SAN FRANCISCO STATE UNIVERSITY FOUNDATION
INVESTMENT POLICY STATEMENT FOR RESTRICTED FUNDS

Approved by the Investment Committee, August 30, 2019

Ratified by the San Francisco State Foundation Board of Directors, September 11, 2019

I. INTRODUCTION

A. It is the role of the Board of Directors of the San Francisco State Foundation ("Board") to develop investment goals, objectives, and strategies for restricted endowment funds ("Endowment Fund", "Endowment", "Fund") held by the San Francisco State Foundation ("SFSF Foundation", "Foundation"). The purpose of this statement is to foster a clear understanding of the San Francisco State Foundation's financial and investment objectives and policies among the Board, the Executive Committee, the Investment Committee, the Foundation's staff, the Investment Advisor and the Foundation's investment managers. This investment policy supersedes all previous versions.

B. Restricted endowment fund assets shall be invested in accordance with this policy and in compliance with State and Federal laws and regulations. This policy statement shall be reviewed periodically, to assess the appropriateness of the asset allocation policy, the investment objectives, the investment policies and guidelines, and the investment restrictions. The Finance and Investment Committee ("Committee") is charged with performing this review and shall recommend appropriate changes to the Board for approval at any time.

II. FINANCIAL AND INVESTMENT OBJECTIVES

A. The long-term financial objective for the Endowment Fund is to preserve the real value (purchasing power) of the principal (gift value) and of its spending distributions, while providing a relatively stable source of funding for recipients. The financial objective applies to the overall Endowment and may not be applicable to every individual gift invested in the Endowment.

B. The primary long-term investment objective is to earn an average annual real (i.e., after adjusting for inflation) total return that is at least equal to the total spending rate (generally 5.25%, as outlined in section III), net of investment fees, over long time periods (i.e., rolling ten-year periods). Over shorter time periods (i.e., rolling five-year periods), the Fund will seek to outperform an appropriate composite of market indices reflecting the Fund's asset allocation policies and to perform on par with other endowment funds with broadly similar investment objectives and policies.

C. In order to achieve the primary investment objective over extended periods, endowments have had to exceed the objective substantially during some periods, such as the 1980s and 1990s, in order to compensate for shortfalls during other periods, such as the 1970s and the 2000's. Hence, evaluation of progress toward this objective should be made with a long-term perspective. This objective implies a high average allocation to equity securities and consequent market price volatility.

D. The desire to maintain the purchasing power of the Fund's principal and to produce a relatively stable and predictable spending stream involves trade-offs that must be balanced in establishing the investment and spending policies.

III. SPENDING POLICY

The general spending policy is a maximum payout of 4%, with an additional 1.25% to cover core operating expenses, yielding an effective spending rate of 5.25%. The Foundation employs a market-value based spending rule using a 12-quarter moving average.

IV. SOCIALLY RESPONSIBLE INVESTING POLICY

The Foundation is sensitive to the issue of social and environmental responsibility when making investment decisions. The Board continues to monitor and take into account a wide variety of information to help it determine what it considers to be socially responsible investments, and determine what actions it can take to foster lower carbon emissions and enable the development of new industries and technologies that serve this priority.

The Foundation will pursue social and environmental investments in a manner that is consistent with the Foundation's investment objectives, by applying selective portfolio restrictions and also proactively including investments that align with its guiding principles. See **Exhibit 1** for a complete articulation of the Foundation's Socially Responsible Investing Policy statement.

V. FUND COMPOSITION AND ASSET ALLOCATION

A. The Fund will be diversified both by asset class (e.g., stocks and bonds) and within asset classes (e.g., within stocks by economic sector, quality, and market capitalization). The purpose of diversification is to enhance prospective returns, lower the volatility of the overall pool of assets, and provide reasonable assurance that no single security or class of securities will have a disproportionate impact on the total portfolio.

B. For purposes of investment policy, the Fund shall be considered as two parts: the Equity Allocation and the Fixed Income Allocation. The Committee will operate within long-term policy ranges for the Equity Allocation and the Fixed Income Allocation, set forth below:

Asset Allocation Policy Ranges

	Long-Term Policy Range
Equity Allocation	70 - 90%
Fixed Income Allocation	10 - 30%
TOTAL	100%

Within the approved long-term policy ranges the Committee may, at its discretion, change the proportions of the Equity and Fixed Income Allocations and their respective components, but it is anticipated that such changes will be infrequent and consistent with the objectives of the Endowment. The current policy targets are set forth in **Exhibit 2**.

C. The primary purpose of the Equity Allocation is to provide long-term capital appreciation in order to facilitate the real growth of the principal and support a growing spending stream.

D. The equity investments will have greater return variability than the fixed income investments. To help mitigate this variability, the equity investments are diversified across different types of assets with return patterns that are expected to be imperfectly correlated (i.e., the returns of which do not always move in tandem).

E. The primary purpose of the Fixed Income Allocation is to provide a hedge against deflation and, secondarily, to provide a source of current income and to help diversify the total Fund.

VI. GUIDELINES FOR THE EQUITY ALLOCATION

A. The Equity Allocation for the Fund will generally be diversified among U.S. stocks, global ex-U.S. stocks, emerging markets stocks, public inflation protection assets, marketable alternative assets, private investment assets and potentially other "opportunistic" investments (e.g., individual allocations to high-yield bonds, emerging markets debt, and other areas that can be expected to generate equity-like returns).

B. The overall long-term investment objective for the Equity Allocation is to outperform, net of investment fees, an appropriate market benchmark or blended benchmark reflecting the Equity Allocation's asset allocation policies.

C. Performance will be monitored quarterly and will be evaluated over rolling three-to five-year periods relative to their benchmarks and peers. It is recognized that active managers will periodically underperform their benchmarks, but should outperform over a complete market cycle (5 to 10 years). The Committee acknowledges that the pursuit of long-term outperformance may increase the volatility of returns, and it will increase the risk that the manager will underperform the benchmark.

D. The objectives for marketable alternative assets are to improve the diversification of the Equity Allocation, reduce Equity Allocation volatility and outperform an appropriate benchmark, net of investment fees, over full market cycles or rolling five- to ten-year periods. These investments shall be diversified among absolute return (multi-strategy/event driven, credit/distressed and global macro), opportunistic and long/short equity.

E. The objective for private investment assets is to enhance the total return of the Equity Allocation, earning superior returns, net of investment fees, over appropriate benchmarks over rolling five- to ten-year periods. Assets in this category may include venture capital, growth equity, buyouts, secondaries, private real estate and private natural resources (i.e., private oil & gas or timber partnerships.).

F. The objectives for inflation protection assets are: (1) to help protect the Fund against unanticipated inflation, which can dramatically decrease the Fund's purchasing power and its ability to sustain spending; (2) to improve the diversification of the Equity Allocation; and (3) to exceed the return, net of investment fees, of appropriate benchmarks over full market cycles or rolling five- to ten-year periods. Assets in this category may include public real estate (i.e., REITs), natural resources (i.e., marketable securities of energy or other natural resource stocks), commodities, and/or TIPS[1].

VII. GUIDELINES FOR THE FIXED INCOME ALLOCATION

A. The Fixed Income Allocation for the Fund will generally be diversified among the following obligations: obligations issued or guaranteed by the U.S. Federal Government, U.S. Federal agencies or U.S. government-sponsored corporations and agencies; obligations of U.S. and non-U.S. corporations such as mortgage bonds, convertible and non-convertible notes and debentures, preferred stocks, commercial paper, certificates of deposit and bankers acceptances issued by industrial, utility, finance, commercial banking or bank holding company organizations; mortgage-backed and asset-backed securities; obligations, including the securities of emerging market issuers, denominated in U.S. dollars or foreign currencies of international agencies, supranational entities and foreign governments (or their subdivisions or agencies), as well as foreign currency exchange-related securities, warrants, and forward contracts; obligations issued or guaranteed by U.S. local, city and state governments and agencies; securities defined under Rule 144(A) and Commercial Paper defined under Section 4(2) of the Securities Act of 1933.

B. The performance objective for the Fixed Income Allocation is to outperform an appropriate bond market index or blend of indices, net of investment fees, over rolling three- to five-year periods. Individual active fixed income managers may be expected to outperform other indices, or blended indices, which more closely parallel the manager's investment style. In addition, active fixed income managers may also be compared against peer benchmarks (e.g., manager medians), but it is recognized that such benchmarks typically contain significant "survivor" or "add-in" bias, and thus are less reliable than market benchmarks in assessing

[1] TIPS and other inflation-linked bonds, though fixed income, may be included in the inflation hedge category because of their inflation-hedging characteristics.

performance. Index fund managers will be expected to perform consistently, net of investment fees, with their appropriate index.

C. To provide a hedge against extended deflation, the Fixed Income Allocation should ordinarily maintain an investment grade credit quality and an intermediate- to long-term duration. An allocation may be made to below investment grade (i.e., high-yield) bonds so long as the weighted average credit rating for the total fixed income portfolio meets the above credit quality standards.

D. In general, the fixed income investments should be prudently diversified in order to minimize risk exposure, except that issues of the U.S. Government or agencies of the U.S. Government may be held without limitation.

VIII. GUIDELINES FOR THE USE OF DERIVATIVES

A. Derivatives are generally defined as securities whose value is derived from the value of one or more other securities. In contrast, cash or traditional securities derive their value from claims on the cash flows arising from economic activity[2]. The use of derivatives by investment managers should be in a manner consistent with the Endowment's goals and policies.

B. The primary intent of derivative security transactions should be to hedge the risk of the portfolio, or to implement investment strategies more efficiently and at a lower cost than would be possible in the cash market. Derivatives-based strategies should not be used to leverage the Endowment portfolio nor should they be used to expose the portfolio to greater risk than would be typical under a strategy utilizing only cash securities. The Committee requires that the manager have appropriate control and review procedures in place to evaluate the risks and exposures of the portfolios on a timely basis. These control and review procedures shall include, but not be limited to, compliance with all necessary legal requirements, creating internal review and control systems to review portfolio risk and using third party pricing of illiquid securities where appropriate.

IX. GUIDELINES FOR TRANSACTIONS

Except under unusual circumstances, all transactions should be entered into on the basis of best execution, which means best realized net price. Consistent with the above, directed brokerage service arrangements may be put in place for payment of services rendered to the Fund in connection with its management.

X. MONITORING THE PORTFOLIO

[2] Notwithstanding this fairly simple "definition" of derivatives, it is actually quite difficult to come up with a comprehensive method of classifying financial assets as being derivatives or traditional. This is in part because many financial assets, including stocks and bonds, have derivative-like features.

A. The Committee will normally review the Fund's asset allocation, manager structure and performance quarterly in order to evaluate diversification, adherence to policies, and progress toward long-term objectives. While short-term results will be monitored, it is understood that the objectives are long-term in nature and that progress toward these objectives will be evaluated from a long-term perspective.

B. Although marketable manager investment performance will generally be evaluated over rolling three- to five-year periods, the Committee will periodically evaluate each manager, as appropriate, to establish that the factors that led to initial performance expectations remain in place and that each manager's philosophy is appropriate for the Fund's overall objectives.

C. It is expected that the Committee will provide each manager of a separate account with a set of mutually agreed-upon guidelines. Subject to such guidelines and the usual standards of fiduciary prudence, the managers will then have complete discretion over the funds.

D. The Committee acknowledges that, if it elects to invest in a commingled fund[3], the policies established for the commingled fund will govern and may not comply fully with policies established for the Fund. As appropriate, the Committee will periodically review the policies (i.e., investment parameters) of any commingled fund investment to determine if they remain appropriate.

E. At its sole discretion, the Committee may terminate any manager at any time if it determines, for whatever reason, that the manager is no longer appropriate.

F. The Committee will periodically review the related services provided to the Fund, including custody services and investment consulting.

XI. REBALANCING

A. Rebalancing is designed to keep the portfolio in line with the policy allocation targets and target ranges established by the Committee. Current policy targets are set forth in **Exhibit 1**.

B. Policy targets are established to maintain the long-term strategic asset allocation of the Fund. The rebalancing process results in the movement of assets from recently strong performing asset classes, which may be overvalued, into weaker performing asset classes, which may be undervalued. The need to rebalance could be occasioned by the disproportionate movement of asset prices within a class relative to movement of prices in other classes, significant inflow of new gifts and/or extraordinary funding requirements of participating projects holding quasi-endowments. Over the long-term, this discipline is expected to enhance portfolio returns while reducing risk (volatility) by realizing gains in one asset class and using those funds to make additional purchases in the undervalued asset class.

C. It should be noted that quasi-endowments are also invested in the Fund. Unlike true endowments, the quasi-endowments allow for distributions from the fund principal. Recognizing the possibility that the capital distribution from a large quasi-endowment could trigger the need to re-allocate the Fund assets among investment managers, the Foundation should limit such distributions to once a year.

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[3] Commingled funds include institutional commingled trusts, mutual funds, limited partnerships and other similar investment vehicles.

EXHIBIT 1

SOCIALLY RESPONSIBLE INVESTING POLICY

The San Francisco State Foundation is sensitive to the issue of social and environmental responsibility when making investment decisions. The Foundation Board continues to monitor and take into account a wide variety of information to help it in determining what it considers to be socially responsible investments, and determine what actions it can take to foster lower carbon emissions and enable the development of new industries and technologies that serve this priority.

The Foundation will pursue social and environmental investments in a manner that is consistent with the Foundation's investment objectives, by applying selective portfolio restrictions and also proactively including investments that align with its guiding principles.

Guiding Principles

The Foundation shall be guided by three principles:

1. The Foundation shall exercise responsible financial stewardship over its financial resources
2. The Foundation shall exercise ethical and social stewardship in its investment policy
3. The Foundation acknowledges the threat of climate change and is committed to taking responsibility for how our activities and investments contribute to its causes

Portfolio restrictions

The Foundation will not directly invest in stocks of companies falling into the following categories, and will make best efforts to minimize exposure to these securities in commingled accounts.

- Countries or companies whose governing regimes are deemed by the Board of Directors to deny civil or human rights.
- Stocks of companies for which manufacture of tobacco products is a significant contributor to sales or earnings
- Stocks of companies that are deemed by the Board of Directors to have significant exposure to production or use of coal or tar sands.

Proactive investments

The Foundation will seek to align its investment capital with its guiding principles by proactively cultivating and implementing investment opportunities that focus on the following:

- <u>The practice of integrating environmental, social, and governance (ESG) factors with other conventional financial analytical tools.</u> ESG factors may help identify i) potential opportunities and ii) potential risks that conventional tools miss. Incorporating ESG factors into the management of the portfolio is consistent with both the financial and ethical objectives of the Foundation.

- Investments that are consistent with the transition toward a low-carbon economy. Such investments may include power generation from renewable energy sources and/or the development of technologies that support the production and delivery of energy from these sources.

Green Portfolio Guidelines

The Foundation has established a Green Portfolio of socially responsible investment opportunities to be considered aside from, and parallel to, its traditional portfolio of investments.

The Green Portfolio will adhere to the same guidelines and strategy as the main fund, and will provide donors with a fossil fuel free investment option.

EXHIBIT 2

SF STATE FOUNDATION – ASSET ALLOCATION POLICY TARGETS

Asset Class	**Interim Targets**	**Long-Term Targets**
<u>EQUITY ALLOCATION</u>		
<u>GROWTH ASSETS:</u>		
Global Stocks	12%	12%
U.S. Stocks	18%	18%
Non-U.S. Stocks	18%	18%
Emerging Markets Stocks	10%	10%
Total Common Stocks	**58%**	**58%**
Private Investments	5%	10%
TOTAL GROWTH	63%	68%
DIVERSIFIERS	5%	5%
INFLATION PROTECTION	5%	5%
TOTAL EQUITY ALLOCATION:	**73%**	**78%**
Fixed Income	25%	20%
Cash	2%	2%
TOTAL FIXED INCOME ALLOCATION:	**27%**	**22%**
TOTAL ASSETS	**100%**	**100%**

Note: Interim targets reflect that it will take several years to reach the policy targets for private investments.