BOARD OF REGENTS
BANKING COMMITTEE

March 21, 2001

The Banking Committee of the Board of Regents met on Wednesday, March 21, 2001, at the University of Northern Iowa, Cedar Falls, Iowa.

Those present were:

Banking Committee members: Regents Ellengray Kennedy (arrived at 1:15 p.m.), Roger Lande, David Neil and Owen Newlin.

Others in attendance were:

Institutional representatives: Mary Sue Coleman, Douglas True, Ann Madden Rice, Cynthia Bartels, Richard Seagrave, Warren Madden, Joan Thompson, Robert Koob, Eunice Dell, Tim McKenna, Gary Shontz, Jim Heuer;

Ken Haynie, Ahlers Law Firm;

Mark Brubaker, Wilshire Associates;

Board Office: Frank Stork, Pamela Elliott, Joan Racki, Deb Hendrickson and Barb Briggle.

Regent Lande called the meeting to order at 1:10 p.m.

APPROVE MINUTES OF THE FEBRUARY 2001 BANKING COMMITTEE MEETING.

MOTION: Regent Newlin moved to approve the minutes of the February 21, 2001, Banking Committee meeting, as written. Regent Neil seconded the motion. MOTION CARRIED UNANIMOUSLY.

INVESTMENT AND CASH MANAGEMENT REPORTS FOR THE QUARTER ENDING DECEMBER 31, 2000.

Director Elliott referred the Banking Committee members to the revised memorandum that was distributed for this item. She said there was an indication that the asset allocation for Iowa State University was out of balance; however, Iowa State University's asset allocation is not out of balance. She then briefly summarized the information which was provided on investment and cash management, noting that for the fourth quarter, the market value of the Regent portfolios exceeded $1 billion.

Mr. Brubaker reviewed with the Banking Committee members the information that was provided by Wilshire Associates for this report. He noted that the report was presented in a slightly different format than was used previously. He stated that the S&P 500 was down 9.1 percent for the year ending December 31, 2000. This was the worst year since 1974 in the U.S. stock markets. It was the first time since 1974 that bonds have outperformed stocks. With regard to international stocks, he said the EAFE is down 14.2 percent for the year. Emerging markets are down almost 32 percent for the year. He presented an update for the current year as of March 20, 2001: The S&P is down 13-1/2 percent, NASDAQ is down 25 percent, the Russell 2000 is down 8.1 percent, bonds are up 3.4 percent, and international stocks are down an additional 13.4 percent. International stock performance is roughly the same as U.S. market performance for the year.

Mr. Brubaker reviewed the specific performance for each fund manager. Seneca is the mid-cap growth manager. He said Seneca had an incredible year last year. It was not their highest return year but it was a strong year relative to the benchmark. The Seneca returns were up almost 14.1 percent in the University of Iowa account and 18.7 percent in the Iowa State University account, versus an index which was down 15.4 percent. He said Sanford Bernstein had a good year in international equities compared to the benchmark. There is a strong value bias in the Bernstein portfolio. Sanford Bernstein is in the top quartile of all international equity managers for the year. Sanford Bernstein underweighted Japan sizably for the year. With regard to the performance of Invesco, he said their tactical decisions between stocks and bonds have done well. However, Invesco has performed below the benchmark for the 5 years.

President Newlin noted that he liked the new format of the report.

Vice President Madden said Iowa State University officials have found it interesting that students are paying their fees earlier versus later. Students are able to pay their bills more promptly than in previous years. (University of Iowa officials noted that the same was not true on their campus.)

ACTION: Regent Lande stated the Banking Committee received the report, by general consent.

PERFORMANCE EVALUATION OF EXTERNAL INVESTMENT FUND MANAGERS.

Regent Lande asked that the fund manager interviews begin with Invesco. Director Elliott suggested that prior to each manager joining the Banking Committee, Mr. Brubaker provide comments in order to stimulate questions or comments of the managers.

Mr. Brubaker stated that in looking at the actual returns for calendar year 2000, Invesco's U.S. equities performed better than the S&P while the fixed income performed a little behind. The longer term numbers are slightly behind the benchmark overall which hurts the overall returns. The Banking Committee members may want to ask about Invesco's fixed income organization being consolidated in Louisville.

Regent Lande asked if Invesco's returns were slightly below the index for the last 5- and 10-year periods. Mr. Brubaker stated that if Invesco had indexed its stocks and bonds and made their asset allocation decisions accordingly, they would have added value over those years. However, when looking at the U.S. equity allocation of the index, they underperformed.

George Hauptfuhrer and Jim Baker of Invesco joined the meeting.

Mr. Hauptfuhrer presented a brief overview of the investment policies and guidelines related to these portfolios.

Mr. Baker presented information on fixed income markets. He stated that, year to date, bonds have had a pretty good year. Bonds played the classic role in asset allocation as a hedge against a weakening stock market. He noted that corporate bond spreads are wide.

Mr. Hauptfuhrer presented an equity market summary. He discussed the cyclicality of growth and value indices as well as the relative performance and valuation of growth versus value. With regard to the performance of the individual portfolios, he said the University of Iowa portfolio (which includes the University of Northern Iowa) was 60 percent stocks, 38 percent bonds and 2 percent short-term investments. He reviewed the performance since inception (4/3/89). The total fund performance was 11.92 percent annually since inception, which he said was way ahead of inflation. Invesco's style will lag in a strong market and will protect on the down side. For the calendar year to date, the endowment performance is down 1.9 percent versus the S&P being down 5.9 percent; Invesco's performance is 4 percent ahead through February. He noted that bonds were up another 1 percent in March to date. Through March 2, the portfolio's stocks were down 1.7 percent while the S&P was down 6.3 percent. Invesco's year-to-date value added is 5.6 percent. Invesco is underweighted in technology; its total return is slightly positive versus the S&P technology stocks. He presented information on asset growth. The value change since inception is $33.6 million for the University of Iowa portfolio and $38.6 million for the Iowa State University portfolio. He then presented an asset allocation summary.

President Newlin asked if Invesco has been a fund manager for the Board of Regents since 1989. Mr. Hauptfuhrer responded affirmatively, saying it had been a great relationship and one which was highly valued.

Mr. Brubaker asked for comment about Invesco's fixed income acquisition and move to Louisville. Mr. Baker stated that Invesco has had four fixed income trader desks. Invesco's new CEO would like to consolidate that to one trading desk in Louisville. For consistency purposes, the intent is to move all of that to Louisville, which will enable Invesco to do an even better job than it has in the past.

Mr. Hauptfuhrer said the building in Louisville is the same building where National Asset Management is headquartered. Invesco has entered into an agreement to acquire that company.

Regent Lande asked where Invesco's equity trading desk was located.
Mr. Hauptfuhrer responded that it is in Atlanta.

Invesco representatives were excused.

Mr. Brubaker stated that Sanford Bernstein representatives would be the next fund managers to be interviewed. The major issue was that the firm merged with Alliance Capital Management last year; Banking Committee members might want to request an update on how that is going.

Sanford Bernstein representatives Andrea Tasker and Jonathan Mann joined the meeting.

Ms. Tasker stated that things had gone smoothly since Sanford Bernstein combined with Alliance Capital Management. She referred to the performance summary provided prior to the meeting and distributed an updated version of the summary. She stated that after underperforming in the second half of 1999, value came back, starting in March 2000. Value had lagged world wide. Beginning in the fourth quarter, the portfolios performed quite strongly and were starting to show a premium in the accounts.

Mr. Mann stated that February 2000 proved to be the point between value and growth in the marketplace; the new economy and the old economy. He presented graphs to communicate how that took place. In the fourth quarter of last year, with Bernstein being a bottom-up manager, the portfolios benefited from significant performance of cyclical companies. He said many companies were still sitting at 50 percent discount. With regard to the solid earnings prospects at low prices of cyclical companies, he said it still looked relatively expensive. With regard to fears of global recession, he said the worldwide slow down has been largely in the U.S. The GDP is generally less than most would believe. Japan is 3 percent of the GDP, driven by trade with the U.S. Europe and Japan are generally more stable than the U.S. currently. With regard to value outperformance, he discussed what did not and what did work. He said it was all part and parcel of the Internet bubble. New economy stocks are now sitting at 34 times earnings. He compared the growth of new economy stocks and old economy stocks.

Mr. Brubaker asked what kind of stocks did Bernstein like in Japan. Mr. Mann responded that Bernstein remains underweighted in Japan. Bernstein runs an unhedged portfolio. He said that to the extent one would make a stock bet toward Japan, one would also be making an underlying currency bet. On the other hand, there are some very interesting Japanese companies; Honda is a great company. While Japan does not look great, if it were pushed to restructure, Bernstein would probably feel more positive about investing in Japan.

President Newlin referred to page 19 of the Bernstein booklet, and asked if the percent of the portfolios in Japan was 19.4. He said it would be good each year for the Banking Committee members to receive such a table of its portfolios, indicating the weight against the benchmarks. Mr. Mann responded that President Newlin was referring to a representative portfolio, not to a Regent account. The Regent portfolios were approximately 17 to 18 percent invested in Japan. The benchmark was 21 to 22 percent; therefore, the portfolios were underweighted in Japan. Overweights were in Europe and Canada.

President Newlin asked if what he read about Japan was overstated; that they are not going in the "tank". Mr. Mann responded that the Japanese mark was up 7-1/2 percent last night.

Regent Lande said the quality of financial reporting in Japan was pretty bad. He asked about the quality of bank reporting generally. Mr. Mann responded that bank reporting was generally improving. There have been some changes made that are beginning to improve the reporting. He noted that some of the stocks were selling at a relatively low price-to-book ratio.

Ms. Tasker stated that she would follow up by providing distribution by country.

Sanford Bernstein representatives were excused.

Mr. Brubaker said there were no issues with Seneca from a performance standpoint. Seneca held up well in a negative environment last year. He said he would be curious to hear where they are finding value in this environment.

President Newlin asked if Seneca was in the top 20 percent of all management firms. Mr. Brubaker responded that, in the mid-cap universe, Seneca ranked in the top 20 percent last year. In the long term, Seneca ranked in the top quartile.

Susan Stannard of Seneca Capital Management joined the meeting. She said this was still proving to be a difficult market, but it was a good time to own bonds. She referred to the fourth quarter synopsis that was provided in Seneca's materials. In looking at what is going on in the economy, she said it was almost somewhat of a recession. The consumer side has held up well; the consumer still seems to be alive and well. The U.S. economy is very resilient and more of a service-based economy. It is not reliant on one to two industries. She expects to see more of a U-type recovery although it was difficult to determine how slow or fast the markets will recover. Market valuation is now more in line with historical averages.

Ms. Stannard reviewed the information that was provided in Seneca's booklet. She presented an organizational update, Seneca's investment objective, and philosophy. She described the status of the portfolio as of December 31 and the cash flow in and out of the portfolio. She then presented a snapshot of the portfolio currently. Thirty-six stocks are being held right now. Seneca is still able to find superior growth rate in companies; they want a growth rate higher than the P/E ratio. She said the top sectors have changed a bit since the end of year. Seneca has been reducing its technology weightings. Energy, health care and some of the financials have helped the portfolio in the last year. She discussed what the sectors looked like as of December 31 and the portfolio characteristics as of that date. The portfolios are invested about 18 percent in health care. She described the portfolio performance for calendar year 2000 and said last year was a good year. The portfolios were up in the double digit range. With regard to how the portfolios are doing year to date, she said they were down 15 to 16 percent through last night. It has been a tough environment. There is a continual loss of consumer confidence. The markets are trying to establish a bottom.

She closed by stating that Seneca is looking for companies that have a proven track record.

Regent Lande stated that when Seneca has such a stellar year, it is difficult to come up with questions!

The Seneca representative was excused.

Mr. Brubaker stated that BlackRock's performance was fine. He noted that they did own Southern California Edison, which has rebounded substantially. Part of the holding was sold at about 80 cents on the dollar.

BlackRock representatives Cheryl Sylwester and Shelley Walker joined the meeting.

Ms. Sylwester provided a business update for BlackRock as well as its investment philosophy and process. She expressed excitement about the fixed income market. With regard to the U.S. economy, she expects a slow down in consumer spending. She said treasury market returned 5 percent during the fourth quarter and was the top performing bond asset class in 2000, returning 13.5 percent. She said BlackRock's strategy has a flattening bias due to its decision to be long in duration, but it favors shorter duration securities in credit-sensitive sectors. Asset-backed securities have done great in 2000 and continue to perform well. BlackRock focuses on high-quality products in that sector of the market. With regard to investment grade corporate bonds, she said the corporate market has suffered quite a bit. More downgrades than upgrades have been seen in the investment grade of corporate bonds.

Ms. Walker provided an analysis of the portfolios and performance. She presented historical portfolio characteristics from December 31, 1999, and December 31, 2000. She provided information on the performance of the portfolios year to date. BlackRock recommends the continued holding Southern California Edison, which is less than 1/2 percent of the portfolios. BlackRock foresees it coming back, hopefully in the next six months. She stated that, for the year, BlackRock has performed very well. She noted that there are very limited guidelines for these portfolios; otherwise, BlackRock could have performed better.

Mr. Brubaker asked how much the guidelines limit the performance. Ms. Sylwester said the guidelines limit the universe. A weighted average life so that it is not a weighted average is often a shorter period than the actual maturity will be.

Vice President True said that could not be done under the statute.

Ms. Sylwester said BlackRock was still doing well, despite the restrictions.

Ms. Walker stated that, last month BlackRock outperformed the benchmark by about 12 basis points. Year-to-date, BlackRock was up 7 basis points over the benchmark. She noted that the portfolios of both the universities are managed exactly the same.

BlackRock representatives were excused from the meeting.

Mr. Brubaker stated that, overall, the portfolios were in good shape. Looking forward, there were some issues. One issue was the possibility of removing the balanced mandate and splitting out the Invesco accounts. Secondly, the historical returns on the U.S. equity portfolios have been quite strong, which was due to Seneca's excellent returns. He noted that Seneca has the potential to underperform the benchmark by that magnitude, as well. He said there is no exposure to small cap value stocks within the equity portfolio. The Banking Committee may want to take steps to reduce the overall risk in the U.S. equity portfolio. There will be a more formal proposal laid out for Banking Committee consideration.

REVENUE BOND FUND AUDIT REPORTS (UNI).

ACTION: Regent Lande stated the Banking Committee deferred action on this item, by general consent,

INTERNAL AUDIT REPORT, UNIVERSITY OF NORTHERN IOWA.

ACTION: Regent Lande stated the Banking Committee deferred action on this item, by general consent,

PRELIMINARY RESOLUTION FOR SALE OF UP TO $23,300,000 ACADEMIC BUILDING REVENUE REFUNDING BONDS, SERIES I.S.U. 2001A AND 2001B.

Mr. Haynie stated that Mark LeMay, Springsted, Inc., provided a refunding analysis. The recommendation is to sell approximately $23 million of new bonds in April to pay off and retire approximately $23 million in outstanding bonds, for a net present value savings of $2.3 million. He said the benchmark of a good refunding is 5 percent savings so this would be a good savings, since the savings are estimated at approximately 10 percent.

Vice President Madden stated that Iowa State University officials believed this was a good time to proceed due to a downturn in interest rates.

MOTION: Regent Newlin moved to recommend that the Board adopt A Resolution authorizing the Executive Director to fix the date or dates for the sale of up to $23,300,000 Academic Building Revenue Refunding Bonds, Series I.S.U. 2001A and 2001B. Regent Neil seconded the motion. MOTION CARRIED UNANIMOUSLY.

ADJOURNMENT.

The meeting of the Regents Banking Committee adjourned at 3:14 p.m. on March 21, 2001.

Pamela M. Elliott Director, Business and Finance	Frank J. Stork Executive Director

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