have entered a period of heightened uncertainty. Weak growth in Europe, Japan, and much of the developing world threatens to disrupt the global economic recovery. Equities have sold off and volatility expectations have spiked as evidenced by the Volatility Index (VIX) jumping to levels not seen since late 2012. U.S. economic conditions appear stable yet growth expectations are being trimmed. Inflationary fears have tempered in the U.S. while Europe is struggling to fend off deflationary concerns and Japan continues to try to manufacture whatever inflation it can. Given continued uncertainty, Callan recommends prudent asset allocation and risk assessment based on future capital needs for both plan sponsors and individual investors.

FY15 Q1 Public University Fund Investment Report

(Prepared by the P.U.F. Administrator)

Performance

The Public University Fund's quarterly total return was 0.2% (including unrealized gains/losses). During the quarter, both the Intermediate-Term Pool and the Long-Term Pool exceeded the performance of their respective benchmarks.

	Quarter Ended 9-30-14	Prior Fiscal YTD	Current Fiscal YTD	3 Year Avg	Market Value	Asset Allocation	Policy Allocation
Oregon Short –Term Term Fund	0.1%	0.1%	0.1%	0.6%	$ 207,846,155	51.3%	$150 million minimum
Benchmark 91 day T-Bill	*0.0%*	*0.0%*	*0.0%*	*0.1%*			
Oregon Intermediate - Term Pool	0.2%	0.8%	0.2%		$ 91,029,579	22.5%	$300 million maximum
Benchmark BAML 1-5 yrs US Corp & Govt A & Above	*-0.1%*	*0.7%*	*-0.1%*	*1.3%*			
OUS-PUF Linked Return				*3.0%*			
PUF Long Term Pool	0.3%	0.8%	0.3%		$ 106,020,053	26.2%	$120 million maximum
Benchmark BAML 5-7 yrs US Corp & Govt AA & Above	*-0.1%*	*0.6%*	-0.1%	*1.4%*			
OUS-PUF Linked Return				*2.8%*			
Public University Fund	0.2%	0.5%	0.2%		$404,895,787	100%	

Investment Income and Participant Ownership

During the quarter, investment earnings distributed to the participants totaled $1,490,187.

	Income Distribution	Market Value	% Ownership
Oregon State University	$ 567,863	$ 158,516,400	39.1%
Portland State University	314,184	103,749,215	25.6%
Western Oregon University	114,973	38,382,457	9.5%
Southern Oregon University	53,483	21,400,489	5.3%
Oregon Institute of Technology	59,932	16,865,405	4.2%
Eastern Oregon University	35,001	6,142,981	1.5%
Chancellor's Office	65,896	59,838,841	14.8%
OUS Internal Bank *(income earned during June 2014)*	278,855	N/A	N/A
Grand Total	$ 1,490,187	$ 404,895,787	100%

FY15 Q1 Oregon State University Investment Report

(Prepared by the University Shared Services Enterprise)

The schedule of Oregon State University's investments is shown in the investment summary below.

Public University Fund Performance

Oregon State University has invested its operating assets in the Public University Fund (P.U.F.). The report on the investment performance of the P.U.F., provided in the separate section above, shows that the P.U.F. returned 0.2% for the quarter.

Pooled Endowment Fund Performance

(*Prepared by Oregon State Treasury*)

Oregon State University has invested its endowment and quasi-endowment assets in the Higher Education Endowment Fund managed by the Oregon State Treasury. The Higher Education (HIED) Endowment Fund (Pooled Endowment Fund) returned 0.2% for the quarter and 13.6% over three years. This three-year performance was approximately 100 basis points above the policy benchmark return of 12.6%.

While equity markets suffered through a flat to down quarter, both the domestic and non-US public equity managers have demonstrated good performance over the trailing three year period. The Blackrock S&P 500 Index returned 23% while Arrowstreet Capital posted nearly a 20% return for three years. On a relative basis, Arrowstreet Capital exceeded its benchmark by 630 basis points for the three year period. On the domestic equity side, Columbia Acorn continued to struggle versus the Russell 2500 benchmark, given their growth-at-a-reasonable-price stock picking approach.

The fixed income mandate, managed by Western Asset, delivered a flat return for the quarter and 5% over the three year period.

For the five-years ended June 30, the fund returned an average of 11.2% annually, 94 basis points above the policy benchmark.

At the end of the quarter, most every manager was downsized or eliminated, to create liquidity for the departure of the University of Oregon from the pool. While we have been able to maintain an overall asset allocation consistent with the OIC's primary targets (i.e., growth assets, inflation hedging, and diversifying assets), the composition of the inflation hedging allocation has shifted with a greater weight towards the TIPS allocation. The portfolio is well positioned in the event that other schools opt to leave the pool.

Staff Recommendation to the Committee

Staff propose that the Board of Trustees' Finance and Administration Committee accept the FY15 Q1 Public University Fund Investment Report and the FY15 Q1 Oregon State University Investment Report.

Oregon State University

Investment Summary

as of September 30, 2014

(Net of Fees)

	Quarter Ended 9-30-14	Prior Fiscal YTD	Current Fiscal YTD	3 Yr Avg	5 Yr Avg	10 Yr Avg	Market Value	Actual Asset Allocation	Policy Allocation Range
OSU Operating Assets Invested in Public University Fund									
Oregon Short Term Fund	0.1%	0.1%	0.1%	0.6%	0.6%	2.1%	$ 81,371,615	51.3%	[1]
Benchmark - 91 day T-Bill	*0.0%*	*0.0%*	*0.0%*	*0.1%*	*0.1%*	*1.6%*			
Oregon Intermediate Term Pool	0.2%	0.8%	0.2%				35,638,013	22.5%	[1]
Benchmark BAML 1-5Yrs US Corp & Govt A & Above	*-0.1%*	*0.7%*	*-0.1%*	*1.3%*					
[2] *Combined Historical Returns*				*3.0%*	*N/A*	*N/A*			
P.U.F. Long Term Pool	0.3%	0.8%	0.3%				41,506,772	26.2%	[1]
Benchmark BAML 5-7Yrs US Corp & Govt AA & Above	*-0.1%*	*0.6%*	*-0.1%*	*1.4%*					
[3] *Combined Historical Returns*				*2.8%*	*N/A*	*N/A*			
Total Public University Fund Investment	0.2%	0.5%	0.2%				$ 158,516,400	100.0%	
OSU Endowment Assets Invested in Pooled Endowment Fund									
Total Pooled Endowment	0.2%	6.0%	0.2%	13.6%	11.2%	6.9%			
[3] Target Alloc Policy Benchmark	*-0.6%*	*4.9%*	*-0.6%*	*12.6%*	*10.2%*	*6.9%*			
Growth									
BlackRock S&P 500 Index	1.1%	5.3%	1.1%	23.0%	15.8%	N/A	$ 4,815,500	13.1%	
Benchmark - S&P 500 Stock Index	*1.1%*	*5.2%*	*1.1%*	*23.0%*	*15.7%*				
Columbia Acorn	-5.4%	10.4%	-5.4%	18.3%	13.6%	N/A	690,683	1.9%	
Benchmark - Russell 2500 Index	*-5.4%*	*9.1%*	*-5.4%*	*22.8%*	*16.0%*				
Arrowstreet Capital	-4.0%	12.8%	-4.0%	19.5%	12.5%	N/A	4,554,527	12.4%	
Benchmark - MSCI World Ex US IMI Net	*-6.1%*	*11.8%*	*-6.1%*	*13.2%*	*6.8%*				
Genesis Asset Management	-4.2%	5.9%	-4.2%	10.1%	8.3%	N/A	1,216,017	3.3%	
Benchmark - MSCI Emerging Markets IMI Net	*-3.2%*	*5.5%*	*-3.2%*	*7.5%*	*4.7%*				
BlackRock ACWI IMI B	-2.7%	8.4%	-2.7%	17.2%	N/A	N/A	73	0.0%	
Benchmark - MSCI ACWI IMI Net	*-2.8%*	*8.3%*	*-2.8%*	*16.7%*					
HRJ Growth Capital II	5.5%	2.0%	5.5% [4]				1,693,472 [4]	4.6%	
Benchmark - Russell 3000+300 bps Qtr Lag	*5.6%*	*3.4%*	*5.6%*						
JP Morgan Venture Capital IV	3.5%	3.2%	3.5% [4]				2,163,107	5.9%	
Benchmark - Russell 3000+300 bps Qtr Lag	*5.6%*	*3.4%*	*5.6%*						
Total Growth							15,133,379	41.2%	50%-75%

(Continued on next page)

Oregon State University

Investment Summary

as of September 30, 2014

(Net of Fees)

	Quarter Ended 9-30-14	Prior Fiscal YTD	Current Fiscal YTD	3 Yr Avg	5 Yr Avg	10 Yr Avg	Market Value	Actual Asset Allocation	Policy Allocation Range
Diversifiers									
Western Asset Core Plus Bond Fund	0.1%	0.6%	0.1%	4.9%	7.1%	5.8%	5,044,647	13.7%	
Benchmark - BC Aggregate Index	*0.2%*	*0.6%*	*0.2%*	*2.4%*	*4.1%*	*4.6%*			
Cash	0.1%	0.1%	0.1%	0.6%	0.6%	2.1%	13,120,967	35.6%	
Benchmark - 91 day T-Bill	*0.0%*	*0.0%*	*0.0%*	*0.1%*	*0.1%*	*1.6%*			
Total Diversifiers							18,165,614	49.3%	20%-30%
Inflation Hedge									
Capital Dynamics GRE III	2.5%	2.7%	2.5% [4]				1,016,063 [5]	2.8%	
Benchmark - Russell 3000+300 bps Qtr Lag	*5.6%*	*3.4%*	*5.6%*						
Morgan Stanley Prime Property Fund	3.8%	3.9%	3.8%	N/A	N/A	N/A	241,397	0.7%	
Benchmark - NCREIF Property Index Qtr Lag	*2.9%*	*2.9%*	*2.9%*						
BlackRock TIPS NL B	-2.1%	0.8%	-2.1%	1.3%	N/A	N/A	2,188,335	6.0%	
Benchmark - BC TIP Index Total Return	*-2.0%*	*0.7%*	*-2.0%*	*1.3%*					
Total Inflation Hedge							3,445,795	9.5%	7%-20%
Endowment Fund Payable							(6,247) [6]	0.0%	
Total Pooled Endowment Fund Investment							36,738,542	100.0%	
Land Held as Separately Invested Endowment Funds							2,693,002 [7]		
Total Endowment Funds							$ 39,431,544		

1 The Public Unversity Fund (P.U.F.) policy guidelines define investment allocation targets based upon total participant dollars committed. Core balances in excess of liquidity requirements for the participants are available for investment in the Intermediate-Term Pool and the Long-Term Pool. Maximum core investment allocations are determined based upon anticipated average cash balances for all participants during the fiscal year.

2 The historical returns presented combine the investment returns from the predecessor fund with the investment returns of the P.U.F., for investments with an identical mandate. The predecessor fund commingled all public universities operating assets into a cash and investment pool.

3 Notes on Policy Benchmark: From November 2012 to current the policy benchmark is 25% Russell 3000, 25% MSCI ACWI Ex US, 25% BC AGG, 10% Russell 3000 +300bps, 7.5% BC Treasury Inflation Protection Index, and 7.5% NCREIF Index.

4 Estimated total return as calculated by University Shared Services Enterprise staff as ((ending balance + sales - costs - contributions)/beginning balance)-1).

5 Value based on equity method of accounting as of September 30, 2014, adjusted for capital contributions and distributions through September 30, 2014.

6 Outstanding payables deducted from market value to derive net Pooled Endowment balance.

7 Physical appraisals completed every five years, with last physical appraisals completed in fy 2012 and 2014 for the two separate forest lands. Valuations in interim years provided by faculty. Land held as separately invested endowments may not be sold. Land use is restricted to teaching and research. Partial harvests, consistent with good forestry management practices are allowed, with specified uses for ongoing funding for scholarships and an endowed chair.

Note: Outlined returns underperfomed their benchmark.