

**Episcopal Diocese of Northern California
Investment Fund**

First Quarter 2020

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

Investment Fund “A”

Discussion Highlights – April 2020

Economic and Investment Outlook

By all accounts, the global economy was hitting its stride entering 2020. In the U.S., dovish monetary policy led to three rate cuts providing the economy room to extend its historically long run. German manufacturing data, a proxy for global trade, was inflecting upward and U.S. employment was as strong as it had been in decades with no signs of slowing down. Investors viewed a trade conflict ceasefire as the last remaining obstacle to be cleared before continuing to add risk. Equity markets had anticipated much of this good news as evidenced by strong 2019 returns that continued into the first seven weeks of 2020.

At the same time, little attention was paid to a growing concern in China about a mysterious and rapidly spreading illness. Even when China placed large portions of its population under quarantine orders in late January, investors dismissed the action as a blip on the radar screen. However, by the end of February, “coronavirus” was becoming a household term. The disease it causes, COVID-19, was formally declared a global pandemic by the World Health Organization on March 13.

The economic and market ramifications of widespread government-mandated social distancing policies intended to prevent contagion were wide and deep. As soon as it became apparent that the problem would not be isolated to China, investors recalibrated to a new paradigm that included a temporary shutdown of major segments of the global economy. Investors raced to exit any asset deemed “risky” in a search for safety. The demand for “risk haven” U.S. Treasury bonds drove the 10-year Note’s yield down to 0.33% from a yield of 1.91% at the beginning of the year.

This extraordinary exogenous shock was like a record scratch of epic proportions for financial markets that were dancing to a very upbeat song. After hitting an all-time high on February 19, the S&P 500 index sold off into bear market territory at the fastest speed on record, and market volatility as measured by the CBOE Volatility Index (VIX), soared to levels that exceeded prior highs set during the Great Financial Crisis in 2008.

Asset Class Commentary

In conjunction with the market selloff in the first quarter of 2020, the overall portfolio performance was negative across asset classes during this period. U.S. Large Cap Equities (-19.6%) outperformed both U.S. Mid Cap Equities (-27.1%) and U.S. Small Cap Equities (-30.6%) in the first quarter, as investors turned towards quality and defensive stocks. For Fixed Income, U.S. Treasuries were the best performer, with the 10-year Note returning 11.9% in the first quarter. In contrast, in reaction to the sudden slowdown in the economy resulting from the COVID-19 pandemic, investment-grade bond spreads exploded and U.S. Corporate Bonds struggled, returning -3.6%. For U.S. styles, Growth outperformed Value across all market caps by 1000 to 1200-plus basis points in the first three months of the year, continuing a dynamic that we have observed for the past decade.

Recent Activity

During the quarter, we initiated a position in the American Beacon AHL Managed Futures Strategy and rebalanced within Alternatives and Large Cap equities.

Investment Fund “A”

Discussion Highlights Continued – April 2020

Fund / Manager Commentary

Equity

The Total Equity portfolio underperformed the MSCI All Country World Index by 128 basis points in the first quarter, reversing a trend from the prior year. While absolute performance was negative across equity market caps (Small, Mid and Large) and regions (Domestic, International and Emerging Markets) a few Small Cap managers had stronger relative performance. The Victory RS Small Cap Growth Fund and the Delaware Small Cap Core Fund beat their benchmarks, the Russell 2000 Growth Index and the Russell 2000 Index by 173 and 300 basis points, respectively. After outperforming its benchmark, the S&P 500 Index, by over 100 basis points in 2019, the HighMark Custom Fundamental Advantage Strategy modestly underperformed in the first three months of 2020. We believe that 2019's outperformance demonstrates the benefits of active management during more volatile market periods and continue to expect active management to add value given increased levels of volatility.

Fixed Income

The combined Fixed Income allocation underperformed the Bloomberg Barclays Aggregate Bond Index by 500 basis points in the first quarter of the year. Our positions in the PIMCO Income Fund (-7.66%) and the PGIM Total Return Bond Fund (-2.84%) acted as the largest detractors to performance in the quarter. Longer term (5- and 10- year periods), all of the fixed income managers (Dodge & Cox, PIMCO, and PGIM) performed in-line with to outperformed the Bloomberg 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 outperformed its benchmark, the Wilshire Liquid Alternative Index, by 138 basis points in the first quarter of 2020. However, absolute returns suffered given the unprecedented dislocation in the global credit markets. Managed futures strategies (American Beacon, AQR, Natixis ASG) were a bright spot. Despite the choppiness in equity markets, these strategies registered positive performance in a month where virtually everything other than U.S. Treasuries were down. Trends in currencies (long U.S. Dollar), commodities (short oil, gas) and interest rates (long bonds) all benefited during the month.

Investment Fund Portfolio Commentary

The Total Account (Net of Fees) underperformed the custom benchmark and the peer group in the first quarter of 2020. However, the loan portion of the portfolio provided some support with a positive return. The Total Managed Portfolio (excluding loans) underperformed for the quarter as well following a very strong 2019. The Fixed Income and International equity managers were the main detractors to performance during this unprecedented global crisis. We have seen a strong rebound in April with nearly all managers showing improved performance as the equity and credit markets have recovered to a large extent. We remain cautious over the next 3-6 months with an underweight to equities and a shift towards higher quality and more defense.

Asset Allocation – Investment Fund A

As of March 31, 2020

| Current Asset Allocation | |
|---------------------------------|----------------|
| Equity | 55.46% |
| Large Cap Core | 31.11% |
| Mid Cap Core | 2.03% |
| Small Cap Core | 2.19% |
| Small Cap Value | 1.60% |
| Small Cap Growth | 1.94% |
| International Core | 4.50% |
| International Value | 3.62% |
| International Growth | 4.29% |
| Emerging Markets | 4.18% |
| Fixed Income | 20.19% |
| Govt/Corp Obligations | 0.04% |
| Short-Term | 3.74% |
| Intermediate-Term | 12.50% |
| Multisector Bond | 3.91% |
| Alternatives | 10.68% |
| Global Macro | 3.58% |
| Managed Futures | 4.68% |
| Merger Arbitrage | 0.90% |
| Multi Strategy | 0.88% |
| Real Estate | 0.63% |
| Real Estate Loans | 8.62% |
| | 8.62% |
| Cash | 5.05% |
| | 5.05% |
| TOTAL | 100.00% |

Weighted Embedded Expense Ratio 0.40

Target vs. Current Asset Allocation (as of March 31, 2020)

Investment Fund “A” Value: \$22,211,121

| <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% | 31.11% | Shifted to modest overweight given relatively stronger fundamentals versus other equity classes. |
| US Small-Mid Cap | 5-15% | 10% | 7.76% | Maintain underweight due to valuations and high beta. |
| International Developed | 10-20% | 15% | 12.41% | Continued underweight due to concerns due to global recession and higher risk |
| Emerging Markets | 0-10% | 5% | 4.18% | Maintain underweight given global recession, higher risk, and dollar strength. |
| Fixed Income | 10-30% | 13% | 20.19% | Gradual shift to reduce given record low rates |
| Alternatives & REITS | 0-15% | 5% | 10.68% | Continued overweight to Alternatives given low correlation to fixed income and equities. |
| Real Estate Loans | 15-33% | 17% | 8.62% | Maintaining position at this time. |
| Cash | 0-10% | 5% | 5.05% | Focus on risk management. Will re-deploy opportunistically given cautious stance. |

Selected Period Performance
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Period Ending: 3/31/2020

| | Year to Date (3 Months) | 1 Year | 2 Years | 3 Years | 5 Years | 10 Years | Inception to Date 01/01/1988 |
|---|-------------------------------|--------|---------|---------|---------|----------|------------------------------------|
| Cash Equivalents | .31 | 1.82 | 1.89 | 1.57 | 1.03 | .53 | 3.08 |
| <i>FTSE 3 Month T-Bill Index</i> | .39 | 2.04 | 2.08 | 1.74 | 1.12 | .60 | 3.09 |
| Total Fixed Income | -2.15 | 2.80 | 3.50 | 3.37 | 3.24 | 3.65 | 5.90 |
| <i>BBG Barclays US Aggregate Bd Index</i> | 3.15 | 8.93 | 6.68 | 4.82 | 3.36 | 3.88 | 6.28 |
| Total Equities | -22.65 | -12.34 | -4.51 | 1.35 | 3.25 | 7.23 | 8.82 |
| <i>MSCI AC World Index</i> | -21.37 | -11.26 | -4.58 | 1.50 | 2.85 | 5.88 | |
| Total Managed Portfolio | -16.09 | -7.48 | -2.37 | 1.78 | 2.97 | 6.25 | 7.59 |
| Total Account Net of Fees | -15.07 | -7.15 | -2.37 | 1.42 | 2.55 | 5.41 | 7.34 |
| <i>IF Benchmark ***</i> | -14.31 | -5.61 | -.50 | 2.64 | 3.43 | 6.29 | |
| <i>IF Benchmark ****</i> | -13.48 | -5.04 | -.70 | 2.53 | | | |
| <i>MS Mod Allocation Avg</i> | -14.71 | -6.90 | -1.68 | 1.34 | 2.24 | 5.37 | |
| Standard Deviation | | | | | 9.25 | | |
| <i>IF Benchmark ***</i> | | | | | 9.04 | | |

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 management fees are approximately 0.23%. **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% FTSE 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% FTSE 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.



As of: March 31, 2020

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 | 24,472 | .31 | 1.82 | 1.89 | 1.57 | 1.03 | .53 | .63 |
| FTSE 3 Month T-Bill Index | | .39 | 2.04 | 2.08 | 1.74 | 1.12 | .60 | .59 |
| Total Fixed Income | 509,714 | -1.73 | 3.43 | 3.75 | 3.31 | 3.08 | 3.51 | |
| BBG Barclays 1-3 Yr US Govt/Credit Index | | 1.69 | 4.53 | 3.77 | 2.58 | 1.90 | 1.62 | 1.99 |
| BBG Barclays Intmtdt US Govt/Cred | | 2.40 | 6.88 | 5.55 | 3.79 | 2.76 | 3.14 | 3.44 |
| Total Managed Portfolio | 534,185 | -1.65 | 3.22 | 3.53 | 2.95 | 2.54 | 2.79 | 3.30 |
| Total Account Net of Fees | 534,185 | -1.65 | 3.22 | 3.53 | 2.95 | 2.54 | 2.79 | 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.



As of: March 31, 2020

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 | 379,765 | .31 | 1.82 | 1.89 | 1.57 | 1.03 | .53 | |
| FTSE 3 Month T-Bill Index | | .39 | 2.04 | 2.08 | 1.74 | 1.12 | .60 | .59 |
| Total Managed Portfolio | 379,765 | .31 | 1.82 | 1.89 | 1.58 | 1.03 | .51 | .60 |
| Total Account Net of Fees | 379,765 | .31 | 1.82 | 1.89 | 1.58 | 1.03 | .51 | .61 |

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