

The University of Houston System Non-Endowed Investments



FISCAL YEAR 2009

DECEMBER 31, 2008

Market Overview

Treasury yields were lower again in December as worries about the credit crisis continued into year end. Weak holiday sales, falling home prices, and further job loss worries all contributed to a strong demand for Treasury securities leading to higher prices and lower yields. The Treasury yield curve flattened as shorter-term yields had little room to fall further, while long-term yields continued their decline. The three-month Treasury yield remained near zero throughout the month as fearful investors continue to forego potentially higher returns elsewhere in exchange for preservation of principal.

The broader fixed income market, as measured by the Barclays Capital Bond Index, returned 3.73% and 4.58% for the month and the quarter, respectively, ending December.

Inflation & Interest Rates

The Consumer Price Index for All Urban Consumers (CPI-U) decreased 1.0% in December. Meanwhile, the core CPI, which excludes food and energy, was unchanged after no change the month before. Year-on-year, the core rate is up 1.7%, compared to up 2.0% in November.

The Federal Open Market Committee (FOMC) lowered rates at their December meeting, bringing the Fed Funds rate to a range of 0% to 0.25%, a historically low level. Since their easing cycle began in September 2007, the Fed Funds rate has declined by 5.0%.

Total Cash and Short-Term Investments

As of December 31, 2008, total non-endowed funds for UH System have a market value of \$271.6 million excluding the \$39.3 million (market value) invested in the endowment fund and \$75.3 million in bond proceeds used for construction projects.

Investment Allocation

The current allocation of the non-endow funds is 47% to the cash pool consisting of money market funds and sweep investments, 40% to the liquidity pool consisting of fixed income, and 13% to the core pool which is invested in the endowment.

Investment Performance

As shown in the first graph below, although the \$125 million fixed income portfolio managed by JPMorgan Chase has underperformed its benchmark for the month and quarter for December, it significantly outperformed its benchmark by 232 basis points year-to-date. The second graph below shows the asset allocation of the portfolio for the most recent and prior quarter. The manager has trimmed its allocation to agencies over the quarter and reinvested the money in treasuries. The manager began purchasing the first of the FDIC guaranteed bank debt issued under the Temporary Liquidity Guarantee Program (TLGP) in late November and December. The \$147 million in money market funds are yielding 1.32% annualized, which outperformed the Merrill Lynch 91-Day Treasury Bill Index of 0.12% annualized.

