

**Episcopal Diocese of Northern California  
Investment Fund**

**Third Quarter 2020**

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

# Investment Fund “A”

## Discussion Highlights – September 2020

### **Economic and Investment Outlook**

Entering the fourth quarter of a calamitous year, financial markets remain keenly focused on a host of short- and long-term challenges facing the global economy in the wake of the COVID-19 pandemic. A record worst U.S. real GDP growth rate in the second quarter of -31.4% annualized was emblematic of the economic distress the rest of the world encountered as governments scrambled to contain the spread of the infection. Meanwhile, a voracious rally in the global stock market from April through August would suggest that investors believe at least the worst of the economic storm may be in the rear-view mirror. Yet, lingering questions remain about what lies ahead in the aftermath.

Confronted with a crisis of epic proportions, policymakers swiftly unleashed unprecedented levels of fiscal and monetary relief, reviving financial markets and a cratering economy. On the surface, economic data from employment to consumer spending has recovered at a heartening pace as the global economy emerges from the depths of a major health crisis. The headline statistics, however, may distort a recovery trajectory that is not as uniform as it may appear. Major segments of the economy, including the travel and hospitality industries, remain hamstrung by virus-driven restrictions prohibiting the resumption of pre-pandemic activity levels. It remains to be seen if this weakness will remain isolated from the broader economy or if it begins to weigh on it.

### **Asset Class Commentary**

Following a challenging first few months of the year, the total portfolio (net of fees) modestly outperformed its blended benchmark for the third quarter. We are encouraged with the performance recovery given the unique and volatile market environment.

Large Cap Equities (8.9%) outperformed both Mid Cap Equities (7.5%) and Small Cap Equities (4.9%) in the third quarter. This continues a trend, as Large Cap Equities have also outperformed Mid Cap and Small Cap for the year-to-date period ending September 30<sup>th</sup>. Fixed Income performed well, with Investment Grade Taxable returning 6.8% for the year-to-date period. For U.S. styles, Growth outperformed Value across all market caps by 300 to 750-plus basis points in the third quarter and by 2500 to 3500-plus basis points for the year-to-date period. This extreme growth vs. value outperformance continues a dynamic that we have observed the past decade.

### **Recent Activity**

During the quarter, we did some modest rebalancing within the large cap equity portion as well as a reduction the AQR Style Premia Fund.

# Investment Fund “A”

## Discussion Highlights Continued – September 2020

### Fund / Manager Commentary

#### **Equity**

Following strong equity portfolio performance in the second quarter, the Total Equity portfolio underperformed the MSCI All Country World Index (“ACWI”) by 94 basis points in the third quarter. Select Small Cap managers such as the Victory RS Small Cap Growth Fund have continued to perform particularly well in 2020, returning 12.85% and beating the Russell 2000 Growth Index by almost 900 basis points year-to-date. The Value and International managers have been detractors. While the HighMark Custom Fundamental Advantage Strategy modestly underperformed its benchmark the S&P 500 for the year-to-date period, we continue to view this allocation as an important part of the overall portfolio, particularly given the benefits of active management during more volatile market periods.

#### **Fixed Income**

In the third quarter, the combined Fixed Income allocation delivered a positive return (+1.74%), outperforming the Bloomberg Barclays Aggregate Bond Index (0.62%) by 112 basis points. The position in the PIMCO Income Fund (3.00%) acted as the strongest contributor to performance in the quarter, though all of the other bond strategies also performed well, with the Dodge and Cox Income Fund, PIMCO Total Return Fund, PGIM Total Return Bond Fund and the Vanguard Short-Term Investment Fund returning 1.48%, 1.49%, 1.77% and 0.93%, respectively. Longer term (5- and 10-year periods), all of the fixed income managers (Dodge & Cox, PIMCO, PGIM, and Vanguard) have outperformed. We remain defensively positioned from a duration standpoint as longer-term bonds offer very little value, with the 10-year Treasury yielding under 1.00%.

#### **Alternatives**

The Alternatives portion of the portfolio underperformed its benchmark, the Wilshire Liquid Alternative Index, by 65 basis points in the third quarter of 2020. AlphaSimplex Managed Futures Strategy continued to outperform, returning 2.70% in the third quarter. The REITs, which are now part of the Alternatives category, as well as AQR Style Premia have been the main detractors. Given the diverse range of strategies within this asset class, there may be 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. 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 believe that Alternatives remain a better source of returns relative to Fixed Income, with particular attractiveness given their profile of uncorrelated returns versus both equities and interest rates.

### Investment Fund Portfolio Commentary

Following an excellent 2019, the underperformance for 2020 year-to-date is due primarily to the challenging and volatile first quarter, during the global shutdown and massive stock and credit market selloff. The Total Account (Net of Fees) underperformed the custom benchmark by 140 basis points and the peer group by 36 basis points for the year-to-date period ending September 2020. However, more recent performance in the second and third quarters has been improving and outperforming. We continue to 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 September 30, 2020

<b>Current Asset Allocation</b>	
<b>Equity</b>	<b>60.85%</b>
Large Cap Core	34.40%
Mid Cap Core	2.28%
Small Cap Core	2.29%
Small Cap Value	1.65%
Small Cap Growth	2.44%
International Core	4.81%
International Value	3.62%
International Growth	4.64%
Emerging Markets	4.71%
<b>Fixed Income</b>	<b>18.10%</b>
Govt/Corp Obligations	0.03%
Short-Term	3.32%
Intermediate-Term	11.21%
Multisector Bond	3.54%
<b>Alternatives</b>	<b>9.34%</b>
Global Macro	3.07%
Managed Futures	3.85%
Merger Arbitrage	0.80%
Multi Strategy	1.01%
Real Estate	0.60%
<b>Real Estate Loans</b>	<b>7.09%</b>
	7.09%
<b>Cash</b>	<b>4.63%</b>
	4.63%
<b>TOTAL</b>	<b>100.00%</b>

Weighted Embedded Expense Ratio 0.39

# Target vs. Current Asset Allocation (as of September 30, 2020)

Investment Fund “A” Value: \$26,195,115

<u>Asset Class</u>	<u>% Portfolio Weighting</u>			<u>Rationale</u>
	<u>Range</u>	<u>Target</u>	<u>Current Portfolio</u>	
<b>US Large Cap</b>	25-35%	30%	34.40%	Reducing overweight given richer valuations versus other equity classes.
<b>US Small-Mid Cap</b>	5-15%	10%	8.66%	Moving to a neutral weight given improving market breadth and fundamentals.
<b>International Developed</b>	10-20%	15%	13.07%	Moving to neutral given cheaper valuations and weaker dollar.
<b>Emerging Markets</b>	0-10%	5%	4.71%	Moving to overweight given improving fundamentals and weaker dollar.
<b>Fixed Income</b>	10-30%	13%	18.10%	Maintain neutral weight to traditional bonds with tactical overweight position to Multi-Strategies.
<b>Alternatives &amp; REITS</b>	0-15%	5%	9.34%	Continued overweight to Alternatives given low correlation to fixed income and equities.
<b>Real Estate Loans</b>	15-33%	17%	7.09%	Maintaining position at this time.
<b>Cash</b>	0-10%	5%	4.63%	Focus on risk management. Will re-deploy opportunistically given cautious stance.

**Selected Period Performance**  
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**Period Ending: 9/30/2020**

	3 Months	Year to Date (9 Months)	1 Year	2 Years	3 Years	5 Years	10 Years	Inception to Date 01/01/1988
Cash Equivalents	.01	.36	.76	1.48	1.46	1.03	.53	3.04
<i>FTSE 3 Month T-Bill Index</i>	<i>.03</i>	<i>.56</i>	<i>1.02</i>	<i>1.69</i>	<i>1.65</i>	<i>1.16</i>	<i>.61</i>	<i>3.05</i>
Total Fixed Income	1.74	5.09	6.00	7.11	4.84	4.85	3.73	6.04
<i>BBG Barclays US Aggregate Bd Index</i>	<i>.62</i>	<i>6.79</i>	<i>6.98</i>	<i>8.63</i>	<i>5.24</i>	<i>4.18</i>	<i>3.64</i>	<i>6.30</i>
Total Equities	7.19	.36	9.30	5.79	7.17	10.67	10.20	9.55
<i>MSCI AC World Index</i>	<i>8.13</i>	<i>1.37</i>	<i>10.44</i>	<i>5.81</i>	<i>7.12</i>	<i>10.30</i>	<i>8.55</i>	
Total Managed Portfolio	5.16	.98	7.08	5.31	5.73	8.28	8.20	8.08
Total Account Net of Fees	4.79	.80	6.38	4.76	5.13	7.34	7.18	7.79
<i>IF Benchmark ***</i>	<i>4.67</i>	<i>1.61</i>	<i>7.29</i>	<i>5.95</i>	<i>6.35</i>	<i>8.31</i>	<i>7.84</i>	
<i>IF Benchmark ****</i>	<i>4.71</i>	<i>2.20</i>	<i>7.96</i>	<i>5.79</i>	<i>6.15</i>			
<i>MS Mod Allocation Avg</i>	<i>4.93</i>	<i>1.16</i>	<i>6.28</i>	<i>4.83</i>	<i>5.39</i>	<i>7.13</i>	<i>7.05</i>	
Standard Deviation						9.78		
<i>IF Benchmark ***</i>						<i>9.59</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 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: September 30, 2020

Performance Report

	Market Value	Year to Date (9 Months)	1 Year	2 Years	3 Years	5 Years	10 Years	Inception to Date 05/01/2008
<b>Cash Equivalents</b>	<b>5,709</b>	<b>.36</b>	<b>.76</b>	<b>1.48</b>	<b>1.46</b>	<b>1.03</b>	<b>.53</b>	<b>.61</b>
FTSE 3 Month T-Bill Index		.56	1.02	1.69	1.65	1.16	.61	.58
<b>Total Fixed Income</b>	<b>524,199</b>	<b>5.19</b>	<b>5.76</b>	<b>7.33</b>	<b>4.69</b>	<b>4.64</b>	<b>3.69</b>	
BBG Barclays 1-3 Yr US Govt/Credit Index		3.12	3.73	4.18	2.84	2.09	1.57	2.02
BBG Barclays Intmtd US Govt/Cred		5.92	6.32	7.24	4.43	3.39	2.91	3.58
<b>Total Managed Portfolio</b>	<b>529,908</b>	<b>4.94</b>	<b>5.51</b>	<b>6.91</b>	<b>4.44</b>	<b>4.03</b>	<b>3.26</b>	<b>3.70</b>
<b>Total Account Net of Fees</b>	<b>529,908</b>	<b>4.94</b>	<b>5.51</b>	<b>6.91</b>	<b>4.44</b>	<b>4.03</b>	<b>3.26</b>	<b>3.70</b>

Returns are gross of fees not including account level advisory fees unless otherwise stated. Gross returns are presented before management and custodial fees but after all trading expenses, embedded and reflect the reinvestment of dividends and other income. Net returns are net of investment management fees in effect for the respective time period. 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



As of: September 30, 2020

## Performance Report

	Market Value	Year to Date (9 Months)	1 Year	2 Years	3 Years	5 Years	10 Years	Inception to Date 05/01/2008
<b>Cash Equivalents</b>	<b>377,888</b>	<b>.36</b>	<b>.76</b>	<b>1.48</b>	<b>1.46</b>	<b>1.03</b>	<b>.53</b>	
FTSE 3 Month T-Bill Index		.56	1.02	1.69	1.65	1.16	.61	.58
<b>Total Managed Portfolio</b>	<b>377,888</b>	<b>.36</b>	<b>.76</b>	<b>1.48</b>	<b>1.46</b>	<b>1.04</b>	<b>.51</b>	<b>.58</b>
<b>Total Account Net of Fees</b>	<b>377,888</b>	<b>.36</b>	<b>.76</b>	<b>1.48</b>	<b>1.46</b>	<b>1.04</b>	<b>.51</b>	<b>.59</b>

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