The Regents of the University of California

INVESTMENTS COMMITTEE
May 14, 2024

The Investments Committee met on the above date at the UC Merced Conference Center, Merced campus and by teleconference conducted in accordance with California Government Code §§ 11133.

Members present: Regents Ellis, Makarechian, Matosantos, Park, Robinson, and Sherman; Ex officio member Leib, Advisory member Steintrager; Staff Advisor Mackness

In attendance: Regents Hernandez and Tesfai, Regent-designate Beharry, Faculty Representative Cheung, Secretary and Chief of Staff Lyall, Deputy General Counsel Woodall, Chief Investment Officer Bachher, Executive Vice President and Chief Financial Officer Brostrom, Interim Senior Vice President Reese, Vice President Kao, Chancellor Muñoz, and Recording Secretary Li

The meeting convened at 12:10 p.m. with Committee Chair Robinson presiding.

1. **PUBLIC COMMENT**

Committee Chair Robinson stated that the University of California valued freedom of speech and viewed individual rights to free expression as key to the open discourse that is vital within higher education. The University sought to make room for all perspectives, and the upcoming public comment period would operate with these freedoms in mind, during which speakers would be given the opportunity to share their viewpoints. Given that some comments might elicit disagreement, the Board asked that all in attendance allow everyone an equal opportunity to express their opinions. The Board would not permit a response of protest that is disruptive, silences other speakers, or prevents the orderly conduct of the meeting. Disruption of this magnitude might require that the public comment period conclude and disrupting individuals be escorted from the venue and possibly subject to arrest. It was the goal of the Board to have a peaceful and respectful public comment period.

Committee Chair Robinson explained that the public comment period permitted members of the public an opportunity to address University-related matters. The following persons addressed the Board concerning the items noted.

A. Madeeha Ashraf, UC Berkeley alumna, urged the Regents to meet the demands of pro-Palestinian protesters calling for divestment and amnesty. She did not believe their demands were controversial; all public institutions should strive for transparency in their investments and should divest from organizations that profit from weapons, killing, and oppression. UC had previously divested from fossil fuels in 2020. Ms. Ashraf noted that students putting their futures at risk should be taken seriously, and she called for the liberation of Palestine.

B. Joel Hass, UC Davis professor, addressed antisemitism at UC. He stated that UC Davis was using its $700,000 allocation of the $7 million President Drake dedicated to address extremism and bias to fund collaborations with groups such as Students for Justice in Palestine, which Mr. Hass regarded as an extremist hate group. He stated that systemic antisemitism dominated certain departments and thrived in areas with strong radical activism.

C. Maribel Lugo, UC Merced staff member, urged the Regents to consider a wage increase for teachers at the UC Merced Early Childhood Education Center (ECEC) to ensure fair and equitable compensation. In the last year, three teachers have left ECEC to take other positions with better pay. The remaining teachers were overworked and underpaid, and only two positions were recently backfilled. UCM childcare teachers supported faculty, staff, student families, and the community.

D. Sergey Sikora, UCLA alumnus, stated that Al-Qaeda banners were waved during a Students for Justice in Palestine rally at UC San Diego and suggested that this be referred to federal authorities so that potential Al-Qaeda members at UCSD could be identified. Mr. Sikora, citing Regents Policy 2301: Policy on Course Content, called for the dismissal of a faculty member who called for a strike in support of Palestine on October 8 and gave credit to students who attended a pro-Hamas rally. He also called for the suspension of Students for Justice in Palestine activities while their links to Al-Qaeda are investigated.

E. Allison Calistro-Yazzie, UC Merced staff member and member of Teamsters Local 2010, asked Chancellor Muñoz and the Regents about UC Merced's staff retention efforts and questioned why the ECEC staff were not making at least $25 per hour. She added that these staff held some of the lowest paid positions while inflation was at an all-time high, contrasting their pay with that of childcare workers at UC Berkeley, UC Santa Cruz, and UC San Diego. Ms. Calistro-Yazzie declared that competitive pay makes employees stay.

F. Samir Al-Alami, UC Riverside alumnus, demanded full divestment from companies such as Elbit Systems, Amazon, and Google, adding that UC must act as it has done in 1968, 1994, and 2020. He stated that, through these investments, the University was complicit in a genocide of his community. Mr. Al-Alami shared that he would not establish a scholarship at UCR until UC fully divests.

G. Abigail Thompson, UC Davis professor, stated that the vast majority of UC Davis' allocation of the $7 million dedicated to addressing antisemitism, Islamophobia, and extremism excluded the mainstream Jewish viewpoint, promoted anti-Zionism, and exacerbated destructive antisemitism. She stated that nearly $500,000 has been used support anti-Zionist activists, students, faculty, such as funding two groups to collaborate with Students for Justice in Palestine, the driving force behind nearriots, criminal vandalism, and harassment of Jewish people on campus. Ms. Thompson quoted a social media post made by the vice president of Students for Justice in Palestine and equated it to the dehumanizing language of the pogrom.

H. Holly Yu, UC Merced student and intern at Power California, asked the Investments Committee to divest from companies that support the genocide of Palestinian people. She stated that UC used taxpayer money to support Israel's operations. She understood the impact of institutions harming people instead of keeping them safe because of her experience with the Oakland Unified School District funding school police instead of the well-being of its students. She urged the Regents to listen to students and to stand in solidarity with them.

I. Fatima C., UC Irvine alumna, called on the Regents to divest from Israel and to stop profiting from the genocide in Gaza. This included the UC Retirement Plan, the endowment, and the campus foundations. She criticized the University's holdings in Blackrock, the largest investor in weapons manufacturing in the U.S., and Lockheed Martin, the largest defense contractor in the world.

J. Jagadeesh Nalluri asked the Regents to address irrationalities in the residency requirements for tuition purposes. He stated that a dependent nonresident student living in California with a resident parent would be admitted to UC as a California resident but would be considered a nonresident after reaching 18 years of age. A dependent student who did not attend high school in California and had separated parents, one of whom is a California resident, would also be considered a resident. This was not the case if the students' parents were married but lived separately.

K. Darlene Lee, UCLA alumna and faculty member, expressed support for students and faculty in the protest encampments as well as their call for divestment from the military-industrial complex. She stated that educational funds should go toward education and community, not war. Ms. Lee condemned police brutality that students and faculty experienced at UCLA and supported amnesty for students, faculty, and staff in the encampments.

L. Hadiya Manzoor, UC alumna, stated that students' right to protest was being repressed. Students were being brutalized by police and had lost their right to freely negotiate with the administration about how funding is used. She stated that students and faculty should have access to information about investments in the endowments and should be able to exercise control over that money. She added that the Board of Regents was not democratically elected and was motivated by business interests.

M. Lilianna Calitto, UC Davis alumna and former UCLA staff member, expressed disappointment that UC permitted police brutality against students and has tried to change the narrative about what was happening on its campuses. Ms. Calitto stated that the University was demonizing students for asking it not to support a genocide. She added that this was not the first instance of police brutality at UC.

N. Alisa Daniels, UCLA staff member, called on UC to rectify pay inequality among early childhood teachers. At UC Merced, no lead teachers were receiving adequate compensation despite their credentials and degrees; fast food workers were earning more than UC childcare educators. Ms. Daniels stated that investing in fair pay was an investment in children's future and equality in the UC system, and that these teachers should be rewarded for their invaluable contribution.

O. Omar Issa, UCLA alumnus, asked the Regents to divest from any companies involved with the State of Israel and in the ongoing genocide. He believed that students and alumni have the right to make sure that UC is not involved with organizations that are complicit in funding and supporting a genocide. Mr. Issa expressed the importance of listening to students and his disappointment in the lack of protection of protesters at UCLA when they were attacked by outside agitators.

P. Manav Patel, UC Santa Cruz alumnus, stated that he was disheartened by the University's continued support for the genocide in Gaza through its investment in defense contractors and weapons manufacturers. He stated that UC was contradicting its teachings about the legacy and impact of colonialism.

Q. Dehice Chavez-Camarillo, UCLA alumna, expressed disgust at UCLA's response to recent protests and fear for UCLA students whom she was mentoring. She asked the Regents to give full amnesty to student protesters and to negotiate with them. She added that Chancellor Block had failed students multiple times.

R. Osvaldo Hidalgo Otamendi, UCLA alumnus, expressed disappointment in the way UCLA has treated student protesters, who were nonviolent and fighting for a noble cause. He asked the Regents to support them.

S. Hadeer Soliman, UC Irvine alumna, stated that it was shocking and abhorrent that UC investments were funding the genocide of Palestinians and demanded that information about UC investments be made available to students, faculty, and taxpayers. She also called on the Regents to divest from weapons manufacturers and companies that profit from the genocide. Ms. Soliman asked why there were double standards for apartheid in South Africa and violations of international law by Israel. She stated that the University had prestige in the community and the Regents had the power and responsibility to overhaul its investments.

2. **REVIEW OF PERFORMANCE FOR THE THIRD QUARTER OF FISCAL YEAR 2023–24 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.]

Committee Chair Robinson thanked those who participated in the public comment period and congratulated the Office of the Chief Investment Officer (CIO) for its hard work and for the great performance of UC investments.

Chief Investment Officer Bachher expressed appreciation for the questions and curiosity of those who participated in the public comment period. To the best extent possible, the Office of the CIO would be responsive to and work collaboratively with the community. He also congratulated students who were graduating. Last November, 300 students attended the inaugural UC Investments Academy Symposium at UC Merced. In under two years, more than 2,500 students have participated in the UC Investments Academy, hundreds of whom were from UC Merced. Of the approximately 175 students placed in jobs and internships, 40 were from UC Merced.

Mr. Bachher noted that he and his team celebrated their ten-year anniversary on March 31. Driven by strong markets, UC investments assets grew 90 percent over the last decade. The Office of the CIO has received many requests to divest or sell, and Mr. Bachher asked if money should be taken from working capital, the endowment, or the UC Retirement Plan (UCRP). The Office of the CIO managed retirement savings for about 350,000 individuals and the pension plan for about 300,000 retirees, as well as day-to-day responsibilities to the University. As of March 31, working capital stood at $14 billion, the endowment stood at almost $30 billion, and retirement assets totaled $133 billion. Mr. Bachher stressed the fiduciary responsibility of the Office of the CIO, which did not take students, faculty, or staff lightly regardless of their views. His office aimed to buy and sell uniformly across all the portfolios it managed and not just for any one constituent. In the fiscal year to date, the net returns for the pension and the endowment were both 9.7 percent. The Blue and Gold Pool grew 13 percent and was likely to outperform other products. The 30-year annualized net return was 9.1 percent for the endowment and 8.4 percent for the pension. Global equities grew 16 percent in FY 2023–24 and 20 percent in the fiscal year to date. In the last ten years, the Standard and Poor’s (S&P) 500 had an annualized return of 13 percent and global equities had a nine percent annualized return, but the pension and the endowment did not have the same rates of return because other asset classes did not perform as well. In fact, the S&P 500 and the MSCI All Country World Index (ACWI) outperformed UC’s other product returns for the last 30 years. Both the United States and India have performed well on a one-year basis, driven primarily by information technology and communications services. Mr. Bachher projected that interest rates and inflation would remain higher for the next three to five years.

Senior Managing Director Satish Ananthaswamy noted that the economy transitioned from a “hard landing” scenario, in which the economy slows after a period of rapid growth, to a “soft landing” scenario, in which the Federal Reserve (Fed) brings down inflation to slow the economy, to a “no-landing” scenario, in which the economy continues to grow despite monetary policies. He explained why interest rates would likely remain higher for longer and were unlikely to return to zero percent in the near future. Short-term interest rates were determined by the Fed and U.S. Treasury bills at two-year constant maturity or less. Long-term Treasury bills were driven by supply and demand. With a deficit of nearly $2 trillion, it would be impossible for the U.S. to bring down long-term interest rates. U.S. Secretary of the Treasury Janet Yellen has issued short-term Treasury bills to fund the deficit but would have to issue coupon-paying and longer-maturity bonds, in which case long-term Treasury yields would not decrease soon. If the Fed has difficulty bringing inflation under control, the federal funds rate or the short-term interest rate could remain higher. These higher rates would have an impact on private assets, the public equity markets, and the fixed income market. Mr. Ananthaswamy suggested observing three things. First, one should note what is happening in Treasury auctions. If fewer people buy Treasury bills, there could be turmoil in the bond market. Second, one should closely watch the actions of rating agencies given UC's need to issue a large amount of debt. Third, one should watch for a higher term premium that would entice investors to buy longer-term Treasury bills. The Federal Reserve Bank of Atlanta tracked U.S. gross domestic product (GDP) at 4.2 percent, but automobile loan and credit card delinquencies were starting to rise. As long as employment was strong, Mr. Ananthaswamy projected that a recession was unlikely to occur in 2024 but could possibly occur in 2025.

Mr. Bachher added that the Fed was closely watching unemployment to determine how to address inflation. According to the research of Christina Romer, Professor of Economics at UC Berkeley, the current Fed seemed very committed to a target inflation rate of two percent. Rising housing and energy prices were also affecting inflation. In the past, if fixed income was returning zero percent, one needed to invest in more private assets in endowments in order to meet the payout obligation. At present, a payout obligation could be met with short-duration fixed income. If these conditions continue for the next three to five years, the University could de-risk its asset allocation by lowering the number of private market investments in the pension and the endowment, and UC could increase endowment payouts to five percent. Mr. Bachher stated that the payout for the Blue and Gold Pool could also be raised to five percent.

Margaux O'Brien, Investment Director of Public Equity, stated that earnings were above historical averages and were still improving. Although the topline has softened slightly, there were no significant fundamental weaknesses observed in the earnings. The Office of the CIO was closely watching the shift from a soft landing to a no-landing scenario.

Mr. Bachher stated that Apple announced a massive buyback of its own stock, and Google announced a large dividend in Alphabet, its parent company. Mergers and acquisitions (M&A) activity seemed strong. All of these boded well for the equity markets. However, higher interest rates weighed on consumers and corporations when they needed to refinance. Higher interest rates typically resulted in more bankruptcies, but people were renegotiating their debt and some lenders were taking equity due to the rising equity market. Mr. Bachher was confident that more opportunities would emerge, adding that UC had about $130 billion of liquidity. The Office of the CIO was investing below its target asset allocation for private assets in the endowment and the pension to avoid risk.

Marco Merz, Managing Director of Defined Contributions Products, announced that, on July 1, investing in the Blue and Gold Pool would be available to UC Retirement Savings Program (UCRSP) participants as the UC Blue and Gold Fund. The fixed income portfolio of the pension was benchmarked against the One to Five Year Government/Credit Index, and participants would later have access to the UC Short Duration Bond Fund, which would mimic the fixed income exposure in the pension. Participants would also be able to buy certificates of deposit (CD) to take advantage of the higher interest rate environment. UCRSP participants were able to save ten to 11 percent on top of their mandatory contribution to the pension.

Committee Chair Robinson asked Mr. Bachher to expound on what divestment would mean in a literal sense. Mr. Bachher recalled that, when he had first joined UC, there was a request from the community to consider divesting from fossil fuels, which were perceived differently in Alberta, Canada, where he was from. From that experience, Mr. Bachher found that UC should listen to and engage with students, faculty, staff, Regents, and the wider community because they were an early warning system of what was happening in the world. The Office of the CIO conversed with UC faculty and researchers to understand the implications of selling or buying assets in fossil fuels. Mr. Bachher also found that environmental, social, and governance (ESG) issues could not act as a policing function and decided that ESG considerations must be part of his office's culture, which was much harder to achieve. Under the leadership of the Board, the Office of the CIO added the consideration of ESG factors as an objective in the investment policy, alongside maximizing return and minimizing risk. The Office of the CIO later deemed fossil fuel investments to be a financial risk because they were stranded assets and decided, over a five-year period, to sell fossil fuel holdings, replacing them with investments in clean and renewable energy, and redistribute that capital to parts of the portfolio with better financial returns for lower risk. Mr. Bachher stated that the process began at the campuses, through organized and respectful public comment periods at Regents meetings. In the past, the Office of the CIO made decisions after peaceful engagement with the UC community, but this time it was different. The Office of the CIO could not discount fiduciary responsibility when making decisions, because UC investments assets belonged to the entire University of California, not individual campuses. Most people seek a binary answer with regard to divestment, but the world is not as binary with regard to investment matters. This careful consideration is what an academic institution is built upon.

Chief Data and Operating Officer Arthur Guimaraes explained that State and federal regulations established the Office of the CIO's fiduciary duty of care, prudence, and loyalty. Maximizing risk-adjusted returns for beneficiaries could not be superseded by some of the issues that have been raised. Mr. Guimaraes noted that both the Office of the CIO and the Regents were fiduciaries. Aside from culture, ESG was also an issue of governance. The Regents owned the UC Investment Policy Statement, and the Office of the CIO implemented it. ESG was also part of the ethos of the University. However, there were laws such as State Assembly Bill 2844, which was passed in 2016 and placed restrictions on divestment. In 2015, the Office of the CIO created a framework for sustainable investment and underwent a detailed process that included research, due diligence, and asset stewardship. The office's compliance team reviewed the portfolio on a quarterly basis to ensure that it remained free of fossil fuel investments. The Office of the CIO engaged with the Global Climate Leadership Council, likeminded investors, and organizations like Principles for Responsible Investment. Mr. Guimaraes presented a timeline of ESG integration at the Office of the CIO, noting the time that was taken.

Wendy Pulling, Director of ESG Integration, stated that, at about $105 billion, UC's biggest asset class was public equities. To address the financial and material ESG risk associated with investing in certain companies, the Office of the CIO employed two strategies: 1) integrating material ESG risk considerations in proxy voting guidelines that are exercised at annual general meetings and 2) engaging with company leadership to raise material ESG risk. The Office of the CIO focused on sectors and companies that were most exposed to risk and worked with other like-minded institutional investors to reach out to companies through a third-party consultant. The Office of the CIO engaged with about 300 companies annually in a multi-year process. For example, the automobile sector was exposed to material risks related to consumer preferences, government regulations, and technological advancements as the world transitions from a fossil fuel economy to a low-carbon economy. The Office of the CIO wished to invest in companies that recognize risks and turn them into opportunities. In a multi-year engagement with BMW through a consultant, the Office of the CIO and fellow investors contributed to BMW's greater ambition related to its electric vehicle sales.

Regent Makarechian asked what the Office of the CIO was planning to do about the missed benchmarks in private equity. Mr. Bachher acknowledged that private equity has significantly underperformed compared with the benchmark in the last two to three years. In the last ten to 30 years, private equity has performed better than the benchmark. He could do nothing about it.

Regent Makarechian asked if this was because the Office of the CIO was locked into this benchmark or had co-investments. Mr. Bachher replied that the Office of the CIO's portfolio strategy has remained the same, but its benchmarks were the public markets. For instance, the performance of the MSCI US REIT Index was not relevant to an investor of a specific building. The benchmark for the private equity portfolio was the Russell 3000 plus three percent.

Regent Makarechian remarked that UC chose inaccurate benchmarks. Mr. Bachher responded that, in any short time period, it is not appropriate to compare private investments to the benchmark. He theorized that things eventually work themselves out in three to ten years.

Mr. Bachher asked Matt Webster, Managing Director of Private Equity, for a long-term comparison between UC's private equity portfolio and the benchmark in aggregate. Mr. Webster replied that the endowment generated 15-year returns of 18.6 percent and ten-year returns of 17.3 percent.

Mr. Bachher noted the positive value-add in comparison with the benchmark. Regent Makarechian observed that the three-year returns were negative and that the 15-year returns were positive. Mr. Bachher emphasized the high returns in the equity markets over the last four years. He has long held the view that it was not for the Office of the CIO to tell UC how to measure its performance. Measurement was more important in the long term.

Regent Sherman explained that the Russell 3000 plus 300 basis points was chosen for lack of a better benchmark, and it justified taking the illiquidity risk as well as the long-term hold of private equity as an asset class. This was a backward-looking measurement over five to ten years or longer, because public markets were not receptive to private companies exiting via initial public offerings or acquisitions. Private equity also lacked realizations that provide good marks, and private equity partners did not have comparable companies to mark to.

Regent Makarechian suggested that UC revisit this matter and expressed hope that private equity would perform well with the growth of artificial intelligence (AI). Mr. Bachher addressed the short-term implications of performance on incentive compensation, which was determined on a three-year basis. Over three years, negative or zero performance in private equity, which made up a large portion of investments, could have an effect on the rest of the portfolio. This was an unintended consequence of the incongruity of the long horizon of private equity and the three-year measurement period.

Regent Makarechian asked what portion of investments in real assets was in precious metals and what portion was in real estate, and whether the investments in real estate were factored into the real estate asset allocation. Mr. Bachher replied that real estate was separate from real assets in the asset allocation. John Ritter, Managing Director of Real Assets Investments, replied that precious metals, categorized as natural resources, made up approximately four percent of real assets and that there was no real estate exposure in real assets. Mr. Bachher added that 60 percent of investments in real assets was in infrastructure, about 16 percent in natural resources, and the balance in diversifying yield.

Regent Makarechian remarked that it was not possible to divest from fossil fuels given that 86 percent of the general economy relies on fossil fuels for manufacturing, as well as UC's fiduciary responsibility and applicable laws. Mr. Bachher expressed agreement, noting the goods that were derived from fossil fuels as well as the use of fossil fuels in transportation.

Regent Makarechian asked why some of the benchmarks and returns differed among the General Endowment Pool (GEP), the pension, cash, and other asset classes. For instance, public equity investments had a 15 percent benchmark but about a seven percent return in the GEP. He asked whether asset classes were managed by different people and how benchmarks were set. Mr. Bachher responded that differences in asset allocation and portfolio implementation had some effect on the returns for GEP and the pension. Both GEP and the pension were long-term assets with almost perpetual horizons, and the Office of the CIO has been working to harmonize and streamline them over the last decade. Marginal differences also came from small investment opportunities, but it was the intention of the Office of the CIO to uniformly invest in both asset classes. For instance, from the Blackstone Real Estate Income Trust transaction, $3 billion was placed in the pension and $1.5 billion in the endowment.

Regent Makarechian asked about the ratings of UC's private credit investments. Mr. Bachher stated that a response would be provided later in the meeting.

Regent Tesfai asked about the process for identifying the University’s investments in weapons manufacturing, highlighting the role of ESG in UC’s investment strategy and noting that Mr. Bachher had met with students regarding this issue. Mr. Bachher thanked Regent Tesfai for encouraging him to meet with students at the previous Regents meeting. Weapons manufacturing was one of several concerns raised in a letter sent to the Office of the CIO by students on April 26. Students asked the University to divest from weapons manufacturers. The Office of the CIO has not actively decided to invest in a weapons manufacturer, but the University was exposed to such investments through stock market and bond indices, such as the S&P 500 and MSCI ACWI. This was equity or debt that UC might own from weapons manufacturers. Across all pools of capital, UC’s exposure to weapons manufacturing was $3.3 billion dollars. Students also asked that UC divest from any company or entity supporting Israel. Mr. Bachher stated this entity was the U.S. government. UC owned $12 billion in U.S. Treasury securities, a $20 trillion asset class. A third question was related to UC holdings in Blackrock. Mr. Bachher stated that UC had a $163 million exposure to Blackrock through the passive index. Other than U.S. Treasury securities, these were not active investments. The fourth question was about investments managed by Blackrock on behalf of the University. Mr. Bachher stated that Blackrock managed $2.1 billion in bonds in UC’s fixed income portfolio. Students asked that the University divest from all of its investments in Blackstone. Mr. Bachher stated that UC had $8.6 billion in investments in Blackstone. Students also asked the Office of the CIO to look into the University’s exposure to 24 companies such as Coca-Cola, Disney, and Intellia Therapeutics. Mr. Bachher replied that UC’s exposure to those companies through the index was $3.2 billion. By his calculation, this letter suggested that UC should sell $32 billion in assets.

Regent Tesfai expressed appreciation for Mr. Bachher’s response and the work of the Office of the CIO to compile these data. He agreed that campus communities were an early warning about what was now a national topic of conversation, and it was important for the Regents to discuss whether the University was putting into practice its ESG principles, such as those related to human rights and inequality. It was also important that this Committee and the Board collaborate with and receive input from students, staff, and faculty. While he might not agree with all of the demands made by students, Regent Tesfai believed that UC must respond to them. Students were not feeling heard, and without a format for students to provide input and receive answers to their questions, one could see more anger and confusion. Mr. Bachher responded that the Office of the CIO demonstrated service to the community through its daily operations, which included listening and engaging. He estimated that these conversations with the community have taken up 25 to 30 percent of his time over the last decade. The Office of the CIO prided itself on a culture of transparency, having regularly disclosed its holdings on its website on June 30.

Faculty Representative Steintrager raised the issue of the relationship between fiduciary responsibility and ESG. In his view, there has been a sleight of hand regarding fossil fuels. He asked what would happen if ESG values disagreed with fiduciary responsibility. Mr. Bachher replied that he would not sell the asset. If the Board instructed the Office of the CIO to sell something, the latter would listen. However, if Mr. Bachher and his team did not think that something was a bad investment, then he would not sell it. The Office of the CIO has engaged with faculty, and views on this issue were not unanimous. The team has also engaged in a discussion about fossil fuels in the context of the UC Retirement Savings Program. One of its 350,000 participants could sue the University for making a decision that was not in UC's best financial interest. The Office of the CIO engaged with faculty and staff using its ESG framework and a clear view of implementation from financial risk and investment return perspectives. Mr. Bachher underscored the clarity in decision making. The Office of the CIO decided to sell its holdings in fossil fuels because it did not believe that stranded assets were a good investment.

Regent Ellis shared that he has read all the communications sent to the Regents regarding divestment, noting his position as Vice President of the Alumni Associations of the University of California (AAUC). He expressed understanding of students' and others' demands, despite not agreeing with all of them. This was a very complex issue in a globalized society and might not be easy to implement. The Office of the CIO has also met with alumni, the foundations, and others. Regent Ellis advised students who were vocal about this issue to sign up for the UC Investments Academy in order to "fix it from within," similar to what he has done in becoming a Regent. When he had served in student government at UC Merced, there was no consensus regarding divestment from fossil fuels. It takes multiple constituency groups to build consensus. Mr. Bachher expressed gratitude for Regent Ellis' remarks. The Office of the CIO could hold an annual sustainability event to engage with faculty, staff, and students in an organized way. The Office of the CIO could set aside a $10 million investment pool for students and then report on their results. There was a learning opportunity in every moment. In this moment, the Office of the CIO must learn to evolve its thinking regarding these issues, which were complex and not clear-cut. Regent Ellis stated that the investment pool would be an amazing experiential learning program.

Regent Ellis stated that increasing the endowment payout to five percent would make a tremendous impact across the system, particularly at UC Merced, which would receive more funding for scholarships and basic needs services. For instance, the UCM Alumni Association's Professional Clothing Closet could buy more professional clothing with such a payout. He asked whether the payout could exceed five percent. Mr. Bachher replied that five percent was prudent; this was a matter for the Finance and Capital Strategies Committee to consider. The payout could be stretched to 5.25 percent, but one must balance long-term sustainability and capital appreciation.

Regent Ellis remarked that alumni wishing to withhold donations to the University gave him great pause. Not all donations went into the investment portfolio; some of it was spent immediately. Generally speaking, UC involvement made things better. UC was acting as an ethical participant in the market through proxy voting and conversing with C-suite officers. UC was doing everything it could to make the world a better place. Regent Ellis thanked the Office of the CIO for its work and for engaging with all constituencies at UC.

Regent Hernandez stated his understanding that about 18 percent of the University's investments was in weapons manufacturing companies or companies that supported Israel. Mr. Bachher replied in the affirmative; this was based on Mr. Bachher's interpretation of the questions. Regent Hernandez stated that UC needed to do better to communicate why divestment was not as simple as selling a coupon. Some investments were time commitments. However, given the political climate, he believed that the University should pause future investments of this nature. Mr. Bachher responded that this could be interpreted as pausing the returns paid to pensioners and savers or pausing one thing at the expense of the University's financial obligations. Over the last ten years, there has been globalization, a harmonious view on trade, progressive monetary and fiscal policies, and growth in the U.S. and around the world. In the next three to five years, Mr. Bachher predicted war, reconstruction, demographic issues with an aging population, technological enhancements, and more trade tariffs. The effect of the next U.S. election was unknown. He also predicted that Regents meetings for the next five years would be dominated by a political issue. He disagreed that the University should pause investing until the nature of political and social issues are understood, as UC still had obligations.

Regent Hernandez shared that he too was a UC pensioner and would not mind if UC removed the 18 percent of investments. Mr. Bachher reiterated UC's responsibility to hundreds of thousands of participants. However, the Office of the CIO served the Board of Regents and would act as instructed.

Staff Advisor Mackness asked if the Office of the CIO has had conversations about weapons manufacturing and divestment with its third-party consultant and like-minded institutions. UC could continue to put pressure on specific companies. Ms. Pulling replied that de-risking was a very limited tool, but UC could join other institutional investors to manage ESG risk through engagement. She contrasted the 300 companies that were part of UC's fossil fuel de-risking effort with the 9,000 companies the Office of the CIO had an opportunity to engage. Federated Hermes was the Office of the CIO's consultant, and the other institutional investors included a pension fund in Europe, the University of Toronto, and Northern Trust. From telephone calls to outcomes, the strategic engagement plan was typically three years long. The Office of the CIO worked with the consultant to identify the biggest risks and responsive holdings. Climate change has been the biggest topic by far, and conversations were also taking place with companies exposed to risk from ongoing wars. Typically, UC did not participate directly in these conversations but managed the consultant and followed the engagement closely. In the U.S., UC was a leader in this type of activity. Many of UC's peer pension funds had in-house engagement teams of 15 to 20 people, but UC was able to engage 300 companies with the help of a consultant.

Regent Sherman noted that, at $38 billion, the UCRSP was UC's second biggest pool of assets, larger than the GEP and Blue and Gold Pool combined. He stated his understanding that UCRSP was self-directed. Mr. Bachher replied that this was correct.

Regent Sherman stated that it might be illustrative to see how UCRSP beneficiaries allocate their assets. He asked, for instance, if they invested a portion of their assets in weapons manufacturing or if they invested in index funds. Mr. Bachher shared the sale of UC's holdings in fossil fuels as an example. The Office of the CIO began by selling holdings from the endowment, followed by the pension and working capital, but did not sell holdings in UCRSP out of concern that one participant could take legal action against the University.

The Office of the CIO made sure that it clearly understood the implications of how UC invests in the UCRSP, and added the MSCI ACWI IMI ex Tobacco ex Fossil Fuels Index to its 401(k) platform in order to bring UC's institutional views into alignment with the retail marketplace and to give faculty, staff, and other participants this option. The same index was found in the pension and the endowment. Out of $38 billion, participants have invested $32 million into this index.

Regent Matosantos expressed gratitude for the discussion about the complexities of divestment, such as the difference between direct investment and exposure and the impact of ESG engagement. She thanked Mr. Bachher for helping the Committee understand the legal landscape and UC's obligation as a fiduciary. The conversation about fossil fuels demonstrated the relationship between UC's ESG efforts and its legal obligations. Her view differed slightly regarding the identity of the client. As a member of the Board, Regent Matosantos did not believe that she was a client. However, she believed that Regent Hernandez, as a UCRSP participant, was a client. The University had a responsibility to different constituents depending on the fund, as well as a collective responsibility to work through difficult times.

Mr. Bachher stated that universities were places to raise issues, teach, and learn. He was passionate about his work, as were students and faculty, and this engagement made the University of California the best public research university in the U.S. and the world. Mr. Bachher expressed gratitude that the Office of the CIO could serve the University and the community. He concluded his remarks by recognizing both past and present staff of the Office of the CIO.

The meeting adjourned at 2:35 p.m.

Attest:

Secretary and Chief of Staff