



ELCA Foundation
Evangelical Lutheran Church in America

ELCA ENDOWMENT FUND POOLED TRUST — FUND A

FOURTH QUARTER 2008 REPORT

Gift acceptance considerations

Laura Knitt, JD

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Funding an endowment with gifts of non-cash assets, like appreciated securities, real estate or personal property can work in favor of your ministry if you consider when you should or should not accept a particular gift asset. Three considerations to include in your gift acceptance policy are donor intent, sale-ability and liability.

1 You have to be able to comply with donor intent. This fosters personal relationships with your donors and keeps you out of trouble with your state’s attorney general. Before accepting a gift for which a donor has requested a specific use, you should negotiate options up front with the donor. For example, if a donor wants you to maintain her family’s land as a retreat but your ministry doesn’t need or want a retreat, you can only accept the gift if the donor’s intent changes to be in line with that of your ministry.

2 Non-cash assets need to be readily convertible to cash, unless your ministry intends to use them as they are. Most securities are readily convertible, but real estate and personal property may present challenges. If a donor has been trying unsuccessfully to sell a timeshare or a vacant lot or a large gem, your ministry probably does not want the responsibility of owning the asset either (e.g., annual fees, real estate taxes, insurance).

3 Owning a non-cash asset should not bring excessive risk to an institution. A stereotypically risky gift would be an old gas station lot — likely to harbor environmental contaminants for which any owner in the chain of title takes responsibility. Before accepting a non-cash asset, you should obtain as much information as possible, including such things as detailed corporate records if being offered shares of a closely held corporation.

THEN REMEMBER: ELCA Foundation staff are trained to help you recognize and address a range of issues that may apply. We’re here for you.

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Fund A — Fourth quarter 2008 performance

To help you understand the “drivers” of Fund A’s overall performance, every quarter we provide you market context for each asset class within Fund A.

MARKET COMMENTARY

Heather H. Williamson, CFA

Senior Investment Manager, ELCA Board of Pensions

*Those who ignore the past are bound to repeat it ...
Past performance is no guarantee of future results ...*

The markets and the economy have boldly demonstrated the dichotomy of these truisms over time. We are called on to learn from the past; yet, we must also understand history’s limitations in prescribing solutions to current and future problems.

Remembering forgotten lessons while learning from the past

As a nation, we disregarded some important lessons and were sent a hard-to-ignore reminder in 2008. Debt can be bad when overused and when underlying risks are not understood. Today, we find ourselves in the midst of the worst credit crisis since the Great Depression.

What we seem to have learned is that rapid and significant response to a credit crisis is warranted, versus the slow response to the Great Depression of the 1930s and Japanese downturn of the 1990s. The U.S. government is responding aggressively with actions such as reducing short-term interest rates, expanding money supply and launching stimulus packages. Hopefully these are the right tactics. There is certainly no playbook.

No simple solutions

Each of the efforts noted above does carry risks that will need to be watched and dealt with. Increased money supply, or “quantitative easing” (a nice way of saying printing money), ironically requires the United States to expand its own debt burden (issue treasury securities). This added debt could over time diminish the confidence of other countries in our credit-worthiness. A devaluation in the dollar (a by-product of the expanded money supply)

exacerbates our financial troubles and fans inflationary flames, despite the immediate and appropriate focus on curbing deflationary trends.

There is also an additional level of complexity on which history has little to tell. This recession is the first significant, globally synchronized recession ever. The complicated consequences of how governments act across the world are unknown.

HOW FUND A FARED IN 2008

Trends seen throughout 2008 extended in a dramatic way into the fourth quarter. Not surprisingly, Fund A experienced returns that are consistent with those experienced in the broader markets in which it is invested. Fund A returned -16.6 percent for the fourth quarter, versus a benchmark return of -18.0 percent. Over the 12-month period during 2008, this outperformance was seen as well; Fund A returned -29.1 percent while the benchmark returned -30.1 percent.

Despite the extraordinary downdraft across virtually all asset classes during 2008, we believe that capitalism (and growth funded by equity and debt) does work and are confident that the markets will recover. If history is a guide, the markets will price in an economic recovery before one is evident. For this reason, remaining fully invested and diversified even in these tough periods is critical for long-term sustainability of endowed assets. Our (and others’) research also suggests that despite the current difficult market, diversification, over long periods of time, is the most efficient and effective strategy for generating sufficient returns at acceptable risk levels to support long term distributions for mission.



FUND A PORTFOLIO MARKET VALUE¹

As of Dec. 31, 2008, Fund A had investments of approximately \$261 million:

- \$135 million in the U.S. equity component
- \$47 million in the investment-grade, fixed-income component

- \$23 million in the high-yield, fixed-income component
- \$40 million in the non-U.S. equity component
- \$16 million in global real estate securities

FUND A INVESTMENT PORTFOLIO PERFORMANCE AS OF DEC. 31, 2008

		FOURTH QUARTER (%)	ONE YEAR (%)	FIVE YEARS (%)
Total Fund A ²		-16.6	-29.1	0.9
Fund A benchmark (Dow Jones Wilshire 5000 Index ³ 50%, MSCI All Country World (Ex-U.S.) Index 15%, Citigroup High-Yield Cash-Pay Capped Index 10%, Custom Citigroup Index ⁵ 20%, Index Dow Jones Wilshire Real Estate Securities Index 5%)		-18.0	-30.1	0.2
EQUITIES	Fund A U.S. equity portfolio ²	-22.0	-37.6	-1.6
	U.S. equity benchmark (Dow Jones Wilshire 5000 Index ³)	-22.9	-37.2	-1.9
	Fund A non-U.S. equity portfolio ²	-23.8	-46.3	N/A ⁴
	Non-U.S. equity benchmark (MSCI All Country World (Ex-U.S.) Index)	-22.3	-45.5	2.6
HIGH-YIELD	Fund A high-yield portfolio ²	-12.8	-16.4	1.7
	High-yield benchmark (Citigroup High-Yield Cash-Pay Capped Index)	-18.7	-25.0	-0.8
FIXED-INCOME	Fund A fixed-income portfolio ²	3.2	2.4	4.4
	Fixed-income benchmark (Custom Citigroup Index ⁵)	4.7	5.3	4.7
REAL ESTATE SECURITIES	Fund A global real estate securities portfolio ²	-35.8	-34.5	N/A ⁴
	Real estate securities benchmark (Dow Jones Wilshire Real Estate Securities Index ⁶)	-41.3	-40.7	0.7

1. Total market value of Fund A is approximately \$261 million, including deposits between monthly valuation dates and operating cash on which a total fee of one-twelfth of 1 percent is deducted monthly from each account.
2. Returns are before the deduction of fees.
3. The U.S. equity benchmark changed from the Russell 3000 to the Dow Jones Wilshire 5000 in November 2007.
4. This portfolio became a component of Fund A less than five years ago, so a five-year return is unavailable.
5. The fixed-income benchmark changed from the Citigroup Broad Investment Grade to the Custom Citigroup Index in October 2007.
6. Late in 2008, the Global Real Estate Securities Benchmark began transitioning to a composite of 60 percent Dow Jones Wilshire Real Estate Securities Index and 40 percent Dow Jones Wilshire ex U.S. Real Estate Securities Index, from 100 percent Dow Jones Wilshire Real Estate Securities Index previously. The transition will continue into early 2009.



U.S. EQUITIES MARKET REVIEW

Josh Stieler, CFA

Assistant Investment Manager, ELCA Board of Pensions

Fund A's U.S. equity component returned -22.0 percent for the fourth quarter, compared to the benchmark return of -22.9 percent. Positive relative returns by the value and growth managers were partially offset by underperformance in the active small/mid-cap segment.

U.S. Equity markets suffered their largest quarterly decline since the fourth quarter of 1987, as focus shifted from turmoil in the credit market to broader economic concerns. Mounting job losses and declining corporate profitability weighed heavily on investor sentiment. All sectors declined during the quarter, led by financials and consumer-related stocks. For the year, the Wilshire 5000 Total Market Index fell by over 37 percent, the worst year since the index's inception in 1970.

Investment style was not a major driver of returns in the fourth quarter. Large cap stocks outperformed small/mid caps by 4 percent.

NON-U.S. EQUITIES MARKET REVIEW

Josh Stieler, CFA

Assistant Investment Manager, ELCA Board of Pensions

Funds A's non-U.S. equity component fell by 23.8 percent for the quarter, compared to -22.3 percent for the benchmark. Underperformance was driven primarily by the value manager.

Although the credit crisis and resulting economic woes originated in the United States, international markets were not immune to the effects. Concerns over the health of financial firms and the impact of the recession drove markets lower. Emerging markets posted particularly weak results, falling almost 28 percent. Developed economies fared little better,

falling 21 percent. All countries declined for the quarter, with Japan posting the best results with a return of -9 percent. For the year, international equity markets, as measured by the MSCI All Country World ex-US Index, fell 45 percent.

Investment style was not a major driver of returns during the quarter with both growth and value falling approximately 22 percent. The U.S. dollar strengthened in the fourth quarter, further reducing the returns of dollar-based investors. Dollar based returns trailed local currency returns by 3 percent.

GLOBAL REAL ESTATE SECURITIES MARKET REVIEW

David Quello, CFA

Investment Manager, ELCA Board of Pensions

The market punished all real estate sectors during the quarter due to concerns about the economy and financial health of companies that rely on any type of financing. Real estate securities continued to experience increased volatility relative to past periods due to the global economic situation and their link to the financial sector. Fund A's real estate securities component returned -35.8 percent in the fourth quarter, compared to the benchmark return of -41.3 percent. The portfolio outperformed its benchmark largely due to stock selection in the industrial, hotel and shopping center sectors.

In December, the portfolio began transitioning from a purely U.S. real estate securities to a global real estate securities portfolio. Approximately 10 percent of the portfolio is now invested in non-US real estate securities. The transition will continue into early 2009 until the portfolio reaches the target allocation of 60 percent U.S. real estate securities and 40 percent Non-U.S. real estate securities. The broadening of the portfolio is expected to improve the risk/return profile of Fund A.



FIXED-INCOME MARKET REVIEW

Mark Haney, CFA

Senior Investment Manager, ELCA Board of Pensions

Fund A's fixed-income portfolio underperformed its benchmark, returning 3.2 percent, versus the benchmark's 4.7 percent, largely due to holdings in high-quality, non-agency mortgage securities that have suffered disproportionately to their underlying value.

The credit markets entered the quarter in a fragile state, and the ensuing flight to safety led to the lowest Treasury yields in 50 years. Risk premiums on even the highest quality non-Treasury securities rose to record levels. The yield on the 10-year Treasury hit 2.06 percent on Dec. 30, and short term Treasury Bills yields were even negative at times during the quarter.

Though Treasuries returned an outsized 8.85 percent for the quarter, credit and mortgage sector returns were 4.16 percent and 4.26 percent, respectively. Some sectors continued to fall; the asset backed sector returned -6.48 percent and the commercial mortgage sector posted negative returns in the double digits. Over all, the high-grade, fixed-income market had a strong quarter and year, returning 5.65 percent and 7.02 percent, respectively, as measured by the Citigroup U.S. Broad Investment-Grade Index.

HIGH-YIELD MARKET REVIEW

Mark Haney, CFA

Senior Investment Manager, ELCA Board of Pensions

The high-yield bond component of Fund A returned -12.8 percent, relative to its benchmark, the Citigroup High-Yield Cash-Pay Capped index, which lost -18.7 percent. The outperformance was due to conservative portfolio positioning and avoidance of the lowest quality portion of this market.

Performance in high-yield bonds was tiered by quality — CCC-rated securities (lower quality) fell -21.16 percent, while BB securities (higher quality) fell -10.20 percent. This reversed dramatically in December when CCCs returned a positive 22.06 percent for the month, versus 7.29 percent for BBs.

The return dispersion between industry segments and security types was wide. Pay-in-kind and deferred-interest bonds lost -42.22 percent and -36.77 percent, respectively. Some consumer discretionary segments were especially hard hit by the economic meltdown — the leisure segment returned -37.87 and automotive was down -28.68. On the more positive side, utilities "only" dropped -6.02 and wireless was up .72 percent.

ELCA FOUNDATION PARTNERSHIP WITH ELCA BOARD OF PENSIONS

The ELCA Board of Pensions serves as investment adviser for two of the ELCA Foundation's investment funds — the ELCA Endowment Fund Pooled Trust and the Charitable Gift Annuity Reserve.

Attractive long-term investment returns allow congregations and beneficiary ministries to further their mission efforts. The Board of Pensions, as the ELCA's lifetime source of health, retirement and other benefits and related services, supports the ELCA Foundation's efforts to help strengthen the mission and benevolence of this church.

THE ELCA FOUNDATION



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SOCIAL PURPOSE INVESTING IN FUND A

Fund A — a social purpose fund — is managed by the ELCA Foundation's investment adviser for the ELCA Endowment Fund Pooled Trust — Fund A, the ELCA Board of Pensions, in a manner designed to achieve attractive long-term returns for Fund A participants while considering the corporate social responsibility work of the ELCA.

Fund A's social purpose program uses three strategies

The overarching investment goal for Fund A is to achieve economic success for participants while considering the corporate social responsibility work of the ELCA. The Board of Pensions uses a three-pronged approach for addressing social and corporate governance issues:

- 1 Positive social investments** — These investments positively benefit communities while earning acceptable returns for Fund A participants.
- 2 Shareholder advocacy** — The Board of Pensions votes proxies, initiates shareholder resolutions and engages in corporate dialogue to motivate corporate leaders to act in the best interests of shareholders (i.e., Fund A participants).
- 3 Social screening** — Social screening prohibits new investments in certain companies whose business practices don't meet the ELCA's corporate social criteria.

Fund A supports positive change

Positive social investing provides a proactive way for Fund A participants to receive market-rate returns on investments that channel capital to underserved markets. Typical investments may include securitized loans to promote community development, sustainable forestry, women- and minority-owned businesses and renewable energy.

Shareholder advocacy supports shareholders

Through shareholder advocacy the Board of Pensions works to motivate corporate leaders to act in the best interests of shareholders. These shareholder advocacy efforts include three components:

- 1 Proxy voting** — The Board of Pensions takes seriously its fiduciary responsibility to vote proxies. All proxy voting decisions are made solely in the best interests of participants and for the purpose of enhancing shareholder value of the company involved.

- 2 Dialogues** — Dialogue involves meeting face to face with corporate leaders. This method of interacting with companies is effective because it helps corporate decision makers understand why a proposed change has been requested. The Board of Pensions works in cooperation with other areas of this church to engage companies in dialogue.

- 3 Shareholder resolutions** — If a company does not respond favorably to dialogue, the Board of Pensions may file a shareholder resolution. Shareholder resolutions appear on proxy ballots prior to a corporation's annual meeting, giving every shareholder the opportunity to vote on a proposed change.

Social screens support church values

Each year, investment managers for screened portfolios receive a list of companies that may not be purchased for the fund due to business practices that conflict with the ELCA's corporate social criteria. Companies may appear on the list if they engage in aspects of these businesses:

- harmful products or services like tobacco, distilled alcohol, pornography or gambling
- those that research and develop nuclear, biological or chemical weapons; or manage U.S. government-owned facilities for such weapons
- those with significant toxic waste releases, hazardous waste sites, and environmental penalties or liabilities; and major producers of toxic chemicals

In collaboration with its social criteria consultant — KLD Research & Analytics Inc. — the Board of Pensions researches and evaluates thousands of companies in the process of determining which companies should appear on the list.



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The ELCA Foundation regional gift planners are located in regional offices throughout the country. Call (800) 638-3522, ext. 2970 or visit www.elca.org/foundation to find out more about how:

- your congregation or other ministry can establish an account in the Endowment Fund Pooled Trust
- you or a friend can leave a legacy for ministry
- you can establish contact with the regional gift planner nearest you



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