

University of Virginia  
Investment Management Company  
**Investment Policy Statement**

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**Exhibit 1 Policy Portfolio**

## **I. Introduction**

### **A. *Organizational Purpose***

The University of Virginia Investment Management Company (UVIMCO) provides investment management to the Rector and Visitors of the University of Virginia (University) and its related foundations (Foundations). Assets deposited in UVIMCO are held in the custody and control of UVIMCO on behalf of the University and Foundations within a long-term co-mingled investment pool (Pool).

### **B. *Standard of Care***

The Board of Directors (Board) and Officers (Staff) of UVIMCO manage Pool assets in accordance with this Investment Policy Statement. In making investment decisions and taking investment actions, they exercise their good faith business judgment and act consistent with required standards of conduct for managers of institutional assets.

Given the uncertain and continuously evolving nature of investment markets, no static list of security types, asset classes, or definitions of investment management strategies can continuously express prudent practice. Therefore, the process by which investment decisions are developed, analyzed, adopted, and executed must satisfy relevant standards of care.

### **C. *Objectives***

UVIMCO's primary objective in managing the Pool is to maximize long-term real return commensurate with the risk tolerance of the University.

To achieve this objective, UVIMCO actively manages the Pool in an attempt to achieve returns that consistently exceed the returns on a passively investable benchmark with similar asset allocation and risk (Policy Portfolio Benchmark).

Recognizing that the University must attract outstanding students, faculty, and staff and provide to them appropriate resources, UVIMCO strives to manage Pool assets to provide long-term real returns that compare favorably with the returns of endowments of other outstanding schools (Peer Group).

### **D. *Spending***

UVIMCO does not set spending rates. UVIMCO communicates the Pool's risk and return estimates to the University and Foundations for their consideration in setting spending rates.

## **II. Governance**

### **A. *Board Responsibilities***

The Board is responsible for establishing this Investment Policy Statement. The Board has delegated to UVIMCO's Chief Executive Officer (CEO) responsibility for managing Pool assets in accordance with this Investment Policy Statement and in accordance with other policies that the Board has or may adopt.

The Board monitors the development, analysis, adoption, and execution of investment decisions and actions by the Staff to ensure compliance with this Policy and applicable standards of care. The Board also evaluates the competence of the management of Pool assets considering the investment process and the resulting return of Pool assets relative to the Policy Portfolio Benchmark and Peer Group. The Board takes action to amend this Investment Policy Statement or replace Staff as necessary to ensure prudent management of Pool assets.

### **B. *Staff Responsibilities***

Staff manages Pool assets within the policies set by the Board and under the direction of the CEO. Staff's investment management responsibilities include tactical asset allocation and selection of external managers. While Staff may directly trade securities or derivatives to manage the Pool's asset allocation, active management of security selection typically is delegated to external managers.

### **C. *Tactical Asset Allocation***

Because an optimal asset allocation evolves through time in response to changing economic circumstances and volatile market prices, Staff may tactically manage the Pool's asset allocation within the risk control ranges of the Policy Portfolio. Implementation of any such tactical strategy recognizes the inherent uncertainty of short-term forecasts of asset class returns and the high relative risk of even small deviations from the market exposures of the Policy Portfolio and Peer Group. Therefore, Staff typically scales any tactical asset allocation positions to ensure only modest risk relative to the Policy Portfolio Benchmark and Peer Group.

### **D. *Manager Selection and Monitoring***

Staff monitors and evaluates the full spectrum of global investment strategies seeking opportunities to employ active external managers. Prior and subsequent to hiring external managers, staff investigates and analyzes managers' investment process, organization, and staff. Staff terminates managers or adjusts manager positions to achieve the objectives of the Investment Policy Statement. While the Board has delegated manager selection and retention decisions to the CEO, the Board monitors the CEO's decision making process and reviews documentation of due diligence in analyzing and monitoring managers.

### ***E. Manager Diversification***

For instruments or funds whose returns are produced only through exposure to capital markets, including index funds and similar derivative securities, allocations are limited by the asset allocation ranges expressed by the Policy Portfolio. For managers whose returns are produced primarily through skill, including hedge funds, no more than 7.5% of Pool assets are allocated to a single manager. For long-term closed-end fund investments, including private equity and real estate funds, the 7.5% limitation applies to the amount committed in currently active funds at the time of the new commitment. For purposes of this limitation, separate funds managed by an investment company or business group are aggregated if the returns of those funds are produced by a common investment process.

### ***F. Leverage and Derivatives***

UVIMCO employs leverage and derivative securities, both directly and within funds, only to the extent that the aggregate risk of the Pool is not increased beyond that which would be allowed by the Policy Portfolio without using leverage or derivatives. UVIMCO defines leverage as a strategy that increases expected return by raising exposure to and risk of a given investment. The most direct form of leverage is borrowing but many other strategies, structures, funds, and derivative securities produce similar results and therefore imply leverage. UVIMCO monitors and controls the effect of both direct and implied leverage on the Pool's volatility and liquidity.

### ***G. Reporting***

UVIMCO provides monthly reports to the University and Foundations displaying the Pool's asset allocation relative to the Policy Portfolio and displaying the returns of the Pool and its component asset classes. UVIMCO provides quarterly narrative reports that explain and analyze the Pool's investment position, strategy, and performance relative to both the Policy Portfolio Benchmark and the Peer Group.

### ***H. Annual Policy Review***

The Board reviews this policy annually. In preparation for that review, Staff provides an analysis of any changes in the risk tolerance and spending plans of the University that have been reported to it and on economic and investment conditions. Staff recommends changes to this Investment Policy Statement accordingly. Typically, annual changes to this Investment Policy Statement are small and gradual. The revised Investment Policy Statement is provided to the University and Foundations on a timely basis.

### **III. Policy Portfolio**

#### **A. *Capital Market Risk and Return Estimates***

The Board reviews and approves Staff's estimates of capital market risks and returns. Staff divides the global capital market into asset classes and examines their historical returns, volatilities, and correlation. If future conditions such as economic risk, inflation, and market integration are likely to differ materially from the conditions during the historical periods examined, then Staff adjusts historical risk and return estimates accordingly.

Perceived temporary deviations of current market prices from equilibrium values do not influence UVIMCO's capital market risk and return estimates. Therefore, UVIMCO's capital market risk and return estimates are changed infrequently and gradually.

#### **B. *Risk Tolerance***

The Board determines the Pool's risk tolerance in consideration of the University's tolerance for volatility in spending. Foundations must determine whether the Pool's risk and return characteristics are appropriate given their investment objectives and spending plans.

In theory, tolerance for spending volatility determines a risk aversion parameter, which in combination with capital market risk and return estimates provides a specific optimal asset allocation that maximizes utility. In practice, risk tolerance is difficult to quantify and the theoretically optimal asset allocation may vary widely within a reasonable range of capital market risk and return estimates. Therefore, the Board's determination of the Pool's risk tolerance is necessarily a judgmental process.

#### **C. *Strategic Asset Allocation***

Based upon the University's risk tolerance together with capital market risk and return estimates, the Board sets a strategic asset allocation designed to achieve the objectives stated in this Investment Policy Statement. The strategic asset allocation is prudently diversified across asset classes. If passively executed, the strategic asset allocation would provide expected returns in line with its risks; it lies near the efficient frontier of portfolios that provide the highest expected return per unit of risk and the lowest risk per unit of expected return.

Benchmark indices are selected to represent the risk and return profile of each asset class. Key considerations in selecting benchmark indices include broad market coverage, ability to passively invest, transparency of index construction, and objectivity of the index provider. The strategic asset allocation together with the selected benchmark indices form the Pool's Policy Portfolio Benchmark – the primary benchmark against which actual Pool performance is measured.

#### ***D. Risk Control Ranges***

The Policy Portfolio specifies risk controls in the form of ranges for Pool asset allocations. The ranges help to ensure adequate diversification, define the permissible magnitude of tactical asset allocation, and constrain both absolute and relative risk. UVIMCO has adopted risk controls principally considering the Pool's tolerance for volatility, but also to ensure adequate liquidity.

Risk control ranges express the acceptable variation from target asset allocations in normal market and economic circumstances. Exceptional circumstances may justify deviation from the ranges specified in the Policy Portfolio. Deviation from risk control ranges caused by an investment decision or action must receive the prior approval of the Board. Deviation from risk control ranges caused by changes in market prices or manager actions is reported by the CEO to the Board monthly along with a recommended plan of action. In any such circumstance, UVIMCO formally communicates to the University and Foundations the reasons for operating the Pool's actual asset allocation outside of the ranges specified by the Policy Portfolio.

## POLICY PORTFOLIO AS OF JUNE 30, 2009

### Strategic Asset Allocation

Asset Class	Allocations (%)	Benchmarks
<b>Equity</b>	<b>60</b>	MSCI All Country World Equity
<b>Real Assets</b>	<b>10</b>	50% MSCI U.S. Real Estate 50% MSCI AC World Real Estate
<b>Fixed Income</b>	<b>30</b>	50% Barclays U.S. Aggregate 50% Barclays Global Aggregate Bond (Hedged)
<b>TOTAL</b>	<b>100</b>	<b>Policy Portfolio Benchmark</b>

### Risk Control Ranges (%)

Net Exposure*	Ranges	Allocations*	North America*	Europe*	Asia*	LAMA*†
Equity	40 – 70	60	28	17	13	2
Real Assets	5 – 20	10	6	1	3	0
Credit	0 – 20	15	11	2	1	0
Government Bond	5 – 20	15	9	4	2	0
<b>Regional Targets &amp; Ranges</b>	<b>70 – 100</b> --	<b>100</b> --	<b>55</b> 25 – 75	<b>23</b> 10 – 40	<b>19</b> 10 – 40	<b>3</b> 0 – 20
<b>Cash &amp; Currency</b>	<b>0 – 30</b>	<b>0</b>	<b>10</b>	<b>-6</b>	<b>-3</b>	<b>0</b>
<b>Current Targets &amp; Ranges</b>	<b>--</b> --	<b>100</b> --	<b>64</b> 50 – 100	<b>17</b> 0 – 30	<b>16</b> 0 – 30	<b>3</b> 0 – 20

\* Regional asset class and currency exposure of the Policy Portfolio Benchmark as of 6/30/09.

† Latin America, the Middle East, and Africa