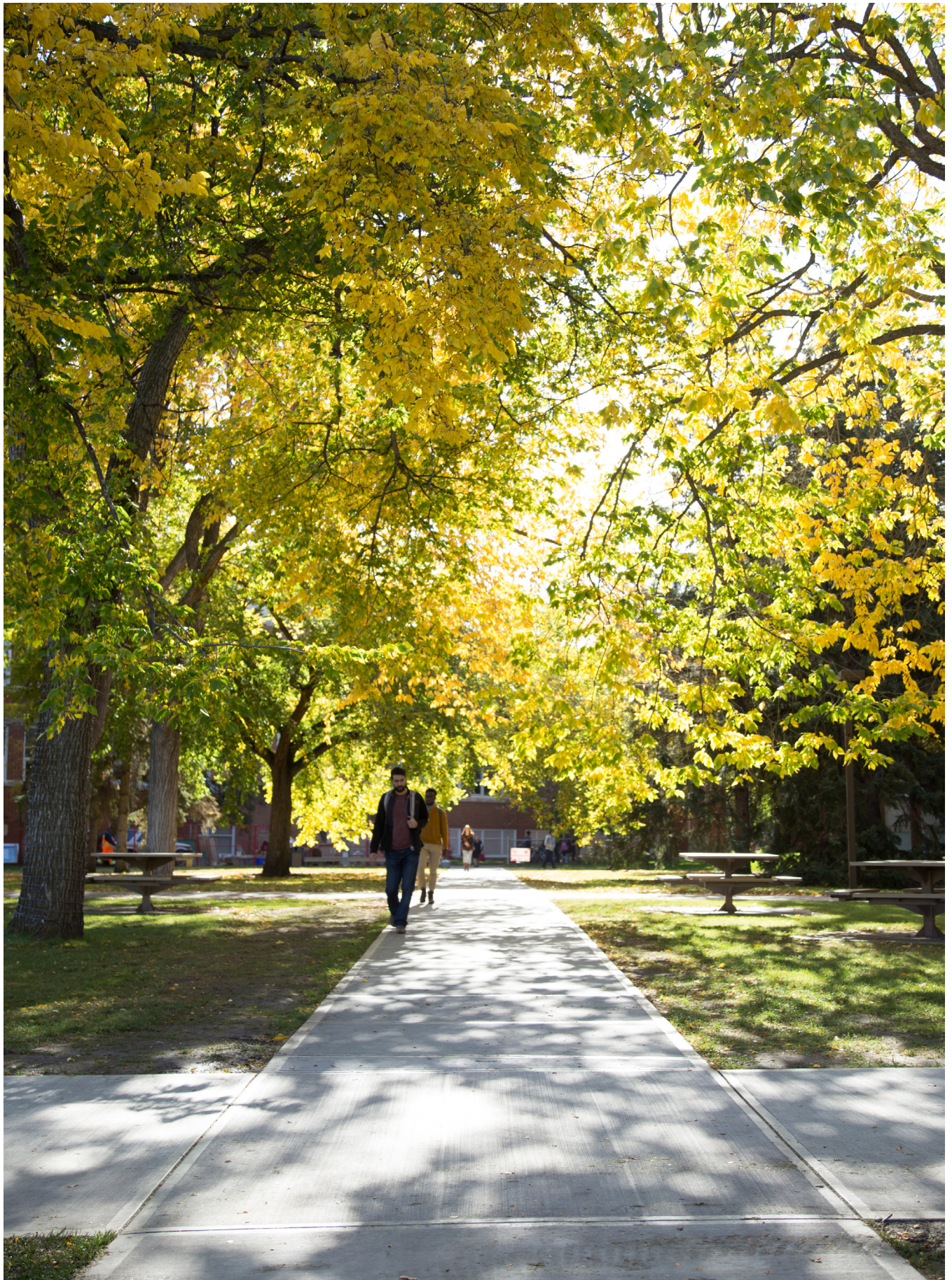


2020 INVESTMENT COMMITTEE ANNUAL REPORT








Investment Committee Annual Report For the Year Ended March 31, 2020

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Letter from the Investment Committee Chair

On behalf of the University of Alberta Investment Committee, I am pleased to present the 2020 annual report. The investment assets under the oversight of the Investment Committee totaled \$2.27 billion as of March 31, 2020, of which \$1.28 billion represented endowments. Over the year, endowment assets generated \$53 million for program spending on scholarships and research, up \$4 million from the prior year.

The University Endowment Pool (UEP) returned -10.2% this past year, which underperformed its benchmark return of -8.4% and fell short of the long-term target of 7.25%. However, the UEP has exceeded this target over the longer term with an 8.9% annualized return since inception. The Non-Endowed Investment Pool (NEIP) returned -1.3%, which lagged its benchmark return of -0.9%.

The past year was truly unprecedented as the global pandemic brought about by the novel coronavirus (COVID-19) altered nearly every aspect of our daily life. In an effort to ease the burden on the global healthcare system governments mandated widespread economic lockdowns, resulting in a global recession that began in the first quarter of 2020. Capital market volatility across many assets increased to levels that surpassed those experienced in the 2008 Global Financial Crisis, in turn prompting an unparalleled fiscal and monetary response. Unemployment levels spiked in the wake of the pandemic, while the actions of governments and central banks around the globe thus far have prevented a global depression. Amidst this uncertain environment, risk assets such as equities and commodities performed poorly while safe haven assets like government bonds and the US dollar outperformed. The UEP suffered from its overweight allocation to Growth assets; however, it saw healthy performance from Deflation Hedging and Diversifiers, which softened the impact. With central bank policy rates effectively zero and yield curves flat across the developed world, the path forward presents a challenge requiring more creativity and a willingness to tolerate higher volatility in order to meet the desired objectives.

The Investment Committee continued to oversee Management's implementation of both the UEP and NEIP target asset allocations as well as the strategic organizational plan to maintain strong investment management practices. In the coming year Management will be completing a comprehensive asset allocation review for the UEP to ensure that the strategic asset allocation remains commensurate with the desired risk and return objectives. With respect to the NEIP, additional progress will continue in advancing the Yield strategy closer to its target asset allocation.

I would like to acknowledge the continued hard work and dedication of both Management and members of the Investment Committee to the University and its stakeholders during this particularly challenging time. We hope everyone continues to stay safe and healthy.

Dave Lawson, CFA
Chair, Board Investment Committee, University of Alberta

Investment Committee

March 31, 2020

Appointed

Dave Lawson, CFA Chair

Derek Brodersen, CFA Vice-
Chair

John Butler, Q.C.

Maria Holowinsky, CFA

Sandy McPherson, CFA

Peter Pontikes, CFA

R. Ryan Thompson, CFA

Ex-Officio

Kate Chisholm, Q.C.

Douglas Stollery, Q.C.

David Turpin, CM, PhD, LLD,
FRSC

Executive Summary

The investment assets of the University of Alberta that are under the purview of the Investment Committee had a total market value of \$2.27 billion as of March 31, 2020 (2019 - \$2.47 billion). This amount consisted of \$1.28 billion (2019 - \$1.43) in Endowed Funds and \$0.99 billion (2019 - \$1.04) in Non-Endowed Funds.

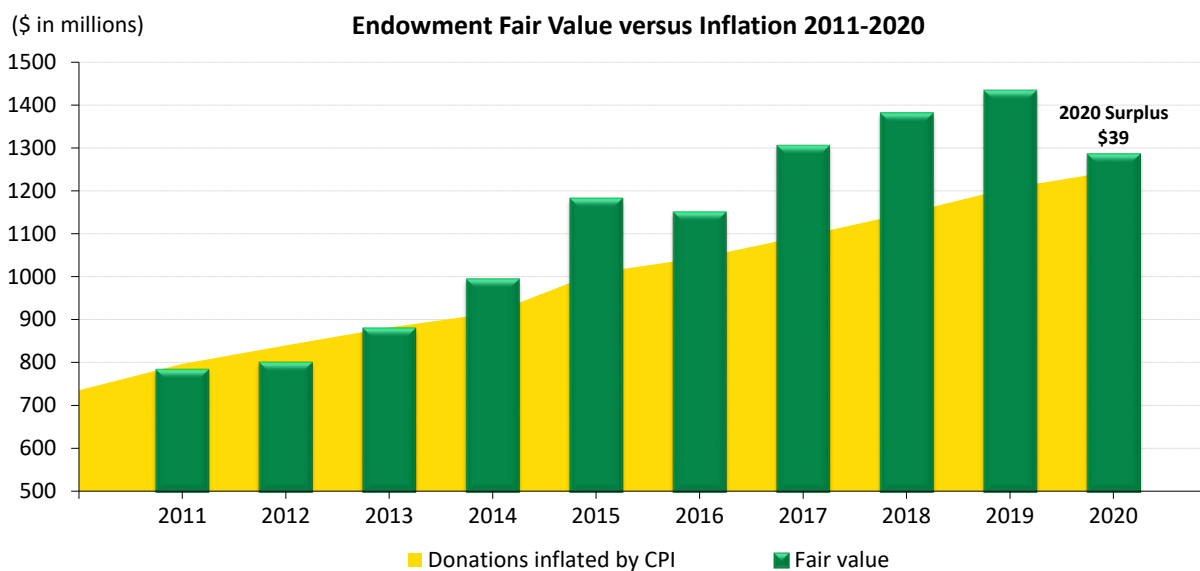
With few exceptions, the Endowed Funds are pooled and invested collectively in the University Endowment Pool (UEP). Endowment funds represent permanently restricted capital, and only a portion of the cumulative earnings can be allocated for their specified purpose. The investment objective of the UEP is to achieve a long-term rate of return that in real terms (i.e. adjusted for inflation) meets or exceeds total endowment spending, as outlined in the UEP Spending Policy. By meeting this objective, the University is able to provide intergenerational equity for students, which ensures a comparable level of support between future generations and current beneficiaries.

The Non-Endowed Investment Pool (NEIP) consists primarily of expendable operating and research funds and remains shorter-term in nature with a greater focus on capital preservation.

Endowment Funds - Highlights

- The UEP returned -10.2% during the year as returns from most asset classes were negative. Exceptions include real estate, government bonds, and diversifying strategies, which generated positive returns in aggregate.
- The market value of the Endowment Funds ended the 2020 fiscal year at \$1.28 billion, down \$148 million from 2019. Inflows, including donations, remained stable at \$28 million however were offset by \$131 million in investment losses, \$53 million in program spending allocation less \$27 million which is restricted for use in future years, \$10 million for investment management costs, and the \$9 million administrative assessment for indirect costs associated with the programs being supported.
- During the year, the real value of the endowments decreased by 16.4%. This decrease was comprised of; total expenditures of 5.3%, inflation of 0.9%, and the return of -10.2%. As a result, the value of the endowments over their cumulative inflation adjusted objective decreased to \$39 million as at March 31, 2020, or 3.1% as outlined in Exhibit 1. The surplus heading into this past year was of sufficient size to allow for sustained spending amidst an uncertain environment going forward.

Exhibit 1



- For the fiscal year, \$53 million was made available for spending on academic programs, faculty support, research, and scholarships. This represents an increase of \$4 million from last year.
- The fund's benchmark returned -8.4%, indicating UEP underperformance of 1.8% over the past year. However, on a ten-year basis the fund has outperformed its benchmark by an annualized rate of 0.4%.

Non-Endowed Funds - Highlights

- The NEIP recorded an overall return of -1.3% for the year, which trailed its benchmark return by 0.4%. The overweight allocation to the Liquidity strategy was insufficient to offset poor performance from the Return Seeking strategy.
- The Yield strategy's implementation continued over the past year with additional investments in unconstrained global fixed income, active Canadian preferred shares, and private credit. A search for multi-asset absolute return strategies is underway and expected to be fully funded in the latter half of 2020.
- The value of the NEIP's Yield and Return Seeking strategies continue to exceed their underlying obligations by \$30 million (2019 - \$56 million) or 5.8% (2019 - 9.8%), and support the investment income reserve. An excess greater than 17% can be used for future strategic initiatives.



Major Initiatives During the Year

Implementation of the UEP Strategic Asset Allocation

Over the past year, Management was active with the continued implementation of numerous strategies that moved the UEP closer to its strategic asset allocation. Within Growth, six commitments were made to various private equity funds throughout the year while capital continued to be called and distributed by legacy funds. In Inflation Sensitive, a commitment to a Canadian opportunistic real estate fund was completed while prior funds continued to return capital. Diversifiers saw the most change over the course of the past year with Management completing new hedge fund allocations. The funding of a customized fund of one took place at the beginning of the year with an emphasis on diversified exposure to global macro, structured credit, and relative value strategies. To augment the portfolio and ensure sufficient convexity, an allocation to a concentrated trend following program was finalized near year-end.

Implementation of the NEIP Yield Strategy

An active Canadian preferred share strategy was initiated using proceeds from the sale of a passive exchange traded fund (ETF) in the same asset class, while a recently completed Canadian mortgage search is expected to fund shortly. A commitment was made to a private credit strategy that is expected to call capital over the next 12-18 months.

UEP Asset Allocation Study

Management also initiated its first comprehensive review of the UEP's strategic asset allocation since 2013. Utilizing internal capabilities, Management is constructing and examining numerous portfolios and their expected probability of meeting the UEP's objectives over the long term. The Investment Committee will maintain ongoing dialogue with Management throughout the process, which will conclude later in 2020.



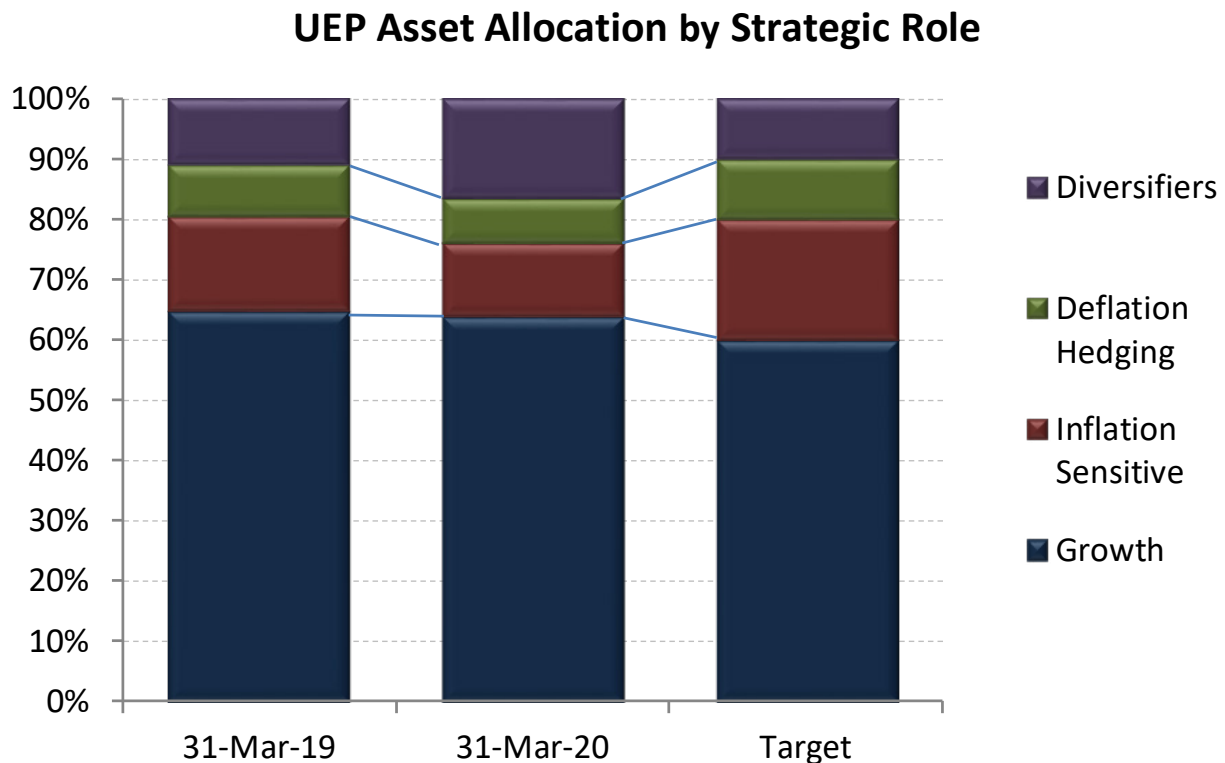
Endowment Funds

The primary investment objective for the UEP is to achieve a long-term real rate of return that equals or exceeds total endowment spending. Emphasis is placed on preserving intergenerational equity to ensure all beneficiaries, current and future, receive comparable levels of support. Assets are classified based on the strategic role they perform within the portfolio, specifically: Growth, Inflation Sensitive, Deflation Hedging, and Diversifiers.

- To meet spending targets and grow the value of the assets over time, a large allocation to public and private equities, hedge funds, and other assets with exposure to equity market returns is necessary.
- Inflation sensitive assets are those that adjust to unexpected and/or rising inflation. The assets in this category include real estate, natural resource equities, energy and renewables, and commodities.
- Deflation hedging assets are those that remain liquid and increase in value during times of extreme economic and capital market turmoil. This asset class consists of high-quality sovereign bonds.
- Diversifiers are any asset classes or investment strategies that have low or no expected correlation with the capital markets and inflation.

Endowment investments are categorized by Strategic Role in Exhibit 2.

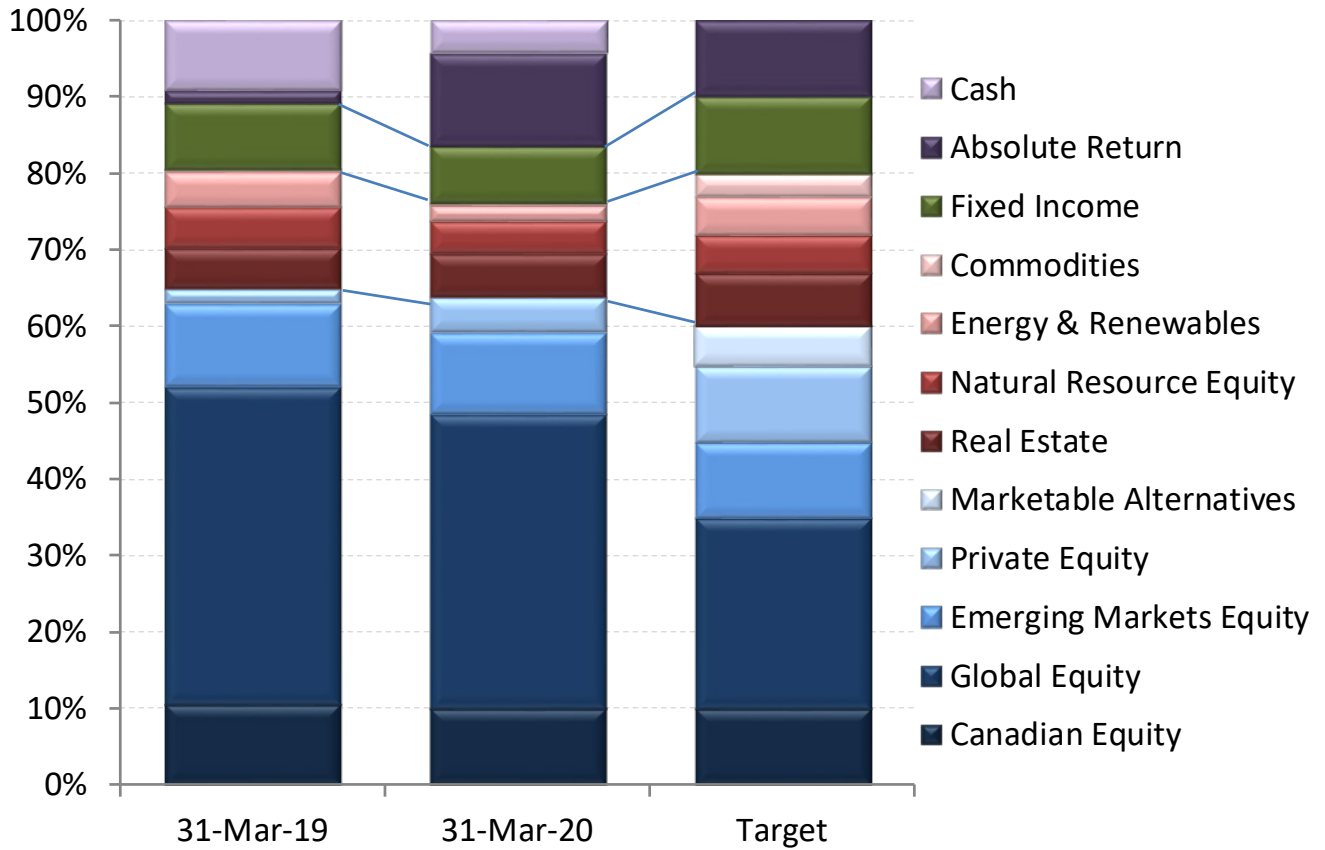
Exhibit 2



Investments are also categorized by Asset Class in Exhibit 3.

Exhibit 3

UEP Asset Allocation by Asset Class



Investment Performance Relative to Objectives

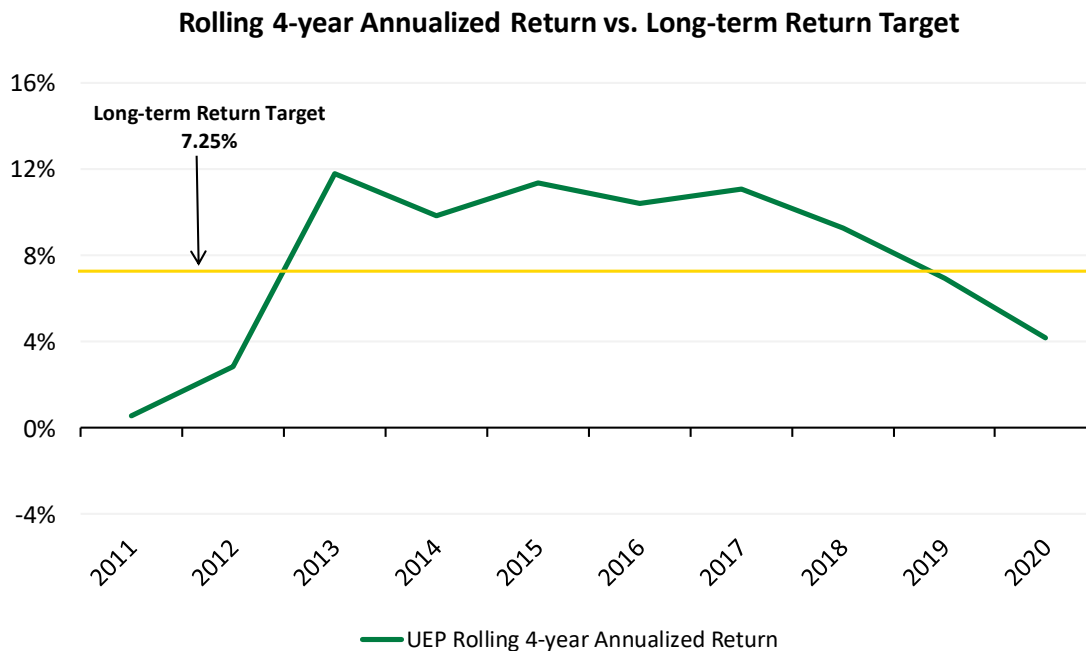
The UEP return over the past year fell short of total spending plus CPI by 16.4%. The ten year and since inception annualized excess return above spending and inflation for the period ending March 31, 2020 were 0.9% and 1.1% respectively.

The fiscal 2020 return of -10.2% reflects:

- An overweight allocation to developed market public equities at the expense of other assets.
- A deliberate tilt towards small cap at the expense of large cap across all public equities.
- Canadian dollar depreciation, which on balance minimized losses.

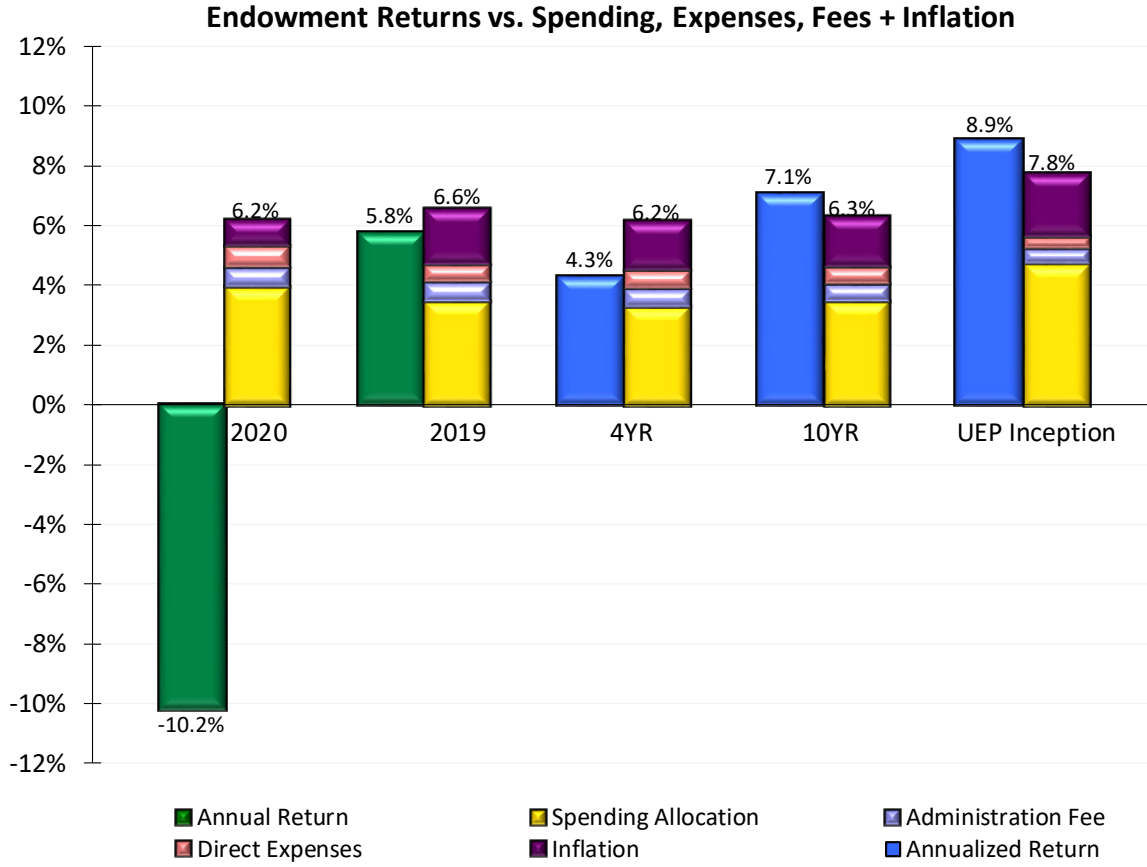
The UEP remains invested for the long-term with the expectation of providing a return in excess of spending and inflation in some years to compensate for years when this is not the case. Exhibit 4 illustrates the UEP's historical performance relative to the return objective of 7.25%.

Exhibit 4



As shown in Exhibit 5, since its April 1989 inception the UEP has produced an annualized return of 8.9%. This return has exceeded annualized total endowment spending plus inflation of 7.8% over that time period, while also achieving this objective over the past ten years. Though recent performance has been modest, the UEP remains in a position to allow for stable support for students, researchers, and the University community.

Exhibit 5



Further Perspectives on Investment Performance

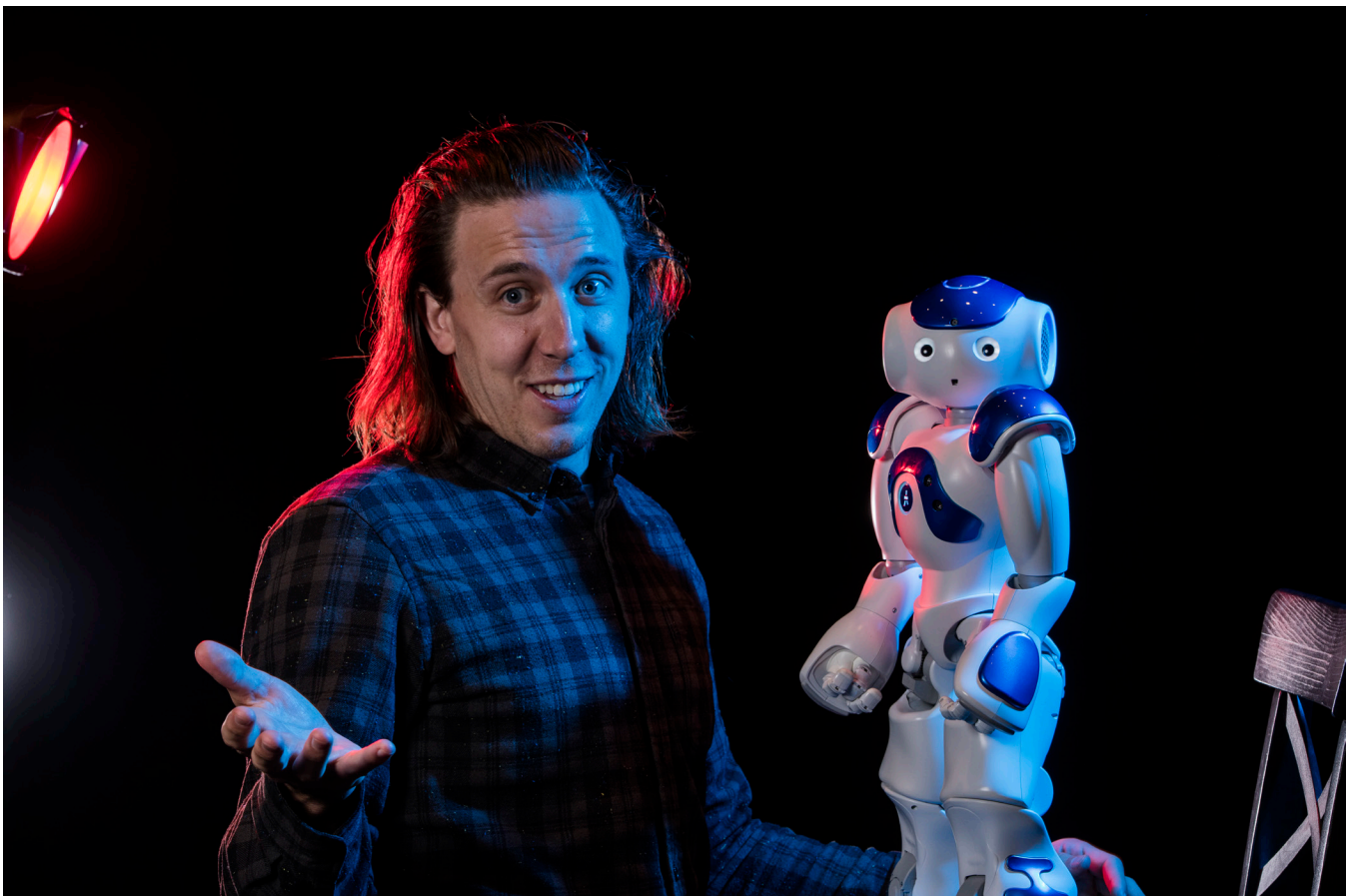
The returns of individual UEP strategies are measured against their respective benchmarks while the overall fund return is compared to the benchmark outlined in Exhibit 6. The difference between the UEP and its benchmark return reflects the impact of allocation decisions by Management together with active management decisions by our external managers.

The UEP return of -10.2% trailed its benchmark return of -8.4%, which is primarily attributable to security selection by the public equity managers within Growth. In aggregate, the UEP's active public equity managers suffered during a particularly challenging period for value and small cap strategies. With respect to allocation, the value added by the overweight allocation to Diversifiers proved beneficial as these strategies outperformed all other assets. The positive impact of an underweight allocation to Inflation Sensitive was offset by an underweight allocation to Deflation Hedging that performed well amidst a risk off environment.

Exhibit 6

UEP Investment Policy Benchmark

MSCI Canada IMI	10%
MSCI World IMI	35%
MSCI Emerging Markets IMI	10%
Cambridge Associates Private Equity Index	5%
IPD/Realpac Global Property Index	7%
S&P Global Natural Resources Index	5%
Dow Jones North America Select Junior Oil/Gas Index	5%
Bloomberg Commodity Index	3%
FTSE/TMX All Federal Bond Index	10%
LIBOR + 6%	10%
	<u>100%</u>



Growth

Growth assets generated a -11.8% return over the past year. Performance was negative across all geographies within public equity as Canada and emerging markets fared worse than most developed markets. Part of the reason for this underperformance stems from the fact that domestic equities do not benefit from a depreciating Canadian dollar during times of market stress. As volatility increased amid the pandemic and subsequent global recession, small cap equities sold off more than their large cap counterparts due to their perceived risk. From a factor perspective, quality, growth, and momentum continued their lengthy streak of outperformance and the divergence with value and low volatility factors widened. These detractors resulted in the poor aggregate performance of the public equity portfolio as a whole.

The UEP's existing private equity investments continued to call and distribute capital as they progressed through their fund lives. In coordination with its private markets advisor, Management made six fund commitments (one to buyout, two to growth, one to venture capital, and two to secondaries) during the year and continues to execute on investment opportunities in accordance with its implementation plan. While the private equity program is still in its infancy, early fund investments are in aggregate meeting expectations.

Inflation Sensitive

Inflation Sensitive assets posted a return of -21.7% over the year with significant divergence between the underlying allocations. Real estate investments performed the best with contribution from both income and capital appreciation. Core real estate in the US and Canada posted double-digit returns while value-add strategies in the US and Europe continued to distribute capital. Management closed on one fund commitment during the year and plans on additional investments over the coming year.

Natural resource equity and energy & renewables were hit particularly hard by the global COVID-19 market disruption. Energy and base metals producers were negatively impacted by contracting economic activity and the corresponding decline in demand for their respective commodities. At the same time precious metals producers benefited from strong demand for gold and silver as a hedge against unlimited quantitative easing from central banks around the world to preserve liquidity. Agriculture was more mixed as select commodities such as wheat and coffee continue to see robust demand globally.

Deflation Hedging

The Deflation Hedging strategy produced a return of 6.3% for the year as interest rates sank across the yield curve following the Bank of Canada cutting the overnight rate to 0.25% in March. The portfolio continues to maintain a shorter modified duration than the index to emphasize capital preservation and support endowment spending during challenging times like these.

Diversifiers

In aggregate, Diversifiers generated healthy results with a return of 8.4%. The customized hedge fund of one launched in 2019 delivered positive returns for the year while trend following generated double-digit performance. Cash also contributed positively due to higher interest rates at the beginning of the year and an allocation to US dollars.

Responsible Investment

The University's Statement of Investment Principles and Beliefs (SIP&B) includes the following statement on responsible investment:

As a long-term investor, the University of Alberta believes that investments in companies with positive attributes such as high ethical standards, respect toward their employees, human rights, and a commitment to the communities in which they do business can improve long-term financial performance. Conversely, investments in companies that manage their environmental, social and governance (ESG) risks poorly can negatively impact returns. The university believes that a proactive approach of engagement on ESG risks and opportunities is more constructive than excluding particular investments.

As of March 31, 2020 the UEP had 88% of its assets managed externally. Of these assets, 89% were managed by signatories to the Principles for Responsible Investment (PRI), a United Nations sponsored organization founded in 2005 and leading proponent of responsible investment. An additional 6% of assets are with firms who belong to the United Kingdom's Stewardship Code or Global Reporting Initiative Sustainability Reporting Guidelines. Nearly all of the UEP's assets remain invested with Environmental, Social, and Governance (ESG) issues considered as part of the investment process.

Specific examples of strong ESG practices from existing investments are outlined below:

Environmental - Recover Energy Services

Recover Energy Services is an Alberta environmental services business that focuses on the recovery and reuse of base oil left on drill cuttings that were created from the use of oil based muds (OBM) in the drilling process. The company has developed a patented technology to recycle drilling waste. Recover's business plan is focused on using this new technology to recycle waste that would have otherwise been disposed of into landfills. Current industry practice is to add sawdust to the drill cuttings and then truck the waste to industrial landfills for disposal. Recover's process displaces the need for specialised landfills by taking this waste material directly from drill sites to its facility near Lodgepole for processing. The results are clean drill cuttings that are disposed of into a standard landfill and refined OBM that is recycled back into the system. Each well produces between 350 and 400 tons of OBM drill cuttings waste. Recover estimates that for each facility it constructs the company can reduce carbon emissions by 71 kT CO₂/year. This represents an 85% reduction as waste materials are no longer evaporating in industrial landfills. Recover is currently planning to expand and setup more recycling facilities across North America.

Social - Empire Company Limited

The University has maintained a long-standing investment in Canadian food retailer Empire Company Limited, parent company of Sobeys, IGA, Safeway, and FreshCo. In addition to 1,500 retail locations across Canada, Empire is in the midst of launching a grocery e-commerce platform powered by tech provider Ocado. Amidst the pandemic, the company has adopted a variety of measures to ensure the safety of its employees and customers such as physical distancing protocols, reduced capacity in its stores, and plexiglass protection for cashiers. Empire has acknowledged its role in society as an essential service and extended wage increases to its front line workers who are ensuring every day that Canadians have economic, reliable, and safe access to food. Furthermore, Sobeys remains committed to reducing food waste by 50% by 2025 and is working with its non-profit partners to address food security through this initiative.

Governance - Altus Group

One of the more recent investments initiated over the past year was Canadian real estate service provider Altus Group. The company provides industry standard and mission critical software, data solutions, and independent advisory services to the commercial real estate sector worldwide. Offering a wide variety of services, Altus has recently adopted a SaaS cloud model, which should have a positive impact on profitability over the coming years. An emphasis on long-term decision making has been an ongoing focus for the company's management team, and Altus prides itself on having some of the best people in the industry due to its ability to attract and retain top talent. Diversity and inclusion programs, competitive compensation and benefits, and a culture of excellence have contributed to this. The company further demonstrates this commitment by having a board constructed of 80% independent directors with diverse expertise, and 30% female representation.

Investment Performance Relative to Peers

The University of Alberta participates in annual benchmark studies with our North American peers. The Canadian Association of University Business Officers (CAUBO) surveys as of December 31. The most recent published data from CAUBO is for the period ending December 31, 2018. This data may make shorter-term comparisons less than informative due to timing. The University's ten-year return of 9.2% for the period ending December 31, 2018 compared with the CAUBO 10 year median return of 9.2%. In the United States, the National Association of College and University Business Officers (NACUBO) in conjunction with Teachers Insurance and Annuity Association of America (TIAA), surveys as of June 30. As US dollar returns can be very different to Canadian dollar returns due to exchange rate movement and allocations to Canadian equities and fixed income, a short-term direct comparison is usually not meaningful. However, over five or ten year periods, the University's returns remain comparable to many larger US endowments.

Costs

The fund incurred direct investment management related expenses of \$10 million or 0.7%. An administrative fee to support centrally funded indirect costs associated with endowment programs is charged to the endowments. For 2020, this amounted to \$9 million or 0.7%.





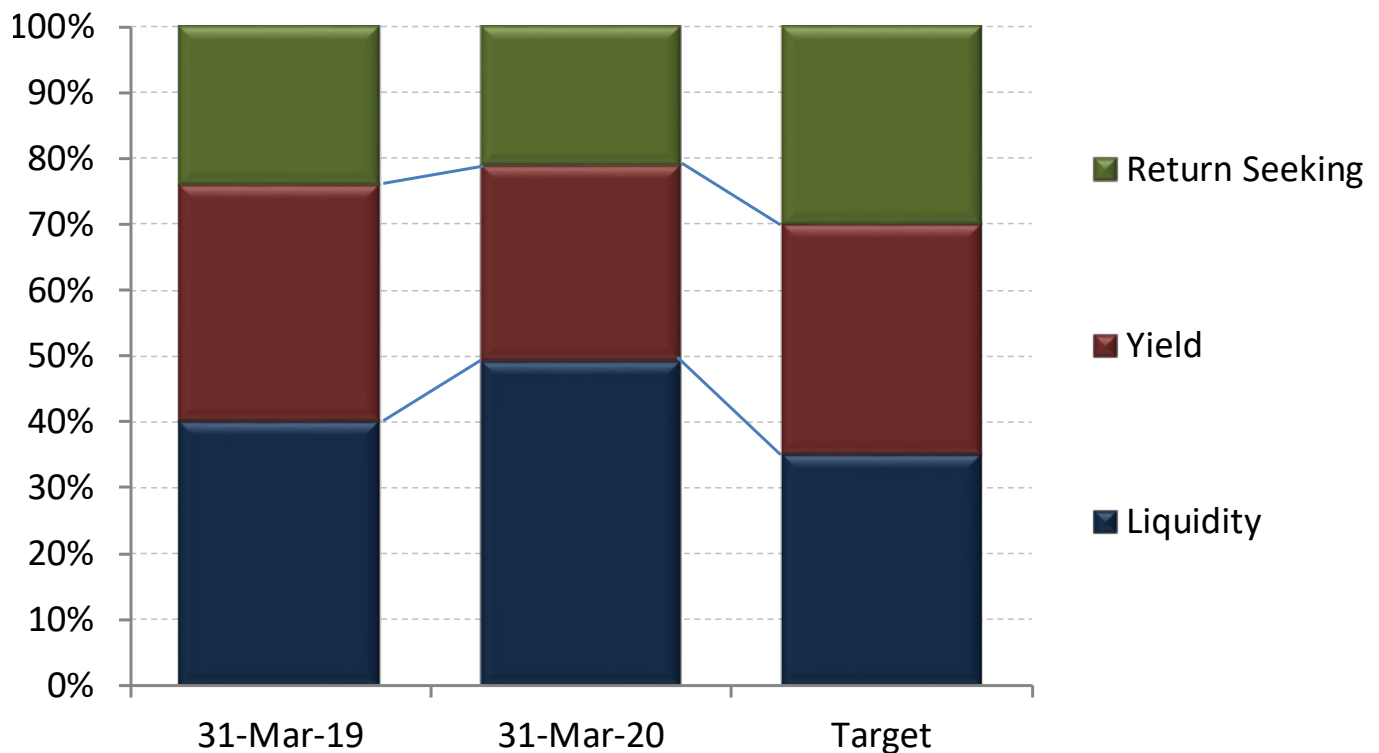
Non-Endowed Funds

The Non-Endowed Investment Pool (NEIP) represents the University's operating, capital, and restricted funds, which are pooled together for investment purposes until required. Long-term cash flow projections indicate that a substantial portion of these funds will not be required in the short-term. Accordingly, Non-Endowed funds are invested across three distinct strategies with varying maturity profiles as summarized in Exhibit 7.

- To meet the University's cash flow requirements, the Liquidity strategy focuses primarily on the preservation of capital and invests in money market securities maturing within one year.
- To generate additional returns above liquidity assets while maintaining an appropriate level of risk, the Yield strategy is permitted to invest in fixed income securities, preferred shares, mortgages, private credit, and absolute return strategies.
- To further enhance long-term returns, the Return Seeking strategy accesses global public and private markets by investing in the UEP.

Exhibit 7

NEIP Asset Allocation by Strategic Role



The NEIP maintained its asset base throughout the year and returned -1.3% compared to the benchmark return of -0.9%. The Liquidity strategy remained overweight and returned 2.1%, which outpaced its Consumer Price Index (CPI) benchmark of 0.9%. The emphasis on Liquidity reflects a conservative stance from Management as fiscal uncertainty was increasing throughout the year.

The Yield strategy returned -0.7% which lagged the revised benchmark (CPI + 3%) of 3.9%. Positive performance from global unconstrained fixed income was offset by negative returns from Canadian preferred shares, which declined markedly after the yield curve sank in early 2020. Towards the end of the year, Management took advantage of attractive valuations and exited its position in internally-managed Canadian fixed income with proceeds moved to the Liquidity strategy.

The Return Seeking strategy invests in the UEP with the expectation that this capital will not be required over the near term. This strategy returned -10.2% compared to its benchmark return of -8.4% and detracted from overall NEIP performance this past year.

Management continues to advance the NEIP closer to its target asset allocation. Upon full implementation, the NEIP is expected to generate higher returns over the medium to long term while maintaining an acceptable level of risk due to diversification. Following a challenging year the value of the Yield and Return Seeking strategies over their underlying obligations stood at \$30 million or 5.8% (2019 - \$56 million or 9.8%) as of March 31, 2020. An excess of 17% is required before any appropriations can be made for strategic initiatives. With interest rates now fractionally above zero it is more critical than ever for the NEIP to reach full implementation to provide increased benefit to the University going forward.

Closing Thoughts and Outlook

The past year will be remembered for some time as fundamental changes to daily life were brought about in response to the pandemic. The University saw classes moved to remotely delivery, with many employees adapting to work from home practices, a routine which is likely continue over the near term. The economic future remains uncertain with the recession expected to leave many companies behind and more people structurally unemployed as a result. Implications of this new reality will likely be an acceleration of trends such as e-commerce, increased adoption of technology, and major changes to how people interact and travel both locally and internationally.

Amidst this challenging backdrop, the real value of the UEP remains healthy, allowing for a continued stable and predictable spending allocation to benefit students, faculty, researchers, and the broader University community. The Investment Committee oversaw Management make significant progress in implementing the strategic asset allocation of both the UEP and NEIP this past year.

Under the purview of the Investment Committee, Management will continue to carry out the implementation of both the UEP and NEIP's long-term strategies. With respect to the UEP, the first comprehensive asset allocation review since 2013 will be completed and provide a road map for several years to come. The NEIP will see capital deployed into mortgages, private credit, and absolute return strategies moving its Yield strategy closer to target. Finally, efforts will continue on ensuring the risk profile of the UEP and NEIP remains consistent with their respective objectives and time horizons.





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