

**Episcopal Diocese of Northern California
Investment Fund**

First Quarter 2019

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HighMark Capital Management, Inc. is a subsidiary of MUFG Union Bank, N.A.

Investment Fund “A”

Discussion Highlights – April 2019

Economic and Investment Outlook

A new year ushered in a new tone for U.S. monetary policy, translating to a much-needed pivot point for investor sentiment following the worst quarterly decline for the S&P 500 Index since the fourth quarter of 2011 (during the height of the European Sovereign Debt Crisis). In the span of a few hours on January 4th, the equity market’s boogey man, a hawkish leaning Federal Reserve (“Fed”), seemingly vanished almost as quickly as it emerged as an underappreciated risk exactly three months earlier. Fed Chairman Jay Powell cast aside past comments indicating that monetary policy was on a predetermined tightening track, opting for more dovish terms that pleased equity market investors, like “patience” and “data dependence”.

In the minds of many investors before Powell’s about-face, the Fed was ignoring softening economic data not only at home but especially abroad. Perhaps the most concerning data point was a downshift in forward looking measures of economic activity in Europe and China. It seemed improbable that the U.S. could remain on an isolated economic island of prosperity as the rest of the world flirted with recession. Since then, the data has confirmed fears of a global economic deceleration with growth in the U.S. slowing in the fourth quarter of last year to 2.2% after having peaked in the second quarter at 4.2%.

Company fundamentals have not been immune to the economic malaise emanating from overseas. Adverse management guidance and analyst earnings estimate downgrades for 2019 have reflected the moderation of global growth. Yet investors piled back into global equities under the assumption that the Fed is on hold and may even retreat (i.e., cut rates). Facing the threat of a global economic slowdown, the removal of a potential accelerant by way of tighter monetary policy substantially reduced investors’ fear factor and resulted in a “V” shaped recovery for riskier assets across the board. At the end of the first quarter, the S&P 500 Index stood at just 3% below its all-time high set in late September 2018.

Asset Class Commentary

In conjunction with the market rally in the first quarter, the overall portfolio performance was mainly positive during this period, with only the Alternatives portion of the portfolio underperforming. In a reversal from the previous quarter, Small Cap Equities (+ 14.6%) outperformed Large Cap Equities (+ 13.7%). Emerging Market Equities also fared better in the first quarter, returning 9.9%. Fixed Income performed well, with Investment Grade Taxable returning 2.9% in the first quarter. For U.S. styles, Growth outperformed Value across market caps by 400 to 500-plus basis points in the first quarter, with Mid Cap Growth (+19.6%) performing the best. Large Cap Value (+ 11.9%) and Small Cap Value (+ 11.9%) were tied for the worst, yet still delivering positive, double-digit returns.

Recent Activity

During the quarter, we added to US Large Cap and Small Cap asset classes. Within Small Cap, we swapped the T.Rowe Price New Horizons Growth Fund for the Victory RS Growth Fund due to the exit of T.Rowe’s lead portfolio manager and three analysts for that strategy.

Investment Fund “A”

Discussion Highlights Continued – April 2019

Fund / Manager Commentary

Equity

The Total Equity portfolio strongly outperformed the MSCI All Country World Index by 168 basis points in the first quarter. Equity performance lagged that of the benchmark in 2018 mainly due to the portfolio’s lack of exposure to high growth technology stocks, which dominated for most of the year. This trend reversed in the first quarter, with strong performance across equity market caps (Small and Large) and regions (Domestic, International and Emerging Markets). Select Small Cap managers such as the Undiscovered Managers Behavioral Value Fund and the Victory RS Small Cap Growth Fund, performed particularly well, beating their benchmarks by 206 and 570 basis points respectively. The HighMark Custom Fundamental Advantage Strategy also outperformed in the first quarter, returning 14.95% vs. the 13.65% of its benchmark, the S&P 500 Index. This outperformance demonstrates the benefits of active management during more volatile market periods. We continue to expect active management to add value given the higher levels of volatility in the market and the normalization of interest rates.

Fixed Income

The combined Fixed Income allocation outperformed the Barclays Aggregate Bond index by 12 basis points in the first quarter. Positions in the PGIM Total Return Bond Fund (+4.02%) and the Eaton Vance Floating Rate Note Fund (+3.91%) largely drove this positive performance. Longer term (3-,5-, and 10- year periods), all of the fixed income managers (Dodge & Cox, PIMCO, and PGIM) have outperformed the Barclays Aggregate Bond index. We continue to be defensively positioned from a duration standpoint and remain focused on reducing credit risk.

Alternatives

The Alternatives portion of the portfolio underperformed its benchmark, the Wilshire Liquid Alternative Index, by 126 basis points in the first quarter. Given the diverse range of strategies within this asset class, there can be large deviations to the index. In accordance with its objective, the Alternatives portion is comprised of diversifying strategies with minimal correlation to equities and interest rates. Uncorrelated returns provide the benefit of diversification, but may result in negative performance during positive equity market environments. Based on our analysis of each Alternative fund’s annual return range along with actual historical results, the calendar year returns of each fund have been within expectations and have exhibited low correlation to equities and bonds. We continue to view Alternatives as a better source of returns in a rising interest rate environment relative to Fixed Income, with particular attractiveness given their profile of uncorrelated returns versus both equities and interest rates.

Investment Fund Portfolio Commentary

The Total Managed Portfolio (Net of Fees) outperformed the custom benchmark by 23 basis points in 2018, driven largely by strong performance from equities, which rallied in the first quarter, following the fourth quarter 2018 sell off. More recent underperformance is dragging down longer-term outperformance relative to both the benchmark and the peer group. Referencing page 8 of the enclosed presentation, the Total Managed Portfolio (excluding loans) has outperformed the past 4 out of 7 annual return periods. We believe that active management will be rewarded in the current environment of higher equity and interest rate volatility.

Asset Allocation – Investment Fund A

As of March 31, 2019

| Current Asset Allocation | |
|---------------------------------|----------------|
| Equity | 60.41% |
| Large Cap Core | 31.13% |
| Large Cap Value | 0.25% |
| Mid Cap Core | 2.79% |
| Small Cap Core | 1.97% |
| Small Cap Value | 2.69% |
| Small Cap Growth | 2.52% |
| International Core | 5.47% |
| International Value | 4.54% |
| International Growth | 4.65% |
| Emerging Markets | 4.41% |
| Fixed Income | 15.18% |
| Govt/Corp Obligations | 0.07% |
| Short-Term | 3.05% |
| Intermediate-Term | 7.96% |
| Multisector Bond | 4.09% |
| Alternatives | 9.45% |
| Multi Strategy | 2.03% |
| Managed Futures | 5.06% |
| Global Macro | 2.36% |
| Real Estate Loans | 9.57% |
| | 9.57% |
| Cash | 5.39% |
| | 5.39% |
| TOTAL | 100.00% |

Weighted Embedded Expense Ratio 0.41%

Target vs. Current Asset Allocation (as of March 31, 2019)

Investment Fund “A” Value: \$21,674,465

| <u>Asset Class</u> | <u>% Portfolio Weighting</u> | | | <u>Rationale</u> |
|---------------------------------|------------------------------|---------------|--------------------------|--|
| | <u>Range</u> | <u>Target</u> | <u>Current Portfolio</u> | |
| US Large Cap | 25-35% | 30% | 31.38% | Modest overweight given relatively stronger fundamentals versus other equity classes. |
| US Small-Mid Cap | 5-15% | 10% | 9.97% | Maintain neutral weight due to valuations. |
| International Developed | 10-20% | 15% | 14.66% | Shifted from overweight to neutral given concerns about slowing global growth and European risks. |
| Emerging Markets | 0-10% | 5% | 4.41% | Modest underweight given contagion concerns and ongoing global trade risk. Possible raise to neutral. |
| Fixed Income | 10-30% | 13% | 15.18% | Maintain underweight to traditional bonds with tactical overweight position to Multi-Strategies. |
| Alternatives & REITS | 0-15% | 5% | 9.45% | Continued overweight to Alternatives given low correlation to U.S. interest rates and equities. No REITs due to richer valuations. |
| Real Estate Loans | 15-33% | 17% | 9.57% | Real estate loans allocation moderated from 10.5% to 9.6% in 1Q19. |
| Cash | 0-10% | 5% | 5.39% | For cash requests, potential loans, and risk mgmt. |

**Selected Period Performance
EPISCOPAL DIOCESE ~A~ IAS**

Account *****1200

Period Ending: 3/31/2019

Actual returns are shown in black. Benchmark returns are shown in orange.

| | Year to Date (3 Months) | 1 Year | 2 Years | 3 Years | 5 Years | 10 Years | Inception to Date (375 Months) |
|---|-------------------------------|-------------|-------------|--------------|-------------|--------------|--------------------------------------|
| Cash Equivalents | .56 | 1.96 | 1.45 | 1.08 | .67 | .39 | 3.12 |
| <i>FTSE 3 Month T-Bill Index</i> | <i>.60</i> | <i>2.11</i> | <i>1.59</i> | <i>1.17</i> | <i>.72</i> | <i>.41</i> | <i>3.12</i> |
| Total Fixed Income | 3.06 | 4.20 | 3.65 | 4.04 | 3.30 | 4.08 | 6.00 |
| <i>BBG Barclays US Aggregate Bd Index</i> | <i>2.94</i> | <i>4.48</i> | <i>2.83</i> | <i>2.03</i> | <i>2.74</i> | <i>3.77</i> | <i>6.20</i> |
| Total Equities | 13.86 | 4.02 | 8.97 | 11.30 | 7.76 | 12.97 | 9.58 |
| <i>MSCI AC World Index</i> | <i>12.18</i> | <i>2.60</i> | <i>8.55</i> | <i>10.67</i> | <i>6.45</i> | <i>11.98</i> | |
| Total Managed Portfolio | 9.71 | 3.02 | 6.76 | 8.50 | 6.07 | 9.82 | 8.11 |
| Total Account Net of Fees** | 8.82 | 2.65 | 5.99 | 7.51 | 5.45 | 8.41 | 7.84 |
| <i>IF Benchmark***</i> | <i>9.29</i> | <i>4.88</i> | <i>7.03</i> | <i>8.28</i> | <i>6.15</i> | <i>10.50</i> | |
| <i>IF Benchmark 2****</i> | <i>8.59</i> | <i>3.84</i> | <i>6.54</i> | <i>7.56</i> | | | |
| <i>MS Mod Allocation Avg</i> | <i>8.91</i> | <i>3.83</i> | <i>5.73</i> | <i>7.30</i> | <i>5.07</i> | <i>9.50</i> | |
| Standard Deviation | | | | | 7.42 | | |
| <i>IF Benchmark***</i> | | | | | <i>7.25</i> | | |

Source: SEI Investments

Returns are gross of account level investment advisory fees and net of any fees, including fees to manage mutual fund or exchange traded fund holdings. Returns for periods over one year are annualized. The information presented has been obtained from sources believed to be accurate and reliable. Past performance is not indicative of future returns. Securities are not FDIC insured, have no bank guarantee, and may lose value. * The Total Managed Portfolio is gross of fees and excludes the Real Estate Loans. The investment managements fees are approximately .23%. **The Total Account Net of Fees includes the Real Estate Loans (which are managed by the Diocese). ***IF Benchmark: 30% S&P 500, 10% Russell 2000, 15% MSCI EAFE, 5% MSCI EM Free, 5% NAREIT, 30% Barclay's Aggregate Bond, 5% Citigroup 3 Month T-Bill Index. Benchmark was created and became applicable at the two year period. ****IF Benchmark 2: 30% S&P 500, 10% Russell 2000, 15% MSCI EAFE, 5% MSCI EM Free, 5% Wilshire Liquid Alternative, 30% Barclay's Aggregate Bond, 5% Citigroup 1 Month T-Bill Index. Benchmark was created and became applicable on 5/01/2016. Due to the change in the investment guidelines to allow for more equities, asset classes, and manager discretion these benchmarks will become a more appropriate comparison. The MSCI AC World Index is becoming a more appropriate benchmark for stock portfolios that include U.S., International, and Emerging Market exposure since the index has representation in all three areas.

Account Name: EPISCOPAL DIOCESE ~B~ BOND FUND

Account ID: *****5500



As of: March 31, 2019

Performance Report

| | Market Value | Year to Date (3 Months) | 1 Year | 2 Years | 3 Years | 5 Years | 10 Years | Inception to Date 05/01/2008 |
|--|----------------|-------------------------------|-------------|-------------|-------------|-------------|-------------|------------------------------------|
| Cash Equivalents | 51,796 | .57 | 1.96 | 1.45 | 1.07 | .67 | .39 | .52 |
| FTSE 3 Month T-Bill Index | | .60 | 2.11 | 1.59 | 1.17 | .72 | .41 | .46 |
| Total Fixed Income | 506,923 | 3.14 | 4.07 | 3.24 | 3.63 | 2.98 | 4.34 | |
| BBG Barclays 1-3 Yr US Govt/Credit Index | | 1.21 | 3.03 | 1.62 | 1.32 | 1.22 | 1.59 | 1.76 |
| BBG Barclays Intmtd US Govt/Cred | | 2.32 | 4.24 | 2.28 | 1.66 | 2.12 | 3.14 | 3.13 |
| Total Managed Portfolio | 558,719 | 2.93 | 3.84 | 2.81 | 2.93 | 2.40 | 3.38 | 3.30 |
| Total Account Net of Fees | 558,719 | 2.93 | 3.84 | 2.81 | 2.93 | 2.40 | 3.38 | 3.30 |

Returns are gross of account level investment advisory fees and net of any fees including fees to manage mutual fund or exchange traded fund holdings. Returns for periods over one year are annualized. The information presented has been obtained from sources believed to be accurate and reliable. Past performance is not indicative of future returns. Securities are not FDIC insured have no bank guarantee and may lose value.

Account Name: EPISCOPAL DIOCESE ~C~ CASH FUND

Account ID: *****5600



As of: March 31, 2019

Performance Report

| | Market Value | Year to Date (3 Months) | 1 Year | 2 Years | 3 Years | 5 Years | 10 Years | Inception to Date 05/01/2008 |
|----------------------------------|----------------|-------------------------------|-------------|-------------|-------------|------------|------------|------------------------------------|
| Cash Equivalents | 345,675 | .56 | 1.96 | 1.45 | 1.08 | .67 | | |
| FTSE 3 Month T-Bill Index | | .60 | 2.11 | 1.59 | 1.17 | .72 | .41 | .46 |
| Total Managed Portfolio | 345,675 | .57 | 1.96 | 1.45 | 1.08 | .67 | .35 | .49 |
| Total Account Net of Fees | 345,675 | .57 | 1.96 | 1.45 | 1.08 | .67 | .37 | .50 |

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