

# **INVESTMENT POLICY STATEMENT**

## **Catholic Foundation for the People of the Diocese of Rockford**

### **Purpose:**

The purpose of this investment policy is to establish the parameters and structure of the investment program for the *Catholic Foundation for the People of the Diocese of Rockford* (Catholic Foundation). The assets of this fund include the endowment assets of many parishes, schools and diocesan agencies (Participants). Each of the Participants should have its own investment guideline documents to state the unique liquidity, investment return, and risk exposure goals which are expected to be achieved through allocations to the various asset classes and investment styles offered by the Catholic Foundation Investment Program.

The Catholic Foundation Investment Program was established to pool the endowment assets of the Participants to achieve expanded diversification, more cost efficient investment services, and professional management that could not be achieved due to limited investment fund size. Participants can custom design their investment programs through varying percentage participation in the equity, balanced, and fixed income investment options offered by the Catholic Foundation Investment Program.

### **Authority:**

The Catholic Foundation has established the **Finance and Investment Committee** to provide oversight and review of the investment program and has entrusted the Committee, at the direction and approval of the Board of Directors and President of the Foundation, with the authority to retain professional services from investment consultants and investment managers and to delegate certain day-to-day responsibilities accordingly. The Uniform Prudent Investor Act, as adopted by the State of Illinois, shall be the legal reference for the investment program of the Catholic Foundation.

### **Investment Goal:**

The objective of the Catholic Foundation's investment program is to maximize the return on investment from these funds within the risk parameters specified in the Investment Guidelines section of this document. Preservation of capital, aversion to unnecessary risk and achievement of investment returns greater than specified investment return goals describe the over-all, guiding philosophy of the investment program. Both investment income and capital appreciation are components of expected total return from the investments. The time horizon for the Catholic Foundation is a long-term horizon; the Catholic Foundation does not intend to make short-term timing moves in the Investment Portfolio.

### **Investment Principles:**

Assets shall be invested with skill, care, and prudence taking into account the Foundation's liquidity requirements. The investment portfolio shall be diversified to

minimize the risk of large losses, unless circumstances at any given point in time indicate that diversification is clearly imprudent. All assets are to be fully invested at all times, including idle cash in overnight short-term instruments.

**Risk Posture:**

Investment theory and historical capital market return data suggest that, over long periods of time, there is a relationship between the levels of risk (i.e., volatility of investment returns) assumed and the level of return that can be expected in an investment program. In general, higher risk is associated with higher expected returns. The same relationship holds true between the volatility of the Catholic Foundation assets and the assets available for withdrawal to Participants. (i.e. historical return data suggests that participants in the Growth Fund should expect higher annual fluctuation in the market value of Foundation assets (either positive or negative), however, over longer time-frames the Growth Fund should grow Foundation assets at a higher rate of return than the Balanced Fund or the Fixed Income Fund.)

Given this relationship between risk and return, Participants in the Catholic Foundation must establish their unique risk posture assessing both capacity and willingness to accept risk (volatility). In determining risk posture, Participants should recognize the time horizon of their Foundation assets and consider their specific funding characteristics such as anticipated contribution experience as well as their withdrawal policy. The Catholic Foundation allows for a broad range of possible portfolios as Participants with a total account value over \$50,000 may blend the Growth Fund, and the Fixed Income Fund according to each Participant’s respective risk posture.

**Investment Objectives:**

**Catholic Foundation Investment Program**

The investment goals for the Growth and Income Fund of the Catholic Foundation Investment Program are to achieve minimum rates of return greater than the indices described below over a 3 and 5 year rolling period (net of management fees).

The benchmark comparisons for the Growth Fund are as follows:

<b>ASSET CLASS</b>	<b>BENCHMARK</b>	<b>% Allocated</b>
Large Cap Core	S&P 500 Index	15.0%
Large Cap Value	Russell 1000 Value Index	12.0%
Mid Cap Value	Russell Mid Value Index	6.0%
All Cap Growth	Russell 3000 Growth	12.0%
All Cap Core	Russell 3000	15.0%
Small Cap Value	Russell 2000 Sm. Value Index	10.0%
International Equity	Morgan Stanley Capital Int’l EAFE Index	30.0%

The benchmark for the Income Fund is the Barclays Aggregate.

## Catholic Foundation Investment Managers

### Quantitative Measures:

Managers will be evaluated against universe comparisons and benchmark comparisons. Actual and composite performance will be evaluated.

### Qualitative Measures:

The Foundation will rely on research alerts and manager due diligence reports provided by the investment monitor in evaluating managers. Due diligence reports will be provided every 12-24 months (or sooner) on each manager currently being used by the Foundation. All existing managers must retain a "Recommended" rating for continued inclusion in the Foundation's investment program.

In the event that MSG issues a "Downgrade" or "Termination" report on any of the Foundation's existing managers, the investment monitor is required to notify the Foundation within 48 hours of such report. In the event of a "Termination" report, the Foundation will require the investment monitor to conduct a manager search. It is the intent of the Foundation to replace any manager that MSG terminates within a reasonable period of time.

The Benchmarks comparisons for each manager are as follows:

ASSET CLASS	BENCHMARK
Large Cap Core	S&P 500 Index
Large Cap Value	Russell 1000 Value Index
Mid Cap Value	Russell Mid Value Index
All Cap Growth	Russell 3000 Growth
All Cap Core	Russell 3000
Small Cap Value	Russell 2000 Sm. Value Index
International Equity	Morgan Stanley Capital Int'l EAFE Index

Benchmarks are to be evaluated over a full market cycle.

### Asset Allocation Guidelines:

The following Asset Allocation Guidelines establish the Risk Control Policy for the investments of the Catholic Foundation Growth and Fixed Income Fund. The percentages apply to the market value of each respective fund. The maximum and minimum percentage limits provide a total portfolio volatility range established by the **Finance and Investment Committee** for each fund. All assets are to be fully invested at all times, including idle cash in overnight short term investments.

FUND	ASSET CLASS	MINIMUM	MAXIMUM	TARGET
<b>Growth Fund Manager Allocation</b>				
International		20%	40%	30%
	Large Core	10%	20%	15%
	Large Value	7%	17%	12%
	All Cap Growth	7%	17%	12%
	All Cap Core	10%	20%	15%
	Mid Cap Value	3%	9%	6%
	Small Cap Value	5%	15%	10%
<b>Income Fund Manager Allocation</b>	Fixed Income	75%	100%	95%

The Balanced Fund is not a separate asset pool, but is an allocation of Participants' investments between the Growth Fund and the Fixed Income Fund. Annually the Finance and Investment Committee, upon recommendation from the Investment Monitor, determines the allocation (the current allocation of the Balanced Fund is 70% Growth Fund / 30% Fixed Income Fund as of 10/1/2003).

The Catholic Foundation will review its asset mix at least annually and rebalance.

### **Marketability of Assets:**

All securities held in the portfolio shall have ready liquidity, meaning that any issue must have an established daily trading activity in excess of the units of the security held in the portfolio. In addition, all securities held in the portfolio must have a daily liquid market.

### **Investment Guidelines:**

#### Allowable Assets

1. Cash Equivalents
  - Treasury Bills
  - Money Market Funds
  - Short Term Invest Funds
  - Commercial Paper
  - Banker's Acceptances
  - Repurchase Agreements
  - Certificates of Deposits
  
2. Fixed Income Securities
  - U.S. Government and Agency Securities
  - Corporate Bonds and Notes
  - Mortgage Backed Securities
  - Preferred Stock - Including Adjustable Rate Issues
  - Collateralized Mortgage Obligations - PACs and "early tranche" Securities only

### 3. Equity Securities

- Common Stocks
- Convertible Notes and Bonds
- Convertible Preferred Stocks
- REITs
- American Depository Receipts of Non-U.S. Companies
- Stocks of Non-U.S. Companies (Ordinary Shares) - Must Be Denominated in U.S. Dollars

### **Derivative Investments:**

Unless approved in writing by the Board of Directors before purchase, or otherwise provided for under specific manager guidelines in this policy statement, the portfolio shall not acquire any derivative securities, including latter tranches of mortgage backed instruments.

### **Prohibited Assets and Transactions:**

Prohibited asset and transactions include:

1. Securities that would violate the Catholic Foundation's Catholic Values Investment Policy
2. Commodities and Futures Contracts
3. Private Placements
4. Options
5. Mutual Funds and Other Commingled Investment Pools \*
6. Limited Partnerships
7. Real Estate Properties
8. Interest Only, Principal Only and Residual Tranche CMOs
9. Short Selling
10. Margin Transactions
11. Securities Lending
12. Investment in the Diocesan DIAL Program (excluding the assets temporarily held in DIAL by the Catholic Foundation for the United in Faith endowment campaign per the trust established in July of 2003)

(\* ) Investment in Mutual Funds and other commingled investment pools may be formally authorized by the **Finance and Investment Committee** as a cost effective way to participate in certain investment styles, but normally would not be held in a portfolio of actively managed securities.

### **Liquidity:**

The amount of liquidity required by each Fund will change from time-to-time. In the absence of specific liquidity instructions, the manager of each portfolio segment is expected to remain reasonably fully invested at all times. During the July - September period, Participants may remove all or a portion of their earnings from the Investment Program. There is a 30-day notification requirement to permit the orderly liquidation of securities, should that be necessary.

## **Diversification:**

The **Finance and Investment Committee** does not believe that it is necessary or desirable that securities held in the portfolio represent a cross section of the economy at all times. There are no concentration restrictions for the ownership of U.S. Treasury, U.S. Government Agency securities or international investments.

## **Quality:**

Fixed income securities shall be investment grade or better. All commercial paper shall be A1/P1 or better. Equity securities held in the portfolio shall have a minimum market capitalization of \$500 million at time of purchase.

## **Investment Monitor Responsibilities:**

The performance record achieved by each manager, each Fund and the entire portfolio shall be prepared and presented to the **Finance and Investment Committee** in a formal report no less frequently than at the close of each calendar quarter. These reports shall provide reference to the specified Index Benchmark for each investment style, describing both rate of return and the standard deviation of returns in the portfolio relative to the benchmark. In addition, the reports should contain peer group comparisons with universes of investment styles represented within the portfolio.

In addition to the above services, when the conditions occur, the Foundation's Investment Monitor will inform the **Finance and Investment Committee** of the following:

- Results of the investment monitor's due diligence and research alerts for each manager, such as:
  - Changes in a fund manager's key personnel, investment assessment team, or our account manager;
  - Style changes or drifting;
  - Changes in the level of risk vs. return performance of the manager(s);
- Results of the annual reassessment of the appropriateness of the policy used to measure each manager's performance.
- Each manager's minimum acceptable return should be compared to their actual quarterly performance.
- Provide investment compliance report (see next section).

## **Manager Search, Evaluation and Retention Guidelines (Compliance Report):**

Each asset class or investment style employed in the Catholic Foundation Investment Program has an appropriate Index Benchmark, which is used in the asset allocation modeling process. This "proxy" for the asset class is measurable in two dimensions, rate of return and risk. Since the selected indices are used to develop the overall risk/return profile for the investment program, they are also appropriate as one of the evaluation tools for both hiring and retaining an investment management firm.

Importantly, these guidelines should be subordinate to the research alerts and due diligence reports from the investment monitor. They are to be considered as supporting data.

## Search

In addition to other qualitative factors, to qualify for consideration in a manager search process, an Investment Manager must meet the following criteria:

- ◆ The manager's composite return must exceed the appropriate Index Benchmark over 3 year rolling periods.
- ◆ In addition, the qualifying manager's composite return must have a Sharpe Ratio (a combined measure of return & risk) that exceeds the Sharpe Ratio for the appropriate Index Benchmark on both a 3 year and 5 year trailing basis.
- ◆ A manager's composite return must achieve a top 25% ranking as compared to an appropriate peer universe over 5-year rolling periods

## Evaluation and Retention

The following quantitative tests measure each manager's return and risk. Each test will be applied quarterly to evaluate whether or not a new manager search process is to be initiated by the Investment Monitor:

- ◆ An existing manager's composite return fails to exceed the appropriate index benchmark for three successive rolling 3-year periods, advancing 1 quarter at a time.
- ◆ An existing manager's composite return versus their appropriate universe comparison fails to achieve top 1/2 performance for three successive rolling 5-year periods, advancing 1 quarter at a time.
- ◆ An existing manager's risk (as measured by the standard deviation of the manager's composite return) shall not exceed 120% of the standard deviation of the appropriate index benchmark over a 3-year and 5-year trailing basis.
- ◆ An existing manager's risk versus return (as measured by the Sharpe ratio of the manager's composite return) shall exceed the Sharpe ratio of the manager's appropriate index benchmark over a 3 year and 5 year trailing basis.

Manager searches may be initiated regardless of the subject manager's tenure with the Catholic Foundation. The subject manager may be treated as a candidate in the search process; additional measures (see bullet points in next section) will also be employed in the evaluation process.

In addition, there may be other qualitative factors, as determined by the **Finance and Investment Committee**, which would facilitate the need for an investment manager search.

The **Finance and Investment Committee** will formally evaluate the Investment Monitor's performance at the February meeting of each odd numbered calendar year beginning with the February meeting of 1999.

### **Investment Policy Review:**

The Finance and Investment Committee on an annual basis shall review this Investment Policy Statement.

## Amendment to Investment Policy

### Specific Manager Guidelines:

The Foundation may utilize certain managers whose strategies include securities and processes precluded in the general policy if said securities and processes are outlined specifically and individually by manager in this section of the Investment Policy Statement.

### Pacific Income Management Company (PIMCO):

PIMCO'S fixed income strategy is best described as "core plus." Unlike most fixed income managers who typically emphasize only government debt and high quality corporates, this strategy has the ability to invest in all sectors of the bond market.

A typical portfolio has eight to twelve US Treasury and/or US Agency bonds that represent approximately 60% of the portfolio. The remaining 40% is invested in PIMCO's Fixed Income Shares ("FISH")\*, which is comprised of 40-Act registered Mortgage-Backed Securities and Investment Grade Corporate sector funds. The sector funds are afforded some flexibility and are not limited to strictly mortgage backed securities or investment grade debt. Thus this product's design allows clients to participate in all sectors of the bond market, including governments, corporates, mortgages, asset-backed, emerging markets, and high yield.

### PIMCO Allowable Assets:

- U.S. Government Securities
- Municipal Bonds
- Mortgage-Related and Other Asset-Backed Securities
- Loan Participations and Assignments
- Corporate Debt Securities
- High Yield Securities
- Variable and Floating Rate Securities
- Inflation-Indexed Bonds
- Event-Linked Exposure
- Convertible and Equity Securities
- Foreign (Non-U.S.) Securities
- Emerging Market Securities
- Foreign (Non-U.S.) Currencies
- Repurchase Agreements
- Reverse Repurchase Agreements, Dollar Rolls and Other Borrowings
- Derivatives

# CATHOLIC VALUES INVESTMENT POLICY

Revised, June 2004

The Board of Directors of the *Catholic Foundation for the People of the Diocese of Rockford* is called to exercise faithful, competent and socially responsible stewardship in how it manages and invests the financial resources entrusted to it. As a Roman Catholic organization, the Board draws its values from the Gospel of Jesus Christ, the teachings of the universal church and the guidance of our local Bishop. The following policy statement is written using the November 12, 2003 Socially Responsible Investment Policy of the United States Conference of Catholic Bishops as its model.

Faithful, competent and socially responsible stewardship directs the actions of the Board of Directors of the Catholic Foundation with dual and inseparable purposes: 1) to achieve a reasonable rate of return of invested financial resources in order for the participating parishes, schools, and diocesan ministries to strengthen their efforts of evangelization, education, service and pastoral care; and, 2) to employ socially responsible strategies and investments based on Catholic moral principles.

The Catholic Foundations' Performance Guidelines for achieving a reasonable rate of return on investments are found in a separate document titled "Investment Policy Statement." The following statements form the Policies of the Catholic Foundation for socially responsible strategies and investments:

Achieving a reasonable rate of return and employing socially responsible investment strategies work together to encourage the Board and its professional advisors to identify investment opportunities that meet both the financial needs and the social criteria. These purposes are carried out through the following strategies:

**1) Do no harm (avoid evil)**

This Fund involves two possible courses of action: 1) refusal to invest companies whose products and/or policies are counter to the values of Catholic moral teachings; 2) divesting from such companies. The decision to avoid or divest must be done prudently to minimize the financial impact and possible other negative consequences.

**2) Active Corporate Participation**

The Foundation will exercise normal shareholder responsibilities such as casting informed votes on proxies, dialoguing with corporate leadership, initiating or supporting shareholders' resolutions, and working with other religious groups who are advocating for corporate responsibility. This approach enables the Foundation to deal effectively with the reality of "mixed investments". One way for the Foundation to act as a socially responsible investor is to set limits for corporations engaged in questionable or objectionable activities, to hold a minimal position in those companies that fall under the threshold, and then to use our position as shareholders to work actively to influence or redirect the activities of the corporation toward activities and policies which are socially beneficial and serve the common good.

**3) Positive Strategies: (Promote the Common Good)**

This could include two possible courses of actions: 1) supporting policies and initiatives in companies owned by the Foundation that promote the values of Catholic moral and social teachings; 2) investing in companies that promote community development, which, in some cases, may result in a lower rate of return, but which are chosen because they give expression to the Church's preferential option for the poor or produce some significant social good.

**In light of the above strategies the Board of Directors of the Catholic Foundation instructs its professional investment advisors in these specific areas:**

Abortion

The Foundation advocates absolute exclusion of investment in companies whose activities include direct participation in or support of abortion. Direct participation in abortion may include, but not

limited to, companies involved in the manufacture of abortifacients and publicly held health-care companies that perform abortions when not absolutely required by federal or state law.

#### Contraceptives

The Foundation will not invest in companies that manufacture contraceptives or derive a significant portion of its revenues from the sale of contraceptives, even if they do not manufacture them.

#### Embryonic Stem Cell/Human Cloning

The Foundation will not invest in companies that engage in scientific research on human fetuses or embryos that 1) result in the end of re-natal human life; 2) make use of tissue derived from abortions or other life-ending activities; or 3) violates the dignity of a developing person. Specific activities covered by the policy include:

- 1) Embryonic stem cell research (ESCR)
- 2) Fetal tissue research or stem cell research from embryos; and
- 3) Human cloning.

#### Pornography

The Foundation will not invest in a company that derives a significant portion of its revenues from products or services intended exclusively to appeal to a prurient interest in sex or to incite sexual excitement. These would include, but not be limited to, sexually explicit (X-rated) films, videos, publications, and software; topless bars and strip clubs; and sexually oriented telephone and Internet services.

#### Production and Sale of Weapons

The Foundation, through its investments as well as its advocacy, seeks to discourage any nuclear and conventional arms race and to limit the distortions in the U.S. and global economy resulting from disproportionate military spending. The Foundation will, therefore, avoid investment in firms primarily engaged in military weapons production or the development of weapons inconsistent with Catholic teaching on war (e.g., biological and chemical weapons, arms designed or regarded as first-strike nuclear weapons, indiscriminate weapons of mass destruction, etc.) The Foundation will not invest in companies that are directly involved in the manufacture, sale, or use of anti-personnel landmines

#### Affordable Housing / Banking

The Foundation will not deposit funds in a financial institution that receives less than a "satisfactory" rating from federal regulatory agencies under the Community Reinvestment Act. The Foundation will encourage the financial institutions where it deposits its resources to undertake programs and implement policies to secure an "outstanding" rating under the act. The Foundation will communicate, where appropriate, to its financial institutions our support for their positive performance under the Community Reinvestment Act.

Using the opportunities available as a Corporate Participant, the Catholic Foundation, acting through its Catholic Values Investment Committee will advocate for Catholic moral and social teachings. Some specific areas are:

#### **A. Abortion**

The Foundation will consider supporting shareholder resolutions on abortion-related issues when deemed appropriate.

#### **B. Human Rights**

The Foundation will actively promote and support shareholder resolutions directed towards protecting and promoting human rights. For example, the Foundation could join efforts to influence corporations that are engaged in extractive industries or are operating in countries with significant human rights concerns. The Foundation will use selected shareholder resolutions and other means to encourage companies to provide sufficient wages, working conditions and other social benefits that enable their employees and families to meet basic human needs. The Foundation will seek means to encourage efforts by companies to promote a respect for fundamental human rights, especially in those countries in which these companies operate that have documented practices that deny or violate the human rights of their citizens.

### **C. Racial and Gender Discrimination**

The Foundation will promote and support shareholder resolutions directed towards equal opportunities for minorities and will work for the inclusion of minorities on corporate board. The Foundation promotes the active participation of women in the life of the company, particularly in terms of policy and decision-making, and inclusion in corporate leadership positions.

### **D. Access to Pharmaceuticals (e.g. HIV/AIDS)**

The Foundation will encourage companies to undertake or participate in programs designed to make life-sustaining drugs available to those in low-income communities and countries at reduced, affordable prices, consistent with our Catholic values. The Foundation will actively encourage and support shareholder resolutions directed towards making life-sustaining drugs more available and affordable to low-income communities and nations.

### **E. Curbing Pornography**

The Foundation will promote and support initiatives, including in some cases, shareholder resolutions, to promote responsible and family-oriented program content development by media companies.

### **F. Production and Sale of Weapons**

The Foundation will support shareholder actions to limit weapons production, to limit foreign sales of weapons and to convert corporate capacity to non-military uses.

### **G. Labor Standards/Sweatshops**

USCCB will actively promote and support shareholder resolutions directed towards avoiding the use of sweatshops in the manufacture of goods. The Foundation will promote and support shareholder resolutions to promote generous wage and benefit policies and adequate worker safety guidelines.

### **H. Protecting the Environment**

The Foundation will actively promote and support shareholder resolutions which encourage corporations to act "to preserve the planet's ecological heritage, addressing the rampant poverty in the poorest nations, redirecting development in terms of quality rather than quantity in the industrial world, [and] creating environmentally sensitive technologies." (***Renewing the Earth, 1991***) The Foundation will encourage policies and business that "undertake reasonable and effective initiatives for energy conservation and the development of alternate renewable and clean energy resources...[and offering] incentives to corporations to reduce greenhouse gas emissions and assistance to workers affected by those policies." (***Global Climate Change, 2001***)

### **J. Encouraging Corporate Responsibility**

The Foundation will encourage companies to report on social, environmental, as well as financial performance and promote and support shareholder resolutions directed towards adoption of corporate social responsibility guidelines within companies.