



Strategic Plan

FY2023 – FY2027

**Endowment Fund Investment
Board of the State of Idaho**

May 19, 2022

Background

When Idaho became the 43rd state in 1890, the Congress of the United States endowed certain lands to be used to generate income for education and other purposes. At statehood, 3.6 million acres of land were granted to the state by the federal government and 2.5 million acres remain. Certain proceeds from the sale of land and income generated by the land have accumulated in the endowment fund, which had assets totaling \$3.1 billion as of June 30, 2021.

Per the Idaho Constitution, the State Board of Land Commissioners oversees the state's endowment assets. The State Board of Land Commissioners is comprised of five elected officials: Idaho's Governor, Secretary of State, Attorney General, Superintendent of Public Instruction and State Controller. Under the direction of the State Board of Land Commissioners, endowment lands are managed by the Idaho Department of Lands and the endowment funds are managed by the Endowment Fund Investment Board, which consists of nine members appointed by the Governor and confirmed by the Senate.

Mission of the Endowment Fund Investment Board

Provide outstanding investment management services to our stakeholders consistent with constitutional and statutory mandates.

Goals

- Meet or exceed the endowment fund's investment benchmark net of fees.
- Meet or exceed the median of our peer group ranking.
- Grow the permanent fund at a rate equal to or greater than inflation and population growth.
- Provide stable annual distributions to endowment beneficiaries.
- Grow beneficiary distributions at the rate of inflation and population growth.
- Maintain adequate earnings reserves to provide a buffer for investment volatility.

Objectives

For our Clients, we will:

- Establish prudent long-term investment policies and strategies that seek to balance risk and return objectives.
- Generate long-term returns consistent with the level of risk associated with the policy asset allocation.
- Utilize outstanding investment managers, consultants, custodians, and other agents to execute those strategies.
- Act professionally, communicate clearly and strive to be a valued partner.

Endowment Fund Clients

Client	Fund
Board of Land Commissioners	Land Grant Endowment Funds
State Insurance Fund	State Insurance Fund
Department of Environment Quality	Bunker Hill Endowment Trust
Department of Environment Quality	Asarco Endowment Trust
Department of Environment Quality	Hecla Endowment Trust
Department of Fish and Game	Southern Idaho Mitigation Endowment Trust
Department of Fish and Game	Craig Mountain Wildlife Mitigation Trust
Department of Fish and Game	Blackfoot Wildlife Mitigation Endowment
Department of Fish and Game	North Idaho Wildlife Mitigation Endowment
Department of Fish and Game	North Idaho Wildlife Operating Fund
Department of Parks & Recreation	Trail of the Coeur d'Alene Endowment
Department of Parks & Recreation	Ritter Island Endowment Fund
Department of Lands	Forest Legacy Funds

Objectives

For our Beneficiaries, we will:

- Strive to make consistent and sustainable annual distributions.
- Strive to maintain earnings reserves sufficient to protect beneficiary distributions from land revenue and investment volatility.
- Strive to grow the permanent corpus at a rate equal to or greater than inflation and population growth.

Endowment Fund Beneficiaries

Public Schools

Charitable Institutions (Idaho State University, State Juvenile Corrections, State Hospital North, Idaho Veterans Homes and the Schools for the Deaf & Blind)

School of Science at the University of Idaho

Normal Schools (Idaho State University and Lewis-Clark State College)

State Hospital South

University of Idaho

Penitentiary

Agricultural College

Capitol Permanent Fund

Objectives

For the State Board of Land Commissioners and Endowment Fund Board, we will:

- Provide resources, information, and support to help the Board of Land Commissioners service as fiduciaries for the land grant beneficiaries.
- Comply with open meeting and public record laws and maintain a website with current and accurate meeting materials to ensure transparent governance.
- Provide consistent and meaningful communication to support effective decision making.

State Board of Land Commissioners

Brad Little, Governor
Lawrence Denney, Secretary of State
Lawrence Wasden, Attorney General
Brandon Woolf, State Controller
Sherri Ybarra, Superintendent of Public Instruction

Endowment Fund Board

Tom Wilford, Chair
Richelle Sugiyama, Vice Chair
Jerry Aldape, Chair of Audit Committee
Robert Donaldson
Joseph Forney
Representative Steven Harris
Irv Littman
Senator Chuck Winder, Chair of Compensation Committee
Brian Yeargain

Objectives

For our Staff, we will:

- Create and maintain an environment that challenges staff to make meaningful contributions and encourages professional development.
- Enhance financial and investment reporting to better communicate performance to stakeholders.
- Improve the use of data analytics to monitor portfolios and investment managers.
- Remain current on investment research and trends.
- Maintain productive relationships with other state agencies.
- Meet at least annually with clients and beneficiaries to provide investment updates and foster collaboration.

Endowment Fund Staff

Chris Anton, Manager of Investments

Chris Halvorson, Investment Officer

Kathy Van Vactor, Fiscal Officer

Liz Wieneke, Office Manager

Key performance measures and benchmarks *(including the rationale for their adoption)*

The efficacy of the Endowment Fund Investment Board can best be measured by:

- Stability and growth of distributions to beneficiaries.
- Maximization of long-term financial returns at a prudent level of risk.
- Growth in permanent corpus to preserve purchasing power for future generations.

Risk/Return Measures & Benchmarks

These measures will be calculated annually and over multi-year periods.

- Measure: Return vs. benchmark
 - Goal: Meet or exceed the endowment fund's investment benchmark gross of fees.
- Measure: Return vs. peers
 - Goal: Meet or exceed median of peer group rankings.

Rationale for establishing these measures/benchmarks

There is no single perfect measure of the performance of an investment portfolio, so multiple performance measurements will be used and calculated for both annual and multi-year periods.

Return vs. benchmark: This is a relative return measure that calculates the value added from “active” versus “passive” investing. One can invest in many asset classes in the financial markets through either index funds or via active management. Index funds essentially own a representative portion of the whole market and are therefore referred to as “passive” investments because they do not attempt to predict which specific securities in the class will perform best. “Active” investing attempts to select the assets within a class that will perform better than average. The efficiency of financial markets makes it challenging to earn an active return in excess of the passive index without taking extra risk.

Return vs. peers: A comparison to relevant peers, allows one to measure whether a fund is doing better or worse than similar participants in the financial markets. It measures a fund's ability to make investment decisions better than average, but is

difficult to achieve over time because, by definition, half of all funds striving to be above average end up being below average. Also, certain peer group data is only available annually and one can never find a perfectly similar peer group, which limits the value of peer comparison.

Land Grant Endowment Growth of Corpus Measures & Benchmarks

- Measure: Percent change in the Permanent Fund
 - Goal: Grow the permanent fund at a rate equal to or greater than inflation and population growth.

Rationale for establishing the measure/benchmark

The mission and ultimate purpose of Idaho's land grant endowments is to provide a perpetual stream of income to the beneficiaries. To balance the needs of current and future beneficiaries, over time the corpus of the endowment funds should grow at a rate equal to or greater than the growth in inflation and population, so that endowment distributions can keep up with the growth in beneficiary funding needs.

Land Grant Endowment Distribution Measures & Benchmarks

- Measure: Stability of distributions to beneficiaries
 - Goal: Provide stable annual distributions to endowment beneficiaries.
- Measure: Level of Earnings Reserves
 - Goal: Maintain adequate earnings reserves to provide a buffer for investment volatility (700% of the last year of approved distributions depending on endowment).
- Measure: Percent change in distributions to beneficiaries
 - Goal: Grow the beneficiary distributions at the rate of inflation and population growth on average over a rolling five-year period.

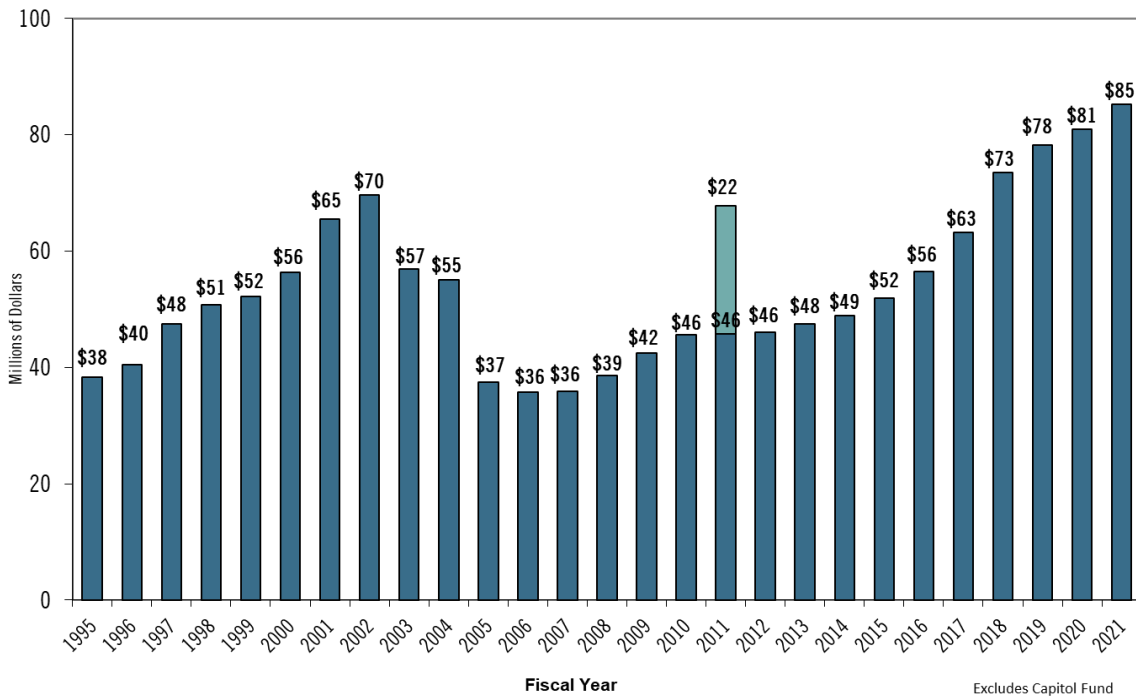
Rationale for establishing the measure/benchmark

The adequacy of the returns of the endowment funds and the efficacy of the Distribution Policy are ultimately measured in terms of the distributions to the beneficiaries, both in absolute dollars and in consistency from year-to-year. While the vision of the state's land and financial endowment assets is to grow distributions over time at a rate equal to or greater than inflation and population growth, endowment beneficiaries experienced declining distributions for four years straight after FY 2002 due to lower timber revenues than expected, especially in FY 2003 and FY 2005, the

significant bear market in equities in 2000-2002 and 2008-2009, and high levels of distributions in FY 2001 and FY 2002 relative to the size of the reserves. The drop in distributions in FY 2003 was especially traumatic, because it coincided with a significant shortfall in expected General Fund revenues. Since most beneficiary funding supports ongoing personnel costs, maintaining consistent distributions year-over-year is strongly preferred. To allow distributions to continue when there is a shortfall in income, the fund maintains reserves of undistributed income.

Beneficiary Distributions 1995-2021

(includes special Public School distribution in 2011 of \$22M)



Earnings Reserve funds for all eight endowments were at target levels at the end of FY 2021. After analyzing the variability of land and fund revenues, the EFIB has determined that having at least seven years of distributions should be sufficient to prevent the need to reduce a beneficiary’s distribution in all but the most extreme disruptions of fund and land revenues. However, if expected land revenues, based on forecasts provided by the Department of Lands, are temporarily much lower than normal, the EFIB may recommend that an endowment temporarily hold additional years of reserves until land revenues recover.

At the end of each fiscal year, any reserves in excess of the level that is determined to be adequate and reasonable to secure future distributions through a market downturn may be transferred to the Permanent Fund. This will allow the Permanent Fund, which is held primarily for the benefit of future beneficiaries, to grow over time at roughly the same rate as the Earnings Reserves, which are primarily for the benefit of current beneficiaries. The policy of setting distributions as a percentage of the Permanent Fund ties growth in distributions to growth in the permanent corpus which further aligning the interests of both current and future beneficiaries.

The Capitol Permanent Fund has a Maintenance Reserve Fund to accumulate earnings in preparation for major maintenance projects at the Capitol Building. The Capitol Reserve is less sensitive to temporary disruptions in annual distributions from its Permanent Fund because annual distributions are normally limited to minor capital improvement projects in anticipation of larger projects in the future.

External factors that could significantly affect the achievement of our goals and objectives

The major outside factors impacting the EFIB are the volatility of investment returns and the level of revenue generated from endowment lands.

Financial Markets

The portfolios managed by the Endowment Fund Investment Board are subject to the variability in the financial markets.

Our investment philosophy values simplicity, transparency, focus and patience. Portfolios are constructed primarily with traditional public equities (domestic equities, international developed market equities, emerging market equities), fixed income securities (treasuries, government agencies, mortgages, asset backed securities, corporate bonds, emerging market bonds and inflation protected securities), and private real estate investments. Most of our investments are in securities that are priced daily and can be easily sold to rebalance the portfolio or provide liquidity.

The single most important factor in determining the absolute level of investment returns is the long-term asset allocation. We use long-term strategic asset class allocations and rebalance to those allocations within suitable ranges. Rebalancing keeps the portfolio diversified and maintains consistent risk/return characteristics. We periodically conduct asset allocation studies to assess the probability of achieving long-term goals and may make adjustments in the allocations to asset classes or sub-asset classes.

The achievement of long-term investment goals is derived from sound investment decisions and efficient and consistent implementation of the strategy. Tactical asset

allocation and frequent manager changes are likely to result in poor outcomes that will impair the long-term performance of the portfolio. Market timing is difficult and ineffective for institutional investors so we remain fully invested in long-term mandates.

We utilize long time frames and appropriate benchmarks to evaluate investment managers. Managers will have periods of both under and out-performance relative to indices and can only be evaluated over a full investment cycle.

The following table outlines the asset allocation of the two portfolios managed by the Endowment Fund Investment Board.

	% of Portfolio Invested	
	Land Grant Endowment Fund	State Insurance Fund
Equities		
Domestic equity	38.0%	10.0%
International equity	19.0%	4.0%
Global equity	<u>9.0%</u>	<u>0.0%</u>
Total Equities	66.0%	14.0%
Fixed Income		
Core	11.0%	44.0%
Core Plus	13.0%	0.0%
Credit	0.0%	12.0%
Securitized	0.0%	12.0%
Treasury	<u>0.0%</u>	<u>12.0%</u>
Total Fixed Income	24.0%	80.0%
Real Assets	10.0%	6.0%
Total	100.0%	100.0%

For the Land Grant Endowment Fund, gains in the Permanent Fund are recognized as income only when the Fund has cumulative gains in excess of inflation. This total real income approach protects the inflation-adjusted corpus or principal in the permanent fund, since gains in any one year will first be applied to offset any past losses in principal. However, this approach will also result in no revenue flowing to reserves in years in which there are cumulative losses in the securities market. Historically, market losses in a 66% equity, 26% fixed income, and 8% real estate portfolio have occurred in one year out of three. Also, in each twenty-five-year historical period there has been one period where no income would have accrued from the permanent fund to earnings reserve for five consecutive years.

Land Revenues

The performance of the land assets is another major external factor that can significantly affect the achievement of the objective of providing sustainable distributions to beneficiaries. About half of the sensitivity of the return on total endowment assets is driven by the net cash earnings on the lands and about half by the total investment return of the funds.

The total cash available for distribution to endowment beneficiaries is highly influenced by variations in net cash earnings of the endowment lands. Over the last fifteen fiscal years, net earnings have averaged \$45 million annually, with a range of about plus or minus \$10 million (about 20%) except for 2010, when revenues plunged 50% below average and 2014, when revenues jumped almost 40% above average.

