The Regents of the University of California

INVESTMENTS COMMITTEE
March 21, 2024

The Regents of the University of California met on the above date at the Luskin Conference Center, Los Angeles campus.

Members present: Regents Cohen, Ellis, Makarechian, Matosantos, Park, Robinson, and Sherman; Ex officio members Drake and Leib; Chancellors Khosla and Wilcox

In attendance: Regents Hernandez, Kounalakis, Raznick, and Tesfai, Regent-designate Beharry, Secretary and Chief of Staff Lyall, Chief Investment Officer Bachher, Chancellors Muñoz and Yang, and Recording Secretary Li

The meeting convened at 2:10 p.m. with Committee Chair Robinson presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of November 16, 2023 were approved, Regents Cohen, Drake, Ellis, Matosantos, Robinson, and Sherman voting "aye."

2. **REVIEW OF PERFORMANCE FOR THE SECOND QUARTER OF FISCAL YEAR 2023–2024 OF UC PENSION, ENDOWMENT, BLUE AND GOLD POOL, WORKING CAPITAL, AND RETIREMENT SAVINGS**

[Background material was provided to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Chief Investment Officer (CIO) Bachher stated that students from the UC Investments Academy would present their experiences to the Committee.

Craig Huie, Managing Director of Private Credit, reported that over 2,000 students from nine UC campuses were involved in the UC Investments Academy. In November, over 300 students attended the UC Investments Academy Symposium held at UC Merced, and among the 15 guest speakers were Regent Park, Chancellor Muñoz, and Executive Vice President and Chief Financial Officer Brostrom. Mr. Huie thanked the Regents for supporting this initiative.

Lara Ibraheem, a UC Davis student, shared that she was an Iraqi immigrant and first-generation college student studying managerial economics and technology management. Previously, she had worked for legislators and at consulting firms, but after joining the Academy, the Office of the CIO team connected her with people in the investment industry and offered valuable advice about optimizing her internship at a global investment firm.

She later introduced Girls who Invest, a nonprofit organization helping women gain entry into asset management, to UC Davis. Ms. Ibraheem planned to attend business school and pursue venture capital work. She expressed gratitude to the UC Investments Academy.

Tatiana Howell, a UC Merced student, shared that she was born in Fresno, California and was studying sociology and business economics. She emphasized the importance of UC Merced in the Central Valley. Ms. Howell participated in the first ever cohort of the UC Investments Academy, through which she received mentorship, exposure, knowledge, and opportunities and became a charter member of the Phi Alpha chapter of the historically Black sorority Delta Sigma Theta. In fall 2022, Ms. Howell became an intern at the Export-Import Bank of the United States through the UC Washington Center. In summer 2023, she participated in an internship at Abrdn, a global asset management firm, and a career exposure program hosted by TIAA Financial Services. This summer, she would be interning at Goldman Sachs. Ms. Howell was grateful for the support provided by UC Merced and the UC Investment Academy; she thanked the Office of the CIO team.

Grace Tang, a UCLA student, shared that she had moved to Seattle, Washington from Shanghai, China and was majoring in economics and communications. She was currently working at Morgan Stanley and later as a summer analyst at the Office of the CIO. Next summer, she planned to work in investment banking in New York. It was difficult to break into a relatively homogeneous industry as a female from an immigrant family. She has signed up to join the UC Investments Academy and believed that it would best prepare her for both her summer internships and her future career. Ms. Tang was excited to learn more technical skills and how to become a confident, flourishing professional in this industry.

Mr. Bachher shared that he and President Drake planned to create a fellowship for 20 UC students that would teach targeted entrepreneurship and finance skills. President Drake clarified that this fellowship was meant for undocumented students. Mr. Bachher shared his plan to launch the fellowship in the summer.

Mr. Bachher then introduced Dennis Slamon, Director of Clinical/Translational Research and Director of the UCLA Women's Cancer Research Program. Dr. Slamon led the development of Herceptin, a cancer drug that was now the standard of care for breast cancer.

Dr. Slamon stated that the University's research mission, which has benefited people across the globe, took finance to maintain. He asked how the University was optimizing or not optimizing the intellectual property (IP) it generated. In the past, industry licensed UC clinical research for further development and would bring the resultant new drugs or therapeutic approaches back to UC medical centers for testing. If that further development occurred within the UC system, the intellectual property would have greater value than if it is licensed at the earliest possible point. Dr. Slamon's discussions with Mr. Bachher years ago about starting a company for this type of development within the University later became Translational Oncology Research Laboratory (TORL) Biotherapeutics at UCLA, using a model that could be replicated at other UC campuses. The University not only collected royalties from its early IP, but the assets could also be later auctioned to industry partners. Friends of the University, a political action committee that advocates for UC, suggested a venture philanthropy concept to attract investors and seeded the initial $50 million, which enabled clinical testing of new drugs for cancer and other unmet medical needs. Without going public, TORL was able to attract over $316 million in Series B funding. TORL was based in the University, and clinical research was executed by UC clinicians and independent faculty. The Office of the CIO had made TORL's first big Series B investment, which drew the attention of major private funds, Goldman Sachs, Bristol Myers Squibb, Vertex Pharmaceuticals, and Parexel. Five new drugs were now in clinical testing. TORL was unique in the country, but Dr. Slamon believed that all UC medical campuses could explore this opportunity.

Committee Chair Robinson asked whether TORL's IP assets were coming from non-UC laboratories. Dr. Slamon replied that assets were coming from UCLA, but this model was transferable to other places. TORL's first round of Series B funding was oversubscribed, as investors were attracted to TORL's effectiveness and efficiency resulting from its ability to conduct clinical trials with existing infrastructure. The company has since opened a second round of Series B funding.

Mr. Bachher praised this revolutionary model and encouraged the Regents to visit TORL. He predicted that it would bring tremendous royalties back to UCLA.

Mr. Bachher stressed how much has occurred globally since the last Committee meeting and presented a list of the Office of the CIO's major concerns. Artificial intelligence (AI) was now playing a significant role in the financial markets, as well as climate change and energy transition. A potential future power shortage presented not only a great risk but also a great opportunity to generate more and cleaner power to run the new technology being developed. Demographics were having an effect on some countries' ability to add to their workforces. Another concern was deglobalization due to an interest in domestic production and two wars. Global events affected UC investments even though three-quarters of those investments were in North America, and most in the U.S.

Mr. Bachher reflected on investment performance in the ten years that he has been with the University, noting the positive performance of investments in both the U.S. and India. He also made note of the COVID-19 pandemic. In the last 30-year period, growth was slow in the first two decades and accelerated in the last decade. As of December 31, 2023, UC investments assets stood at $169 billion and currently stood at $178 billion. Working capital stood at about $15 billion. The endowment, which stood at $27.7 billion, had grown due to capital inflows from working capital and the markets. Currently, the pension stood at $95 billion. Over the last 30 years, the General Endowment Pool (GEP) has grown at about 8.7 percent per year, the pension at about eight percent per year, and the Short Term Investment Pool (STIP) at about 3.6 percent per year. In the last year, the Blue and Gold Pool has grown 18.6 percent. Mr. Bachher presented a chart of fiscal-year-to-date returns. Currently, 90 percent of UC assets were managed through 30 key relationships, which meant that UC was paying $30 billion less in fees. In the last ten years, passive investments have increased from $30 billion to $120 billion and active investments have decreased from

$65 billion to $49 billion. The Office of the CIO charged only two basis points, compared with fee structures of 25 to 50 basis points elsewhere in the industry.

Senior Managing Director Satish Ananthaswamy stated that, this time last year, three banks had failed and markets were predicting a recession, but the Office of the CIO believed that the economy would be fine as long as new jobs were being added and the Federal Reserve (Fed) was combating inflation. Markets later began to reprice, and economic growth in 2023 was ultimately three percent. Inflation came down to more manageable levels, and the equity market emerged from its trough. The Standard and Poor's (S&P) 500 was now up 33 percent and the NASDAQ was now up 45 percent. The previous day, in an unprecedented move, Federal Reserve Chair Jerome Powell increased growth and inflation prospects and signaled the Fed's readiness to cut interest rates. While inflation would decrease, it would not reach two percent as previously projected. The U.S. fiscal deficit increased by $1 trillion in 2023.

Mr. Ananthaswamy explained how the U.S. economy survived the prior year's turmoil. Although the U.S. fiscal deficit increased to $2 trillion in 2023, the Inflation Reduction Act and the CHIPS Act enabled significant investment in structures. Many data centers, facilities, and warehouses were built, and the Fed increased interest rates from zero to 5.5 percent. Although the U.S. had a low inventory of housing due to underinvestment and a lower mortgage rate of 3.5 percent for 80 percent of homeowners, the housing market was still strong. The Fed was discussing the prospect of rate cuts to prevent a recession. Otherwise, the Treasury would have to issue enormous amounts of debt to fund the deficit. Globally, equity markets were performing strongly. Chinese equities were slowing down, but Japanese equities were doing well, and India was showing strong economic growth. The Office of the CIO believed that global equities would provide a higher return than fixed income and preferred to take a long position in equities and avoid buying duration in fixed income. In order to fund the deficit, the U.S. Treasury would eventually have to issue longer-duration coupon bonds, and inflation could become an issue if the Fed cuts interest rates, so the Office of the CIO wished to maintain a shorter duration. Mr. Ananthaswamy believed that the U.S. has exited the low-rate, low-growth, and low-return environment.

Mr. Bachher stated that growing income inequality has had an impact on populism. Auto loans and consumer credit card debt were growing at higher rates now than during the global financial crisis. Fidelity had the highest number of 401(k) retirement accounts with more than $1 million but also had the highest number of hardship withdrawals from such accounts. In India, growth in companies that make consumer goods was flat, anemic, or declining. Common prosperity was also an issue in China. Four billion people around the world would vote this year. The U.S. gross domestic product (GDP) has grown $10 trillion in the last ten years, but the combined market capitalization of the top ten companies has grown from $1 trillion $14 trillion in that time. Mr. Bachher predicted that the speed of change of innovation through the use of AI would surpass past innovation cycles. Private AI companies were valued at a total of $250 billion and did not make a large impact on market capitalization. The top ten companies, however, held cash and cash equivalents of $750 billion. If the earnings of these companies were to slow down, there could be more turmoil in the markets.

In response to a question from Regent Leib, Mr. Bachher noted that OpenAI was valued at $100 billion, and the total venture capital invested into AI companies was about $60 billion.

Regent Makarechian remarked that the valuation depended on how one defined AI, citing Nvidia as an example. Mr. Bachher clarified that he was counting private companies. Nvidia has grown 24,000 percent. In comparison, Berkshire Hathaway has only grown 200 percent in the same time period. Public companies driven by AI were growing at a much faster rate. In the last four years, the top ten companies have grown 200 percent each.

Regent Matosantos stated that she had trouble reconciling the risk of running out of power and the concern about demographics with the strength of the global equities market and overall optimism. Mr. Bachher underscored that predictions tend to be wrong most of the time. Inflation was sticky, but a good effort has been made to bring it down from nine percent. Still, interest rates were likely to remain higher. In his view, Mr. Powell's remarks seemed to acknowledge the upcoming presidential election. With regard to equities, investors seemed to be very excited about AI's potential. With regard to power, energy was needed to run computers and electric vehicles. The two-year time horizon was suggested by chief executive officers of data center companies.

Mr. Bachher presented a table of the University's asset allocation as of December 31. Out of a total of $169 billion, about $91 billion was invested in the stock market, about $35 billion in the bond market, about $35 billion in private assets, and about $7.6 billion in cash and cash equivalents. UC investments have remained overweight in equities and benefited from their rise. There was much noise in the markets, but Mr. Bachher believed that UC was positioned well, and the Office of the CIO would be cautious.

Regent Makarechian noted the counterintuitive nature of the current environment. High interest rates have not affected the housing markets or corporate borrowing, and the Fed projected interest cuts despite inflation. He stated his understanding the Office of the CIO paid out about $1.5 billion every year. Mr. Bachher replied that this was correct.

In Regent Makarechian's view, the Committee and the Office of the CIO ought to focus investments on what would actually take place in the future, such as the need for faster computer chips and energy, beyond the buzz surrounding things like AI. Lawrence Livermore National Laboratory's graph of U.S. energy production and consumption could serve as a map for investments. There was a percentage of electricity that was produced but not used. Regent Makarechian suggested further discussion of things that concern the Office of the CIO, distinguishing calls for divestment from UC's obligations, and bringing in advisors to speak to the Committee. Mr. Bachher replied that the Office of the CIO was trying to gather insights from experts and could bring these experts to Committee meetings or some other type of event.

The meeting adjourned at 3:30 p.m.

Attest:

Secretary and Chief of Staff