The San Diego Foundation
Growing a Vibrant Region

INVESTMENT NARRATIVE
QUARTER ENDING MARCH 31, 2019

After an extremely volatile end to 2018, global capital markets rebounded significantly in the first quarter of 2019. The turn in markets was largely attributable to the Federal Reserve Bank (Fed) changing its posture. Late in the year, the Fed raised interest rates, reporting strong economic growth, low unemployment, and some concern over wage growth, an important driver of inflation. After global markets tumbled throughout the quarter, the Fed reversed course and signaled to the market it had become more data dependent and less likely to hike interest rates. Throughout 2019, the Fed has remained fairly accommodative, leaving interest rates unchanged year-to-date.

Another reason for the strong market returns of the first quarter included easing concerns around trade tensions. In March, negotiations resumed between high-level U.S. and Chinese trade delegations. The global equity markets began forecasting a more optimistic outlook of a Chinese trade deal.

The fixed income markets also produced strong results for the first quarter. The more dovish stance of the Fed led to a decline in treasury yields throughout the quarter. Treasury yields have an inverse relationship with bond prices, resulting in broad appreciation. Corporate bonds also performed well after selling off in the fourth quarter, particularly more risky areas like high yield.

Endowment

In the Endowment portfolio, all major asset classes delivered positive performance for the first quarter. The portfolio was largely able to recoup the losses it experienced in the fourth quarter of last year. The Endowment portfolio was up 7.8% for the first quarter, ahead of its policy index by 60 basis points. Global equities were the strongest contributor to performance, led by the U.S. markets, followed by non-U.S. developed markets and emerging markets.

The largest detractor from relative performance was the hedge fund segment of the portfolio, posting a 2.3% gain for the first quarter. The Endowment portfolio utilizes hedge funds to reduce the overall volatility of the portfolio. Because the portfolio's hedge funds tend to be more conservative, they posted a smaller loss in the fourth quarter when markets were down, yet posted a smaller gain in the first quarter when markets rebounded.

Non-Endowment

The Long-Term Portfolio was up 8.8% for the quarter, slightly underperforming the policy index by 0.2%. The biggest relative detractor from performance was in alternatives. During the quarter, the alternatives portfolio was restructured. The portfolio had previously consisted of "liquid alternatives," or investment vehicles attempting to replicate more traditional hedge fund strategies. Early in the quarter, those positions were eliminated and replaced by more traditional hedge funds, in order to dampen the volatility of the portfolio. These positions tend to have less correlation to the market and more capital protection elements, resulting in underperformance for the quarter.

The Medium-Term Portfolio was up 5.6% for the quarter, slightly outperforming the policy index by 0.2%. Again, International Equity made huge relative gains. Equity positions produced the strongest relative performance, followed by fixed income. Within the Medium-Term Portfolio, one of its fixed income managers produced very strong relative results after underperforming in the fourth quarter.

The Short-Term Portfolio was up 0.6% during the quarter. As the Fed increased short-term interest rates, money market rates have increased. This has resulted in a more attractive return on cash-like assets, such as those held in the portfolio.