Investment Narrative

Quarter Ending December 31, 2022

Slight improvements to key economic data fueled a sizeable rebound in the fourth quarter as investor sentiment began to lighten with the growing possibility of a soft landing by the Federal Reserve. Driven mainly by decreasing energy and gas prices, inflation rates have been dwindling each month - signaling that the U.S. may be past its peak inflationary environment. However, other products such as food, housing, medical care, and airfare have either remained elevated or continued to increase. The Federal Reserve upheld its plans to combat inflation with quantitative tightening and pressed on with smaller, additional rate hikes. As such, capital markets have been stifled by the increased cost of capital and many companies have been forced to cut expenses or delay projects. This resulted in a slight decrease in GDP growth and additional layoffs across the U.S. with a sizeable portion concentrated in the technology sector. Lofty prices, cuts to personal income, and economic uncertainty were partly evident in the decreased consumer spending overall and increasing retail inventories. Nevertheless, employment rates have remained strong and GDP growth was still positive.

Despite weakness in December, the fourth quarter was positive for the U.S. markets. The broad U.S. stock market, which is tracked by the S&P 500 Index, was up 7.6%, the U.S. small cap market, which is represented by the Russell 2000 Index, was up 6.2%, and the U.S. bond market, which is reflected by the Bloomberg U.S. Aggregate Bond Index, was up 2.2%.

The fourth quarter rally was even more robust outside of the United States. Importantly, the U.S. dollar strength may have peaked during the quarter, resulting in strong gains for stocks denominated in foreign currencies. For the fourth quarter, the non-U.S. developed markets, which are tracked by the MSCI EAFE Index, were up 17.3%, and the emerging markets region, which is represented by the MSCI Emerging Markets Index, was up 9.7%.

When the market bells rang for the last time in 2022, the year concluded to be that of an anomaly. For the first time since 1969, stocks and bonds were both down for the year. This is an extremely rare occurrence that has only happened a total of 6 times since 1890. Navigating this market environment proved to be arduous for investors being that no allocation, no matter how aggressive or conservative, was safe from the drawdowns experienced over 2022. For the year, the broad U.S. market was down 18.1%, U.S. small cap was down 20.4%, international ex-U.S. was down 14.5%, emerging markets was down 20.1%, and the U.S. bond market was down 13.0%.

Endowment

The Endowment portfolio was up 4.7% for the fourth quarter, outpacing its policy index by 0.4%. Over the 1-year, 3-year, 5-year and 7-year periods, the Endowment has ranked within the top quartile relative to its peer set of similarly sized endowment and foundations. Most asset classes were positive for the quarter. International equities and emerging market equities were the best performers. Real estate was the only assets class with a negative return of 3.8%. Over the year, the portfolio was positioned more defensively and benefitted from being tilted towards hedge funds, private equity/credit, and real estate and underweight global equities in an attempt to avoid the volatile drawdowns. While the underweight to global equities detracted during the fourth quarter, the portfolio's positioning for the year allowed it to outperform both stocks and bonds.

Non-Endowment

The Long-Term portfolio was up 6.9% for the quarter, outpacing its policy index by 0.3%. The biggest drivers of outperformance this quarter were largely due to the portfolio's fixed income and international equity investment managers. The best performing asset classes in the portfolio were equities and real assets, yielding returns of 10.5% and 7.0%, respectively.

The Medium-Term portfolio was up 4.7% for the quarter and outperformed its policy index by 0.8%. As interest rate hikes slowed, bond prices have continued to normalize, but have still experienced some volatility. The portfolio is mainly composed of fixed income and therefore will benefit less from rallies in the equity markets than the Endowment or Long-Term portfolios. Once prices fully stabilize in the bond market, the portfolio will greatly benefit from a higher interest rate environment. Attribution for the quarter was driven by allocations to short-term fixed income and manager selection in international equities.

The Intermediate-Term portfolio, which consists purely of bonds, was up 2.3% for the quarter and outperformed its policy index by 0.7%. The portfolio's 60% allocation to intermediate-duration bonds supported its outperformance.

The Short-Term portfolio was up for the quarter with a return of 0.9%. The portfolio has greatly benefited from the Federal Reserve's continued tightening policy as short-term rates remain higher. Additional rate hikes will be favorable to the portfolio's performance.

The Sustainable Endowment and Non-Endowment portfolios were up 6.6% for the quarter, compared to their policy index up 7.6% in the same period. The main detractor to the portfolios' performance was due to the lack of energy sector exposure within their global equity allocations. Performance has improved significantly from Q3 to Q4 as the overall equity markets have recovered over the last few months.