

The University of Houston System Non-Endowed Investments



FISCAL YEAR 2008

FEBRUARY 29, 2008

Market Overview

Concerns about the economy continued in February. The further slide in housing activity, a sharp decline in consumer confidence, and another rise in inflation all impacted investor confidence. Inflation fears took yields higher for most of February, but the sell-off was reversed late in the month on poor US economic activity data and a downbeat assessment from the Fed. The fixed income market, as measured by the Lehman Aggregate Bond Index, was up 0.1% for the month of February.

Treasury Yield

Treasury yields were lower in February as market participants attempted to ascertain the consequences of financial market volatility, a housing-led economic slowdown and Federal Reserve interest rate cuts.

Interest rates moved lower on short-to-intermediate maturities, but drifted higher on longer-dated Treasury bonds as increased inflation expectations dragged yields higher. The yield curve retained its normal shape.

Inflation & Interest Rates

The Consumer Price Index for All Urban Consumers (CPI-U) increased 0.3% in February. On a seasonally adjusted basis, the CPI-U was virtually unchanged in February. The Federal Open Market Committee (FOMC) took a break from their easing cycle in February. However, on March 17th, the Fed urgently cut the discount rate by 25 basis points from 3.5% to 3.25%. Then during the FOMC meeting held on March 18th, The Fed cut both the Fed Funds rate and the discount rate by another 75 basis points. The Fed Funds rate and the discount rate is now 2.25% and 2.5%, respectively.

Total Cash and Short-Term Investments

As of February 29, 2008, total non-endowed funds for UH System have a market value of \$250.3 million *excluding the \$60.7 million invested in the endowment fund*. This \$250.3 million represents a decrease of \$59.7 million as compared to the month ending January 2008. The decrease is due to a transfer of \$16.9 million to the endowment fund in February and the use of money market funds to support ongoing cash flow needs of the system components including UH's purchase of the McGregor property and temporarily funding other capital projects.

Investment Allocation

We have completed the reallocation of the non-endowed funds to the cash, liquidity and core pools. This effort has targeted the reallocation of these funds as follows: 40% to the cash pool consisting of money market funds, 40% to the liquidity pool consisting of fixed income, and 20% to the core pool which is invested in the endowment.

Investment Performance

For the month, the money market funds are yielding 0.28% (or 3.41% annualized), which outperformed the Merrill Lynch 91-Day Treasury Bill Index of 0.15% (or 1.80% annualized). The Enhanced Cash Portfolio outperformed the Merrill Lynch 1-5 year Government/Credit Index return by 5 basis points for February. The first graph below compares the longer term returns of the fixed income portfolio to its benchmark. The second graph shows the asset allocation of the portfolio for the most recent and prior quarter.

