# Catholic Foundation of Northeast Kansas (CFNEK)

**Investment Committee Responsibilities:**

- Monitor appropriate risk posture and time horizon of both the Equity Portfolio (EP) and Fixed Income Portfolio (FIP)
- Monitor target allocation
- If allocation is not “in line,” understand why and take appropriate steps to correct
- Monitor rebalancing procedures
- Monitor investments according to the CFNEK Investment Policy Statements (IPS) guidelines, including Catholic value screens
- Perform reviews quarterly

## CFNEK Investment Committee Statement – 3Q 2020

For the second consecutive quarter, stock markets saw significant strength, though optimism, irrepressible in July and August, softened in September as investors considered this conundrum:

Can the market maintain momentum in the presence of elevated ambiguity? The trifecta of an unpredictable Presidential election, the caginess of a COVID vaccine and the valuation of the indices (rising prices, but petering profits) has made markets justifiably jumpy.

It is often said that financial markets climb a “wall of worry” when referring to their resilience in the face of adversity. And it is fair to say that resting at base camp is well-deserved given their ascendancy from the “floor” (the pandemic lows of late-March).

As you’ll read in the commentary below the team at Tower Wealth Managers has made some tactical modifications to their asset allocation, while adhering to the United States Conference of Catholic Bishops (USCCB) Socially Responsible Investing Guidelines, to fortify the portfolio for the summit attempt in the 4th quarter.

www.cfnek.org/IPS

Doug Ciocca
Chair, Investment Committee

## Market Commentary from Tower Wealth Managers, LLC

Tower Wealth Managers (TWM), a wholly owned subsidy of Country Club Trust Company, has been the investment manager for the CFNEK funds since mid-2017. The first two months -July and August, 2017 - were a transition period for the funds. During this time assets were received by TWM from the previous manager and repositioned to funds and assets used by TWM. Due to the transition of the assets during the months of July and August, performance numbers are not available on the individual solutions in each of the Equity and Fixed Income Funds for these two months. Hence, we are only able to provide performance for the total Equity Fund and Fixed Income Fund during this time. TWM's investment performance for the two Funds has an inception date of August 31, 2017.

One of the main goals the CFNEK Board has for the management of these funds is a strict adherence to the United States Conference of Catholic Bishops (USCCB) Socially Responsible Guidelines. The Board set a target of 97.00% compliance with the USCCB Guidelines. The compliance ratio for the portfolios may change marginally due to fluctuations in the prices of individual assets and new additions to the USCCB noncompliance list. TWM monitors the compliance ratio for all assets of the funds twice per month to help assure that the portfolio stays at, or above, the 97.00% level.

At the end of the quarter, the Equity Fund compliance level was 97.22%. The compliance ratio at quarter end for the Fixed Income Fund was 99.9%. A hypothetical balanced portfolio of 60% stocks and 40% fixed income therefore would have resulted in compliance of approximately 98.29%.

**CFNEK Equity Fund (EF)**

During the third quarter a variety of adjustments were made to the stock strategies, primarily for allocation reasons. The iShares Russell 1000 Growth and DFA Emerging Markets Equity funds were reduced with proceeds shifting to the iShares MSCI EAFE Growth, DFA International Social Core and JPMorgan Emerging Markets Equity funds. The latter was a new position for the portfolio.

An end of the third quarter "look-through" that classifies all the stock positions for the total Equity portfolio reflected the following allocation: U.S. Large Cap 60.1%; U.S. Mid/Small-Cap 11.5%; International Large-Cap 13.0%; International Mid/Small-Cap 5.5%; Emerging Markets 7.4%. The remaining approximately 2.5% was in Cash Equivalents.

The total Equity Fund performance for the third quarter was 8.58%. The blended benchmark return for this portfolio was 8.32%. Year-to-date, the Fund has basically been flat, producing a return of -.01% versus 2.09% for the blended index. For the 37 months of TWM measured performance, the Equity Fund's annualized return was 7.30% (7.63% excluding alternatives) vs. 9.02% for the blended benchmark. The benchmark for the Equity Fund consists of 70% Russell 3000 and 30% MSCI All Country World Index ex-US, (ACWI ex US) which closely reflects the current make-up of the portfolio. All TWM performance numbers are net of fees.

In general, although the portfolio outperformed its benchmark during the quarter, the longer term shortfall has been primarily due to the portfolio's historical slight tilt toward value oriented equities (which have underperformed their growth style brethren for an extended period, including 2020) and the corresponding circumstances in general in regard to the DFA socially responsible solutions, which tend to be smaller stock and somewhat value oriented.

**CFNEK Fixed Fund (FF)**

The total return of the Fixed Income Fund during the third quarter was up slightly at .55% vs. .62% for the Barclays Intermediate Government/Credit Index. Year-to-date, the return was 4.20% versus 5.92% for the benchmark. During the 37 months of TWM management, the annualized return was 2.65% versus 4.16% for the index. All TWM performance numbers are net of fees.

Due primarily to a shortened duration of approximately 3.3 years for the Fund, mostly geared to protect the portfolio from a potential rising rate environment, versus that of the benchmark's 4.1 years, the portfolio was competitive, but slightly underperformed for the quarter. The rate on the ten-year U.S. Treasury Note closed at .69% at the end of September; the rate was .66% on June 30 and 1.92% at the close of 2019. While the rate on the 10-year rose a bit during the quarter, the two-year's slightly declined from .15% to .13%, versus 1.57% on December 31, 2019.

Other than reinvestment of cash receipts, including proceeds from maturing and called bonds, there were no material, tactical adjustments to this Fund over the quarter.

**General Market Comments**

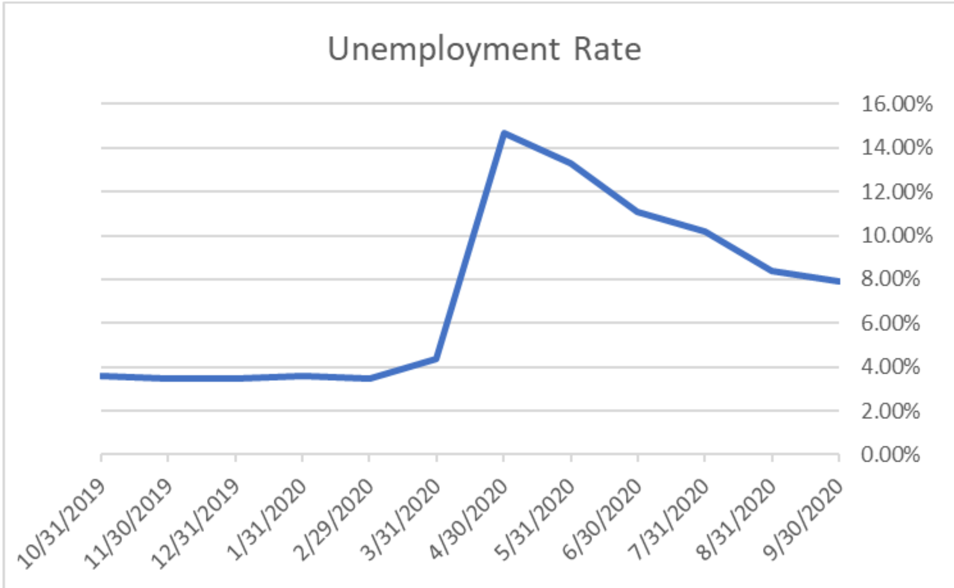
After a tumultuous period earlier in the year, the third quarter saw the financial markets, equities in particular, continue to bounce back with remarkable resilience. The primary storyline remained the ongoing battle with COVID-19, not only from a financial perspective in light of the previously mandated economic and social shutdown, but also certainly from a health related one as well. That being said, during the third quarter, the following were some key coronavirus specific related items:

- Testing, not only increasing in quantity, but also the production of additional, more expeditious mechanisms.
- Numerous vaccine candidates progressed at an unprecedented speed.
- Treatment options evolved and increased in number, including the use of a drug from Gilead Sciences (Remdesivir), the steroid Dexamethasone, antibody cocktails and the Mayo Clinic's experimental use of plasma containing coronavirus antibodies.
- Post initial re-openings, including schools of various levels across the country, case numbers spiked nationally. However, the level of severe cases, including mortalities, thankfully, did not seem to follow suit as the average age of those infected continued its downward trajectory.
- In late September, the governor of Florida announced the lifting of all restrictions on businesses statewide that had been imposed to control the spread of the virus.
- Across the globe, the concern is that a significant "second wave", a mutation of the virus and/or the impact of the normal flu season, will cause havoc before a well-tested, reliable vaccine becomes available, presumably initially to health care professionals and subsequently to the general community.

From a broader perspective and in addition to COVID, the markets seemed to be engaged in a tug of war, particularly toward the end of the quarter, in light of the ongoing politically charged environment preceding the upcoming U.S election and the Supreme Court vacancy due to the passing of Justice Ginsburg.  The prospect that the Presidential election results may be delayed due primarily to the expected volume of mail-in ballots has added some "spice" to these items. Together, these facets have likely had an impact on the potential passing of the next fiscal stabilization package as well.

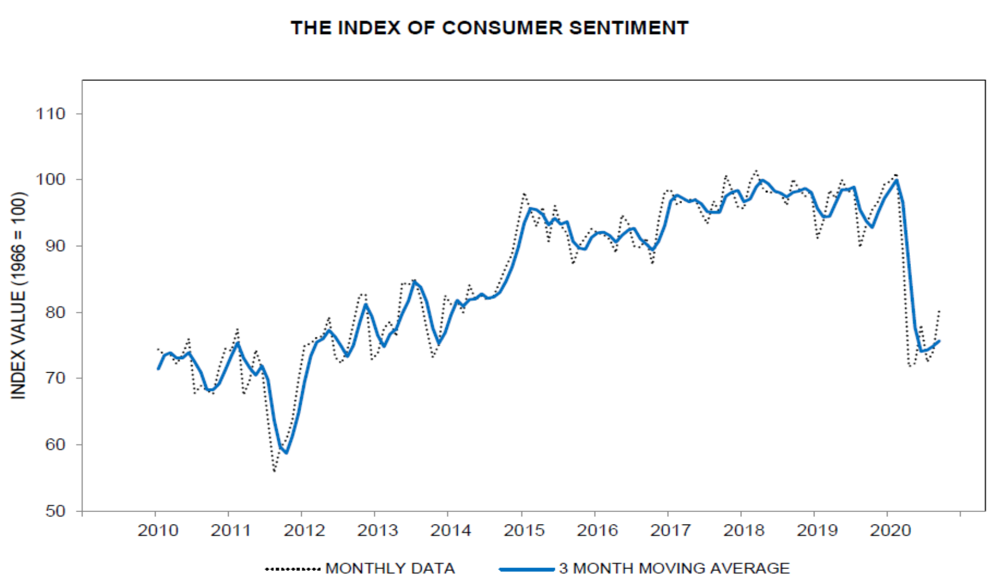
On the economic front:

- The third quarter saw a material bounce in economic activity, although this pace is widely expected to slow in the fourth quarter; largely due to the virus and politics as mentioned above.
- The "modern economy" has shown signs it can still be relatively robust due to technology.
- The small business sector continues to struggle with serious damage inflicted by the earlier, widespread lockdowns.
- Housing has been a particular source of strength (including sales of new and existing homes) as low interest rates on mortgages have attracted many.
- In general, the demand for goods has continued to outpace that of services.
- As shown in the graph below, the U.S. Unemployment Rate has fallen significantly from its April high which exceeded the 14% level, but remains materially above the sub-4% status achieved prior to the outbreak of the pandemic.  It should be noted that at least some of this decline may have been driven by a drop in labor force participation.
- In the short-term, the virus and the world's collective approach to it are considered deflationary.  However, the volume of the policy actions may in the end result in inflationary pressures over the next decade.
- Trade tensions with China resurfaced, but in a turnaround from earlier in the year, seemed to take a back seat to other issues.




Source: Fred.stlouisfed.org

As we have mentioned in previous publications, as we move forward, the unemployment question has broad impacts on a variety of fronts, including all-important Consumer Sentiment. It has been well documented that the U.S. consumer has been the backbone of our domestic economy, encompassing nearly 70% of Gross Domestic Product (GDP). Although confidence and spending patterns took significant hits during the aforementioned shutdown, activity has increased as communities across the country have engaged in reopening phases. The higher the level of health safety, the greater likelihood of increased tailwinds on this front. Although the level of Consumer Sentiment, as seen in the graph below, has bounced off its recent lows, it still has quite a way to go to reach its early 2020 levels. Weakness remains present in TSA traveler traffic (i.e. airlines at -70%), U.S. seated restaurant diners, which has declined by over 40% (and one wonders if this will worsen during the winter with the lack of outdoor seating) and hotel occupancy at -32%. Recreational vehicle sales have consequently been robust by the way.



Source: Surveys of Consumers University of Michigan: sca.isr.umich.edu/charts.html

Suffice it to say, it would be an understatement to comment that a lot has transpired over the first three quarters of the year and it would once again seem safe to say there will be more peaks and valleys ahead. Although we are still not yet “out of the woods” from an economic standpoint, with the foundation the Federal Reserve and the U.S. government built to bridge the COVID-19 related economic gap (and continue to do so), we believe a return to as normal an environment as reasonably possible still depends on the trajectory of COVID-19 and medical breakthroughs needed to keep it as minimized as possible.