The University of Houston System
Non-Endowed Investments

FISCAL YEAR 2008 | JUNE 30, 2008

Market Overview

Bond yields were slightly lower in June. The market's recent activity stems from concerns over a slowing economy and continued financial market volatility, as well as rising inflation expectations. Treasury yields were slightly lower and volatile during June. The broader fixed income market, as measured by the Lehman Aggregate Bond Index, returned -0.1% and -1.0% for the month and quarter, respectively, ending June.

Inflation & Interest Rates

The Consumer Price Index for All Urban Consumers (CPI-U) increased 1.0% in June. The core CPI, which excludes food and energy, firmed to a 0.3% increase after a 0.2% rise in May. The consensus had forecast a 0.2% rise. Year-on-year, the core rate edged up to up 2.4%, compared to up 2.3% in May. Higher energy and food prices are clearly boosting inflation and now there are signs of seepage into the core.
The Fed held interest rates steady at June's Federal Open Market Committee (FOMC) meeting, their first without a rate cut since last summer. The FOMC statement highlighted diminished concerns over economic growth and heightened concern over rising inflation expectations, indicating that an interest rate increase may be its next move. Fed Funds futures are increasingly pointing to higher rates by the end of 2008.

Total Cash and Short-Term Investments

As of June 30, 2008, total non-endowed funds for UH System have a market value of $244.9 million *excluding the $56.1 million (market value) invested in the endowment fund*. This $244.9 million represents a decrease of $22.1 million as compared to the month ending May 2008.

Investment Allocation

The current allocation of the non-endow fund is 42% to the cash pool consisting of money market funds, 39% to the liquidity pool consisting of fixed income, and 19% to the core pool which is invested in the endowment. The target allocation is 40%, 40%, and 20% to the cash, liquidity, and core pools, respectively.

Investment Performance

The money market funds are yielding 2.39% annualized, which outperformed the Merrill Lynch 91-Day Treasury Bill Index of 2.16% annualized. The Enhanced Cash Portfolio outperformed the Merrill Lynch 1-5 year Government/Credit Index return by 21 basis points for June. However, it underperformed the benchmark for the quarter by 16 basis points last month. 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.