AGENDA

COMMITTEE ON FINANCE

Meeting: **3:00 p.m., Tuesday, September 24, 2019**
Glenn S. Dumke Auditorium

Lillian Kimbell, Chair
Jack McGrory, Vice Chair
Larry L. Adamson
Jane W. Carney
Rebecca D. Eisen
Juan F. Garcia
Hugo N. Morales
Romey Sabalius
Lateefah Simon
Peter J. Taylor

Consent
1. Approval of Minutes of the Meeting of July 23, 2019, *Action*
2. California State University Quarterly Investment Report, *Information*

Discussion
3. Planning for the 2020-2021 Operating Budget, *Information*

MINUTES OF THE MEETING OF THE COMMITTEE ON FINANCE

Trustees of the California State University
Office of the Chancellor
Glenn S. Dumke Conference Center
401 Golden Shore
Long Beach, California

July 23, 2019

Members Present

Lillian Kimbell, Chair
Jack McGrory, Vice Chair
Rebecca D. Eisen
Jane W. Carney
Juan F. Garcia
Hugo N. Morales
Romey Sabalius
Lateefah Simon
Peter J. Taylor
Adam Day, Chairman of the Board
Timothy P. White, Chancellor

Trustee Lilian Kimbell called the meeting to order.

Public Comment

Public speakers expressed concern over the proposed application fee increase and proposed change to Title 5 that would allow the California State University Board of Trustees to set the application fee. They also made comments about CSU administrators and the recent state audit report.

Approval of Minutes

The minutes of the May 21, 2019 meeting of the Committee on Finance were approved as submitted.

Approval to Issue Systemwide Revenue Bonds for a Housing Project at California State University, Long Beach and Recreation Center Expansion at San Diego State University

Trustee Kimbell presented agenda item three as a consent action item. The committee recommended approval of the proposed resolution (RFIN 07-19-04).

Admission Application Fee Proposal and Title 5 Revision

Information about a proposed $15 increase to the CSU Admission Application Fee and corresponding changes to Title 5 were presented for approval. The fee has not been changed since 1989 and revenue will help support the Cal State Apply application system and facilitate review of redirected applications.

Following the presentation the trustees asked clarifying questions about the proposed amendment to Title 5, the process for notifying the public of proposed changes, and distribution of funds to the campuses. They also discussed elements of the application system and resources available to students to help them determine if a campus is impacted prior to applying.

Appointment of the California State University Investment Advisory Committee

The trustees were informed of the decision to keep Trustee Peter J. Taylor as the chair of the CSU Investment Advisory Committee. Trustee Rebecca Eisen expressed support.

2019-2020 Final Budget

Information about final California State Budget allocations to the CSU was presented, including funded components of the trustees' budget request and new reporting requirements.

Following the presentation, the trustees commented on the funding received for mental health services and legal services for undocumented students. They asked about the process for developing the required new campus studies and requested that a sustainable funding model be secured from the state prior to creating another campus. They also asked how budget request shortfalls will be handled and about reporting of tenure-track hiring.

Trustee Kimbell adjourned the meeting on Finance Committee.

COMMITTEE ON FINANCE

California State University Quarterly Investment Report

Presentation By

Steve Relyea
Executive Vice Chancellor and
Chief Financial Officer

Robert Eaton
Assistant Vice Chancellor
Financing, Treasury, and Risk Management

Summary

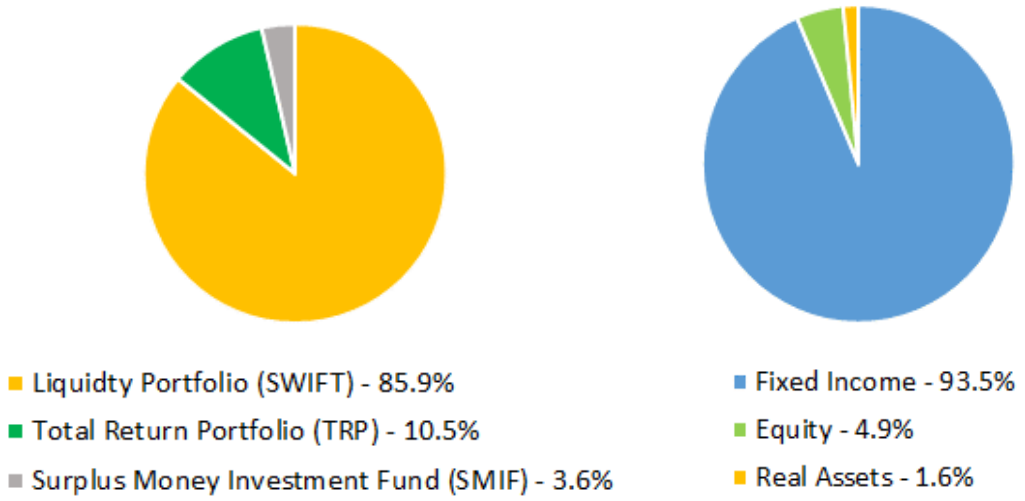
This item provides the quarterly investment report to the California State University Board of Trustees for the fiscal quarter ended March 31, 2019. The information in Attachment A provides the entire quarterly investment report regarding CSU investments as required by California Education Code section 89726.

Background

Pursuant to the CSU Master Investment Policy (included as Attachment B), CSU investments as of March 31, 2019 consisted of investments in the Liquidity Portfolio (Systemwide Investment Fund Trust or SWIFT), the Total Return Portfolio (TRP), and the State of California Surplus Money Investment Fund (SMIF). Except for amounts held at the State in SMIF, all CSU investments are held by US Bank, the custodian bank for the CSU. Neither state general fund nor CSU auxiliary funds are included in CSU investments. In addition, this report does not include approximately $850 million in bond proceeds, which by state law are required to be held by the state and are invested in SMIF.

CSU Investments – Balances, Allocations, and Returns
March 31, 2019

	Balance	% of CSU Investments	Twelve Month Returns
Liquidity Portfolio (SWIFT)	$4.10 billion	85.9%	2.59%
Total Return Portfolio (TRP)	$502 million	10.5%	6.69%
Surplus Money Investment Fund (SMIF)	$170 million	3.6%	1.82%
CSU Investments	**$4.77 billion**	**100%**	



CSU Investment Portfolios

For detailed information on the investment performance and characteristics of the CSU investment portfolios, please see Attachment A.

CSU Liquidity Portfolio (Systemwide Investment Fund Trust or SWIFT)

The purpose of the Liquidity Portfolio is to provide sufficient and immediate liquidity to meet the operating needs of the CSU. The investment objective is safety of principal and liquidity.

The Liquidity Portfolio is managed through contracts with two investment management firms, US Bancorp Asset Management and Wells Capital Management, each of whom provides investment management services for the program. While the custodian, US Bank, holds the funds invested in the Liquidity Portfolio, for investment management purposes additions to the portfolio are split evenly between the investment managers and invested according to permitted investments outlined in the Government Code of the State and the Liquidity Portfolio investment policy. Consistent with state law, the Liquidity Portfolio is restricted to high quality, fixed income securities.

CSU Total Return Portfolio (TRP)

Legislation effective January 1, 2017 expanded the CSU investment authority to allow investment in mutual funds (including equity mutual funds) and real estate investment trusts. The Total Return Portfolio was created to take advantage of the new investment authority.

The purpose of the TRP is to provide opportunity for additional risk adjusted returns on CSU funds over a full market cycle. The investment objective is to achieve a prudent return within a moderate risk level.

Under State law, investment of funds in the TRP is subject to the CSU meeting certain conditions regarding investment oversight, reporting, and use of earnings, and may not be more than $600 million as of June 2019, nor more than thirty percent of eligible CSU investments thereafter. The CSU Investment Advisory Committee (IAC), established by the Board of Trustees in September 2017, oversees the TRP and focuses on key issues such as investment policy, asset allocation, investment manager oversight, and investment performance.

The TRP investment policy provides a framework for the investment of portfolio funds in the TRP and includes the following key elements as further described in the TRP Investment Policy:

- Investment Objectives
- Spending Policy
- Time and Investment Horizon
- Risk Tolerance
- Expected Return
- Asset Allocation
- Benchmarks
- Investment Manager Selection
- Roles & Responsibilities
- Environmental, Social and Governance Framework
- Risk Management
- Monitoring and Control Procedures

The IAC has adopted an investment schedule for the TRP that utilizes a dollar-cost averaging approach and provides regular monthly contributions to the TRP. An initial investment of $33.5 million into the TRP was made on April 1, 2018, with the goal of reaching the fiscal year 2018-2019 statutory limit of $600 million in the first half of 2019. After June 30, 2019, implementation of a revised investment schedule established by the IAC and staff will commence, as the TRP can be increased to as much as 30 percent of CSU investments at that time. The investment schedule may also be adjusted by the IAC at any time depending on market conditions. Consistent with state law, specifically Education Code 89726, additional moneys earned through investments in the TRP shall be used only for capital outlay or maintenance, and shall not be used for ongoing operations.

The purpose of the TRP is to provide opportunity for additional risk adjusted returns on CSU funds over a full market cycle. For the year ending March 31, 2019, the TRP total return exceeded the Liquidity Portfolio (SWIFT) total return by 4.15 percent (net of fees) or $9.8 million.

Surplus Money Investment Fund (SMIF)

The State Treasurer also provides investment vehicles that may be used for CSU funds. The Surplus Money Investment Fund (SMIF) is used by the State Treasurer to invest state funds, or funds held by the state on behalf of state agencies, in a short-term pool. In order to facilitate certain expenditures, the CSU maintains small amounts of funds with the State. The portfolio includes Certificates of Deposit, Treasuries, Commercial Paper, Corporate Bonds, and U.S. Government Agencies.

Next Steps

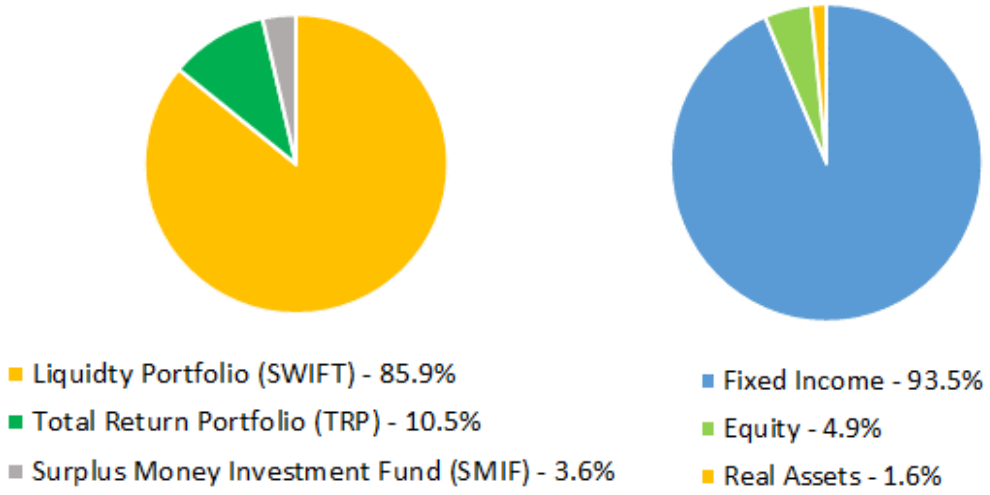
Staff will continue implementing the TRP investment schedule with oversight from the IAC. Staff is also working on developing the Intermediate Duration Portfolio, consistent with the CSU Master Investment Policy, with the goal of implementing this portfolio in late 2019 or early 2020. The next investment report to the Board of Trustees is scheduled for November 2019 and will provide information on the fiscal year ending June 30, 2019.

CSU Quarterly Investment Report
For the Quarter Ended March 31, 2019

CSU investments as of March 31, 2019 consisted of investments in the CSU Liquidity Portfolio (Systemwide Investment Fund Trust or SWIFT), the Total Return Portfolio (TRP), and the State of California Surplus Money Investment Fund (SMIF). All CSU investments (except for funds invested in SMIF) are held by US Bank, the custodian bank for the CSU. Neither state general fund nor CSU auxiliary funds are included in CSU investments. In addition, this report does not include approximately $850 million in bond proceeds, which by state law are required to be held by the state and are invested in SMIF.

Balances and Allocations as of March 31, 2019

	Balance	% of CSU Investments
Liquidity Portfolio (SWIFT)	$4.10 billion	85.9%
Total Return Portfolio (TRP)	$502 million	10.5%
Surplus Money Investment Fund (SMIF)	$170 million	3.6%
CSU Investments	**$4.77 billion**	**100%**



For the nine months ended March 31, 2019, direct investment management fees[1], advisory, and custodial fees totaled just over $1.67 million, or about 0.035 percent (3.5 basis points) on CSU investments total balance as of March 31, 2019.

[1] Direct investment management fees exclude TRP mutual fund investment management fees. TRP mutual fund investment management fees are included as mutual fund expenses and reported as a percent of total fund assets. See TRP Fund Expense Ratio (Fee) in the table on page 3.

CSU Liquidity Portfolio (Systemwide Investment Fund Trust or SWIFT)

The purpose of the Liquidity Portfolio is to provide sufficient and immediate liquidity to meet the operating needs of the CSU. The investment objective is safety of principal and liquidity. Consistent with state law, the portfolio is restricted to high quality, fixed income securities.

	CSU Liquidity Portfolio	Benchmark[2]
1 Year Annualized Return[3]	2.58%	2.59%
3 Year Annualized Return	1.31%	1.08%
5 Year Annualized Return	1.12%	0.94%
10 Year Annualized Return	0.94%	0.90%
Annualized Since Inception Return[4]	1.34%	1.59%
Yield	2.44%	2.37%
Duration (Years)	0.85	1.49
Average Credit Rating	AA-	Aaa/AA+

Holdings by Asset Type (% of CSU Liquidity Portfolio):

Treasuries	31.76%
U.S. Government Agencies	30.71%
U.S. Corporate Bonds	24.82%
CD's and Cash Equivalents	6.47%
Asset-Backed Securities	5.01%
Municipal Obligations	1.23%

[2] Benchmark for the CSU Liquidity Portfolio (SWIFT) is the Bank of America Merrill Lynch 0-3 Year Treasury Index.
[3] CSU Liquidity Portfolio (SWIFT) returns reported as gross of fees and total return, including income and gains (realized and unrealized).
[4] Inception Date for the CSU Liquidity Portfolio (SWIFT) was July 1, 2007.

CSU Total Return Portfolio (TRP)

The purpose of the Total Return Portfolio is to provide opportunity for additional risk adjusted returns on CSU funds over a full market cycle. The investment objective is to achieve a prudent return within a moderate risk level. Consistent with state law, the TRP is invested in mutual funds subject to registration by and under the regulatory authority of the United States Securities and Exchange Commission or in United States registered real estate investment trusts.

	CSU Total Return Portfolio[5]	Strategic Benchmark[6]	Policy Benchmark[7]
3 Months Return	9.53%	2.18%	9.37%
1 Year Return	6.69%	6.62%	4.65%
Annualized Since Inception Return[8]	6.69%	6.62%	4.65%

Holdings by Asset Type (% of CSU Total Return Portfolio):

Equity Mutual Funds	46%	Passive Index Mutual Funds	74%
Fixed Income Mutual Funds	39%	Actively Managed Mutual Funds	26%[9]
Real Asset Mutual Funds	15%		

For the one year ending March 31, 2019, the TRP total return exceeded the Liquidity Portfolio (SWIFT) total return by 4.15 percent (net of fees) or $9.8 million.

Finally, during the quarter, consistent with the TRP implementation plan, the Investment Advisory Committee approved replacing passive Vanguard funds for Emerging Market Equity and Emerging Market Debt with the following active investment managers:

Emerging Market Equity

- Driehaus Emerging Markets Growth Fund
- DFA Emerging Markets Value Portfolio
- RWC Global Emerging Equity Fund

Emerging Market Debt

- Payden Emerging Markets Bond Fund
- T. Rowe Price Emerging Markets Bond Fund

Values, Holdings & Fees (CSU Total Return Portfolio)

[5] TRP Returns are net of mutual fund investment management fees and expenses.
[6] The TRP Strategic Benchmark is Inflation (Core Consumer Price Index) plus 4.5% per annum. The long-term rate of inflation is assumed at 2.5% per annum.
[7] The TRP Policy Benchmark is a blend of passive indices whose weights match the TRP target asset allocation.
[8] TRP Inception Date was April 1, 2018.
[9] The percent of Actively Managed Mutual Funds is likely to increase marginally in the future while the percent of Passive Index Mutual Funds would decrease marginally consistent with the TRP implementation plan.

Asset Class	Strategy Name	Ticker	Value (millions)	% of Total Return Portfolio	TRP Fund Expense Ratio (Fee)	Universe Median Expense Ratio (Fee)
Fixed Income						
	Vanguard Total Bond Market Index Fund	VBMPX	109.8	22%	0.030%	0.490%
	Vanguard Inflation-Protected Securities Fund	VIPIX	25.0	5%	0.070%	0.450%
	Lord Abbett High Yield Fund	LHYOX	30.1	6%	0.600%	0.730%
	Pacific Funds Floating Rate Income Fund	PLFRX	15.0	3%	0.720%	0.760%
	Payden Emerging Markets Bond Fund	PYEIX	7.5	1.5%	0.690%	0.850%
	T. Rowe Emerging Markets Bond Fund	TREBX	7.5	1.5%	0.700%	0.850%
Equity						
	Vanguard Total Stock Market Index Fund	VSMPX	120.8	24%	0.020%	0.780%
	Vanguard Developed Markets Index Fund	VTMNX	60.1	12%	0.060%	0.910%
	Driehaus Emerging Markets Growth Fund	DIEMX	30.3	6%	1.210%	1.160%
	DFA Emerging Markets Value Fund	DFEVX	15.1	3%	0.540%	1.160%
	RWC Global Emerging Equity Fund	RWCEX	5.1	1%	1.250%	1.160%
Real Assets						
	Vanguard Real Estate Index Fund	VGSNX	35.4	7%	0.100%	0.910%
	Vanguard Energy Index Fund	VENAX	10.0	2%	0.100%	1.030%
	Vanguard Materials Index Fund	VMIAX	10.1	2%	0.100%	0.990%
	First State Global Listed Infrastructure Fund	FLIIX	19.9	4%	0.950%	0.985%
Cash			0.0	0%	NA	NA
Total			501.8	100.00%		

Surplus Money Investment Fund (SMIF)

The Surplus Money Investment Fund (SMIF) is managed by the State Treasurer to invest State funds, or funds held by the State on behalf of State agencies, in a short- term pool. The portfolio includes Certificates of Deposit, Treasuries, Commercial Paper, Corporate Bonds, and U.S. Government Agencies.

Apportionment Annual Yield[10]	
Trailing 12 month as of 3/31/19	1.82%
Average Annualized (FYE 06/30/07 – 3/31/19)	1.08%

[10] Annual Yield calculated by CSU Treasury Operations based on the quarterly apportionment yield rates published by the State Controller's Office.

The California State University
OFFICE OF THE CHANCELLOR

Master Investment Policy

For The California State University

Approved on November 8, 2017
By The Board of Trustees of The California State University

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I. Scope and Purpose

This California State University Master Investment Policy ("MIP") governs the investment of California State University ("CSU") funds. CSU investments are centrally managed on behalf of the CSU System and its campuses.

The purpose of the MIP, together with investment policies that govern individual Portfolios (as defined in Section IV) and are created pursuant to delegated authority contained herein, is to provide a framework for the investment of CSU funds consistent with the goals of the CSU Board of Trustees (the "Board") and the educational mission of the CSU.

The MIP sets forth objectives, guidelines, and responsibilities that the Board deems to be appropriate and prudent in consideration of the needs of, and the legal requirements applicable to, the CSU's investment program. The MIP is also intended to ensure that the Board, and any parties to whom the Board delegates authority, are fulfilling their fiduciary responsibilities in the oversight of CSU investments.

The MIP is a dynamic document and will be reviewed from time to time. The MIP will be modified, if necessary, to reflect the changing nature of the CSU's assets and investment program, organizational objectives, and economic conditions.

II. Compliance with Law and Adherence to Policy

CSU investments are to be managed in full compliance with all applicable laws, rules, and regulations from various local, state, federal, and international political entities that may impact the CSU's assets, including but not limited to the provisions of the California Education Code and California Government Code applicable to the investment of CSU funds, and in accordance with the policy objectives, guidelines, and responsibilities expressed herein.

III. Background and Investment Objectives

The investment objectives for the investment of CSU funds have been established in conjunction with a comprehensive review of current and projected financial requirements. The Board desires to provide the Chancellor, the Chancellor's Staff, and the IAC (as defined in Section V) with the greatest possible flexibility to maximize investment opportunities. However, as agents of the Board, the Chancellor, the Chancellor's Staff, and the IAC must recognize the fiduciary responsibility of the Board to conserve and protect the assets of the CSU investment program, and, by prudent management, prevent exposure to undue and unnecessary risk.

The following objectives shall govern the investment of CSU funds:

1. Safeguard the principal.

2. Meet the liquidity needs of the CSU.

3. Obtain the best possible return commensurate with the degree of risk the CSU is willing to assume in obtaining such return.

The Board acknowledges that these objectives may be weighted or prioritized differently for individual Portfolios depending upon the purpose of the Portfolio.

IV. Investment Portfolios

Consistent with its investment objectives, the Board has determined that CSU funds may be invested in three investment portfolios (individually, a "Portfolio" and together, the "Portfolios") created by the CSU, with oversight by the Chancellor, the Chancellor's Staff, and the IAC, and each with its own investment policy.

The three Portfolios and general purpose of each Portfolio are as follows:

Liquidity Portfolio (Systemwide Investment Fund—Trust or "SWIFT")

The purpose of this Portfolio is to provide sufficient and immediate liquidity to meet the operating needs of the CSU. The investment objectives for this Portfolio shall be safety of principal and liquidity. The existing CSU Systemwide Investment Fund—Trust (SWIFT) shall serve as the Liquidity Portfolio and shall be comprised of investments authorized pursuant to California Government Code Sections 16330 or 16430.

Intermediate Duration Portfolio (IDP)

The purpose of this Portfolio is to provide opportunity for modest, additional risk adjusted returns on CSU funds not needed for immediate liquidity. The investment objectives for this Portfolio shall be safety of principal, liquidity and return. The Intermediate Duration Portfolio shall be comprised of investments authorized pursuant to California Government Code Sections 16330 or 16430.

Total Return Portfolio (TRP)

The purpose of this Portfolio is to provide opportunity for additional risk adjusted returns on CSU funds over a full market cycle. The investment objectives for this

Portfolio shall be to achieve a prudent total return within a moderate risk level. The Total Return Portfolio shall be comprised of investments authorized pursuant to California Government Code Sections 16330, or 16430 or California Education Code Sections 89724 or 89725.

The acceptable allocations for the Portfolios are as follows:

Portfolio	**Min – Target – Max**
Liquidity – Systemwide Investment Fund Trust ("SWIFT")	**5% - 20% - 100%**
Intermediate Duration Portfolio ("IDP")	**0% - 52% - 95%**
Total Return Portfolio ("TRP")	**0% - 28% - 30%**[1]

In addition, the CSU may invest any amount (from 0% to 100%), in any California State Treasury investment option, available now, or in the future, that the IAC and the Staff deem prudent, including, but not limited to:

- Surplus Money Investment Fund (SMIF)
- Local Agency Investment Fund (LAIF)

V. Roles and Responsibilities

Board of Trustees

The Board assumes fiduciary responsibility to conserve and protect the investment assets of the CSU, and by prudent management, to prevent exposure to undue and unnecessary risk. However, the Board also acknowledges investments are inherently risky with risk of loss and, as such, are viewed with a long-term time horizon.

As a fiduciary, the primary responsibilities of the Board are to:

1. Maintain and approve the MIP.

[1] Percentage allocations to the TRP are subject to annual phase-in restrictions through June 30, 2020 per state law.

2. Ensure that CSU investments are prudently diversified in order to obtain the best possible return commensurate with the degree of risk that the CSU is willing to assume.

3. Report annually to the California state legislature and the California Department of Finance regarding the investment of CSU funds.

The Board shall have oversight responsibility for investment of the assets and has delegated investment authority to the Chancellor, the Chancellor's Staff, and the IAC.

Chancellor and Chancellor's Staff

As agents of the Board, the Chancellor, the Executive Vice Chancellor and Chief Financial Officer, the Assistant Vice Chancellor responsible for CSU investments, and their designees (the "Chancellor's Staff"), recognize the fiduciary responsibility of the Board to conserve and protect the investment assets of the CSU and, by prudent management, to prevent exposure to undue and unnecessary risk.

The Chancellor and the Chancellor's Staff are hereby authorized to establish policies and procedures to implement the provisions of this MIP, including, but not limited to, the following activities:

1. Overseeing and implementing general administrative and investment operations for the Portfolios.

2. Informing the IAC on the overall investments of the CSU and each of the Portfolios to assist the IAC in fulfilling its duties.

3. Developing and implementing policies that are suitable for achieving the strategic objectives for each Portfolio, including coordination with the IAC in developing and implementing policies for the TRP.

4. Selecting, contracting with, and monitoring third party service providers, including, but not limited to, investment advisors, investment managers, and custodians. For the TRP, such actions will be based on the recommendations of the IAC.

5. Directing the investment of funds, including the ordering of purchase and sale transactions to, from and between the Portfolios to meet investment objectives and strategic asset allocations.

6. Monitoring and reviewing the performance of the Portfolios to their stated objectives.

7. Reporting to the Board regarding the investment of CSU funds as requested, but no less than quarterly.

8. Controlling and accounting for all investment, record keeping, and administrative expenses associated with the Portfolios.

9. Identifying the need for updates, monitoring the Portfolios for legal and policy compliance, and acting on the recommendations of the IAC, as appropriate.

10. All other duties designated or delegated by the Board or the IAC.

Investment Advisory Committee

As required by state law, the CSU has created an Investment Advisory Committee (the "IAC"), to provide investment advice and expertise to the Board, particularly with respect to the management of the TRP.

The IAC shall be an advisory body and shall make recommendations, as appropriate, to the Board for approval or to the Chancellor and the Chancellor's Staff for implementation. The IAC shall be responsible for overseeing all aspects of the TRP and is hereby authorized to recommend policies and procedures for the creation and implementation of the TRP, including, but not limited to, the following activities:

1. Understanding the overall investments of the CSU and each of the Portfolios as informed by the Chancellor's Staff, investment advisors and/or investment managers.

2. Developing and approving an IAC charter to establish guidelines for operations of the IAC.

3. Developing, approving, and overseeing the implementation of an investment policy statement for the TRP.

4. Reviewing and approving target asset allocations and ranges for the TRP.

5. Monitoring and reviewing the performance of the TRP to its stated objectives.

6. Prudently reviewing, selecting, monitoring, and replacing investment management firms engaged to manage the TRP's assets.

7. Monitoring and supervising all service vendors and fees for the TRP.

8. Any other investment or administrative duties deemed necessary to prudently oversee the investment program for the TRP.

Prudence, Ethics and Conflict of Interest

All participants in the investment process shall act responsibly. The standard of prudence applied by the Board, the Chancellor, the Chancellor's Staff, and the IAC, as well as any external service providers, shall be the "prudent investor" rule. The "prudent investor" rule in part, states, "A trustee shall invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill and caution. A trustee's investment and management decisions respecting individual assets must be evaluated not in isolation but in the context of the trust portfolio as a whole and as part of an overall investment strategy having risk and return objectives reasonably suited to the trust."

Furthermore, all participants in the investment process shall use the same care, skill, prudence, and due diligence under the circumstances then prevailing that a prudent person acting in a like capacity and fully familiar with such matters would use in the conduct of an enterprise of like activities for like portfolios with like aims and in accordance and compliance and all other applicable laws, rules and regulations.

All investment personnel shall refrain from personal business activity which could create a conflict with proper execution of the investment program, or which could impair the ability to execute impartial investment decisions. All investment personnel shall disclose to the Chancellor's Staff or the IAC any material financial interests in financial institutions which conduct business within the jurisdiction and shall disclose any material financial investment positions which could be related in a conflicting manner to the performance of the Portfolios. All investment personnel shall report any potential conflicts of interest consistent with Government Code Section 87200. Further, the Chancellor shall report to the Board in writing any issues that could reflect any conflict in the performance of the Portfolios.

Document Acceptance of the Investment Policy Statement

The Chancellor's Staff shall provide a copy of this MIP, and the relevant Portfolio investment policy, to each firm retained to provide investment services to the CSU and each such firm shall acknowledge in writing receipt of the document and accept its content.

VI. Environmental, Social and Governance Framework

The Board acknowledges the importance of understanding the potential risks and value that environmental, social, and governance ("ESG") factors may have on CSU investments. Therefore, the Board expects that the consideration of ESG factors shall be integrated into the investment decision processes of the CSU.

Approved:

The California State University Board of Trustees
November 8, 2017

COMMITTEE ON FINANCE

Planning for the 2020-2021 Operating Budget

Presentation By

Steve Relyea
Executive Vice Chancellor and
Chief Financial Officer

Ryan Storm
Assistant Vice Chancellor
Budget

Summary

The California State Constitution requires the submittal of the governor's budget proposal each year by January 10. In order to meet consequent deadlines of the Department of Finance, it is necessary to commence planning for the 2020-2021 California State University Operating Budget. The CSU Board of Trustees will be provided preliminary assumptions for purposes of preparing the 2020-2021 budget request to the governor. The final budget request will be presented to the Board of Trustees for review and approval in November 2019.

State Budget Overview

As the 2019-2020 budget year begins, and the CSU looks ahead to the 2020-2021 fiscal year, California remains the fifth largest economy in the world with a gross domestic product (GDP) of almost $3 trillion. However, this strong foundation is also facing increasing risks including slower economic growth, larger federal deficits, threat of natural disaster, and unexpected cost increases. The Department of Finance projects slower but continuous growth through 2022-2023, but also warns that a recession could result in a $65 billion to $70 billion revenue decline over three years. Similarly, the Legislative Analyst's Office projects slower, but continuous revenue growth over the coming years but also indicates that a moderate recession could amount to a decline in revenue of $10 billion over three years, which would be $46 billion below the current growth projections for the next three years.

Paying down liabilities and building a rainy-day fund have been top priorities for Governor Newsom's administration. Without an uptick in economic growth, California could make more modest new investments in the coming years, focusing more on one-time allocations and continued savings. In his first budget proposal, Governor Newsom emphasized three high-level priorities beyond fiscal resiliency, which include: effective government, affordability and opportunity, and

justice and dignity. These fiscal policy priorities could be present throughout his administration. With the potential for a more volatile economy for 2020-2021, it is difficult to estimate what the governor and legislature will choose to support with recurring new revenues in the next fiscal year.

Recent Funding of the CSU

The 2019-2020 CSU Operating Budget Request of $554 million was the largest in recent history. Governor Newsom's first budget, in partnership with the legislature, showed their commitment to the university when they provided $332.9 million in new recurring funds. Combined with new tuition revenue from growth in enrollment, the CSU's budget grew by $379 million to reach a total operating fund budget of $7.1 billion for 2019-2020. Recent growth in the CSU operating budget is detailed in the chart below:

Fiscal Year	Total Operating Fund Budget	% Growth
2015-16	$5,680,022,000	6.2%
2016-17	$6,065,892,000	6.8%
2017-18	$6,435,660,000	6.1%
2018-19	$6,721,056,000	4.4%
2019-20	$7,146,814,000	6.3%

New Investment from the State

Over the last several weeks, Chancellor's Office staff have met with many stakeholder groups to solicit feedback on the potential contents of the 2020-2021 Operating Budget Request. Based on that feedback, the preliminary 2020-2021 budget plan would allow the CSU to both catch-up and provide another round of investment in Graduation Initiative 2025, grow full-time equivalent student (FTES) enrollment, cover mandatory cost obligations, and provide fair compensation for all employee groups. Additionally, progress could be made on infrastructure and deferred maintenance needs. These align with the Board of Trustees' long-standing priorities and the preliminary expenditure plan below reflects those priorities.

The 2020-2021 budget request will assume that the state continues to see positive state revenue growth for at least another 12 to 18 months, and will presume continued investment by the state in the CSU. To encourage that continued investment, the Chancellor's Office will initiate conversations this fall with the governor's administration to discuss possible elements of a multi-year plan or agreement between the state and the CSU.

If a recessionary event were to affect the state budget picture sooner rather than later, the CSU would explore and implement some combination of the following strategies:

- Use reserves designated for economic uncertainty on a one-time basis;
- Limit investment in new budget priorities;
- Redirect existing campus resources toward significant priorities;
- Explore new revenue sources; and
- Discuss a possible increase in tuition.

The Chancellor's Office would continue to engage with students, faculty, staff, campus executives, the state, and other CSU stakeholders to garner state support then explore alternatives for balancing budget priorities and necessary resources.

2020-2021 CSU Operating Budget—Preliminary Planning Approach

It is very early in the budget development process and appropriate for the Board of Trustees to begin discussion of CSU priorities for the 2020-2021 Operating Budget Request. The planning approach presented below represents a range of funding levels that can be balanced to communicate the university's key funding needs. At this stage, it is important for the Board of Trustees to provide input on fiscal policy priorities for 2020-2021.

These estimated incremental funding amounts or ranges provide an opportunity for discussion about priorities and would add to the 2019-2020 base budget of $7.1 billion.

Preliminary Expenditure Plan - $497 Million to $620 Million

Graduation Initiative 2025 - $105 million

The CSU will continue to invest in people, programs, technologies, and strategies that have demonstrated success in improving graduation rates, shortening time-to-degree, and eliminating equity gaps. Each campus has developed multi-year plans to reach their Graduation Initiative 2025 goals that will require multi-year investments across the system in the six pillars of the initiative:

- Academic preparation
- Enrollment management
- Financial aid
- Data-driven decision making
- Administrative barriers
- Student engagement and well-being

Because the governor and legislature provided financial support in 2019-2020 for activities related to the student engagement and well-being pillar (e.g. student mental health, emergency student housing, and basic needs partnerships), it is worth noting that the CSU has addressed, and will continue to address, the well-being of all CSU students through these and many other related activities with Graduation Initiative 2025 funding. Over the course of this fourth year of the Graduation Initiative 2025, campuses plan to spend at least $75 million on their local priorities to improve student success and completion with particular emphasis on student engagement and well-being. To properly support the initiative, an incremental recurring investment of $105 million in 2020-2021 is necessary. This would fund the fourth year of a six-year, $450 million investment plan in support of Graduation Initiative 2025, and make permanent the $30 million of one-time funding included in the 2019-2020 state budget for Graduation Initiative 2025.

Full-Time Equivalent Student Enrollment Growth – $172 million to $215 million

The Public Policy Institute of California (PPIC) concluded that the state will fall about 1.1 million college graduates short of economic demand by 2030 if current trends persist. The PPIC suggests that in order to close the degree gap, there is a need for 480,000 CSU graduates beyond the current trend. Demand for the CSU continues to climb as more students graduate from high school having met the A-G requirements for admission to the CSU and more transfer students complete the Associate Degree for Transfer. This fall, the CSU implemented the application redirection policy to give CSU eligible first-time full-time, upper-division transfer and Associate Degree for Transfer students the option to have their applications reviewed by other campuses. Redirection will be helpful to a limited number of prospective students, but substantial increases to funded enrollment growth would be necessary to help narrow the PPIC's reported degree gap.

A range of four percent to five percent growth in full-time equivalent student (FTES) enrollment is estimated to add between $172 million and $215 million in new costs for between 14,900 and 18,700 additional FTES. Even though staff offer a range of enrollment growth here for the Board of Trustees' consideration, it is noted that an earlier analysis conducted by the Office of the Chancellor concluded that a five percent growth in FTES would be necessary in 2020-21 for CSU to help narrow California's projected degree gap. This increase would allow for growth in the average unit load for continuing students in support of graduation rate goals, and fund access for more new students. Funding for this item comes from two sources; additional tuition revenue from new students and state general fund. For planning purposes, each one percent increase in enrollment would cost approximately $43 million and would allow for growth of approximately 3,740 FTES.

Employee Salary and Benefit Increases – $150 million to $200 million

Most collective bargaining agreements expire at the end of 2019-2020 and discussions between bargaining units and the Office of the Chancellor will commence as early as this fall for successor agreements. Early estimates indicate that salary, health care premium, and pension cost increases for all employee groups will cost between $150 million and $200 million in 2020-2021. As CSU hires more faculty and staff in support of Graduation Initiative 2025 and enrollment growth, the cost to provide salary increases and cover benefit cost increases also grows. Staff will have more precise figures from campuses and complete its analysis by the November 2019 meeting, but for conservative planning purposes, this estimate is a reasonable starting point.

Mandatory Costs – $20 million

Staff anticipate that mandatory cost increases for existing university commitments will be approximately $20 million in 2020-2021. Mandatory costs include increases to operations and maintenance of newly-constructed facilities and other compensation-related costs, such as state wage law changes. If operating budget requests do not include these types of mandatory cost increases, campuses must redirect resources from existing programs, services and priorities to meet those cost increases.

Facilities and Infrastructure Needs - $50 million - $80 million

The systemwide academic facility improvement needs, including deferred maintenance totals approximately $11.2 billion. The restructuring of the CSU's facilities and infrastructure debt and previous support from the state in one-time and recurring funds has enabled $2.5 billion in new and revitalized facilities and a reduction in the deferred maintenance backlog. The 2019-2020 budget request of $80 million for academic facilities and infrastructure was not funded, but $239 million in one-time funding was provided by the state to help campuses with their deferred maintenance and infrastructure needs in the coming year.

Agenda Item 3 of the September 24-25, 2019 meeting of the Committee on Campus Planning, Buildings and Grounds includes the preliminary list for the 2020-2021 Capital Outlay program. The list prioritizes critical infrastructure and utility renewal projects and facility renovation to support the academic program needs. The addition of $50 million to $80 million in recurring funds would finance approximately $750 million to $1.2 billion of needed facility and infrastructure projects that increase capacity for student growth and complement the plan to address deficiencies in existing facilities. The CSU continues to refine the planning and financing process in light of the increased capital financing authority granted in 2014.

Additionally, CSU continues efforts in Sacramento to ensure an education facilities general obligation bond for the March 2020 primary election ballot. If approved by the governor and the voters, it could provide $2 billion in funding for CSU academic facilities and infrastructure. Additional details are contained in Item 3 of the September 24-25, 2019 meeting of the Committee on Governmental Relations.

Requesting between $50 million to $80 million recurring to pay the annual debt service on projects and sponsorship of a general obligation bond voter initiative are two important fiscal strategies to help address facility and infrastructure needs. A third, complementary strategy would be to include a request between $250 million and $500 million in one-time funds from the state to further address the deferred maintenance backlog.

Preliminary Revenue Plan

At this preliminary stage, the planning effort focuses on stating the CSU's budget priorities and needs. Accounting for enrollment growth revenue (approximately $20 million per one percent increase in enrollment targets), the preliminary plan's range of new investments would require additional new ongoing revenues from the state ranging from $415 million to $520 million.

Operating Fund Designated Reserves

Designated reserves in CSU's operating fund are used in several ways to deal with non-recurring expenses by managing short-term obligations and commitments, providing funding for capital infrastructure repairs and maintenance, and helping to ensure that operating costs can be paid during times of economic and budgetary uncertainty. Reserve designations are determined and reported annually by the campuses and the system office and are published on CSU's financial transparency portal. Designated reserves are not used to fund recurring expenses, such as salary increases. The use of one-time monies to pay recurring, permanent expenses can lead to structural deficits where recurring resources are insufficient to pay for recurring costs.

As of June 30, 2019, designated reserves in the operating fund totaled $1.7 billion and are held for short-term obligations, capital needs, and operations.

Short Term Obligations

Amounts held for short-term obligations are designated for payments for open contracts and purchase orders, near-term debt service payments, financial aid obligations, and programs that are in development. Reserves for short-term obligations totaled $814 million at the end of last year and cover expected needs, which are typically paid in the following fiscal year.

Capital

Capital reserves are designated for new projects and to repair current buildings, as well as planning costs and equipment acquisition associated with those buildings. Capital reserves fall well short of the expected need, which is at least ten percent of the cost of academic projects approved in the most recent five-year capital plan. Capital designated reserves totaled $356 million and are approximately half of the amount required for academic projects approved by the Board of Trustees as part of the 2019-2020 through 2023-2024 five-year capital program.

Operations

Reserves for operations are designated to provide a prudent reserve to sustain operations during periods of economic uncertainty such as short-term recessionary cycles or state budget fluctuations, and catastrophic events such as floods or earthquakes. Operating reserves are intended to be used in the future as one-time supplements to help manage the often-rapid decline in state resources, allowing time to appropriately adjust operating budgets to balance reductions and minimizing disruptions to students' education as much as possible. Designated reserves for operations set aside for economic uncertainty amount to $468 million and are less than one month of operating expenses, well below the need to maintain three to six months of operating expenses. Designated reserves for catastrophic events accounted for an additional $40 million of designated reserves for operations.

Conclusion

This is an information item presenting a preliminary framework for the 2020-2021 CSU Operating Budget Request to the governor and the Department of Finance. Using feedback provided by the Board of Trustees at the September 2019 meeting, Chancellor's Office staff will present an updated and detailed operating budget recommendation for Board of Trustees' approval in November 2019.