Market Commentary

New Covenant Funds

May 2020

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- Global financial markets continued their sharp rallies in May amid loosening lockdowns, promising progress toward COVID-19 vaccine development, and the ongoing extraordinary support of central banks.
- Legislation passed the Congress in early June that would adjust Paycheck Protection Program rules to extend the period during which companies can spend loan proceeds and remain eligible for loan forgiveness, as well as allow a lower minimum share of loan proceeds to go toward covering payroll.
- We remain mindful of the known risks inherent to investing in the capital markets as well as the potential for devastating surprises such as the COVID-19 pandemic that struck in early 2020 and remains a threat today.

Economic Backdrop

Global financial markets continued their sharp rallies in May, albeit short of their remarkable April rebounds. The "risk-on" sentiment came amid a push by local governments to slowly reverse lockdowns of non-essential economic activity; the promising news of progress made in the race to develop COVID-19 vaccines; and the sustained extraordinary support of central banks.

Equities around much of the world experienced a choppy first half of May that ultimately gave way to a strong second half for the month. However, mainland Chinese and Hong Kong stocks were outliers; both came under pressure as the month progressed, with the island territory finishing the period with a steep loss. U.S. and European stocks generated solid monthly performance, while U.K. stocks delivered more subdued gains.

The blended earnings of S&P 500 Index constituents declined by 14.6% during first-quarter 2020 from a year earlier (based on 97% of companies that had reported results) putting the Index on track for its deepest year-over-year decline since third-quarter 2009. U.S. investment-grade corporate-bond issuance continued an unprecedented recovery from its standstill in March, racing past $1 trillion in year-to-date issuance in late May; the $1 trillion issuance milestone wasn't broken in 2019 until November.

Government-bond rates followed divergent paths from country to country. Short- and long-term U.S. Treasury rates increased as intermediate-term rates declined for the month. Rates mostly declined for U.K. gilts, yet increased for those with the longest maturities, while they increased across all maturities for eurozone government-bonds.

In the U.S., the total recorded number of COVID-19-related deaths surpassed 100,000 in late May—out of about 350,000 total worldwide. President Donald Trump's administration imposed travel restrictions on Brazil amid the South American nation's struggle to contain the outbreak; the federal government also prolonged its mandate for land-border closures with Canada and Mexico by one month, now effective through June 22. State-by-state responses continued to vary widely, with some local governments facing challenges to the legality of their orders: Wisconsin's state supreme court overturned the governor's stay-at-home order in mid-May; the U.S. Supreme Court rejected a California church's challenge to the legality of placing restrictions on gathering in places of worship—thereby validating California's state government to enforce such restrictions.

U.S. legislators continued to explore ways to improve the Paycheck Protection Program—a government loan designed to incentivize small businesses to keep workers on the payroll—legislation passed the Congress in early June that would extend the period during which companies can spend loan proceeds and remain eligible for loan forgiveness, as well as allow a lower minimum share of loan proceeds to go toward covering payroll. Toward the end of May, the House of Representatives also passed an additional $3 trillion in COVID-19 relief funds, but the legislation was held up in the Senate with unclear prospects for approval.

The U.K. COVID-19-related death toll eclipsed that of Italy in early May, reaching the highest number of losses in Europe (although Italy lost a greater percentage of its smaller population). U.K. Chancellor of the Exchequer Rishi Sunak announced his intention to extend the government's mortgage-payment holiday beyond June as its initial three-month timeframe approached. As of mid-May, U.K. banks had granted these repayment holiday terms to 1.7 million homeowners.

Italy provided reason to celebrate halfway through the month as its number of new COVID-19 cases per day fell below 100 for the first time since March. The peninsular nation announced plans to begin reopening borders in early June. Prime Minister Giuseppe Conte proposed a €55 billion relief package intended to freeze corporate taxes for many businesses; provide forgivable grants of up to €40,000 for small businesses and emergency incomes of up to €800 for struggling families; extended unemployment payments; and offer funding for healthcare, tourism, research and agriculture, among others initiatives. The Italian government's announcement preceded the mid-May proposal by the European Commission for nearly €2 trillion across the EU, with €750 billion devoted to recovery efforts and another €1.1 trillion to budgets over the next seven years.

The National People's Congress in China concluded the month with its approval of a resolution to impose new national-security laws on Hong Kong amid ongoing anti-Beijing protests, marking a significant dilution of the "one country, two systems" governance ethos that has defined the relationship since the U.K.'s handoff of Hong Kong to China in 1997.

Several governments around the world condemned this development and began to explore concrete responses. U.K. Prime Minister Boris Johnson said Britain was considering a path to citizenship and relocation for British Nationals (Overseas) (a class of British nationality extended to Hong Kong residents prior to the 1997 handover). Meanwhile, the U.S. began examining Hong Kong's special territorial exemptions and evaluating multiple avenues for putting economic pressure on China—including sanctioning the mainland Chinese financial sector and imposing limitations on technology sharing by adding dozens of Chinese entities to trade blacklists.

The increasingly tense U.S.-China relationship was further stressed in May by a U.S. push for more transparency in the ownership of U.S.-listed Chinese companies and the U.S. government's barring of certain Chinese holdings from its retirement plans. Canada's relationship with China was also strained during the month after a Canadian judge ruled in favor of a U.S. petition to extradite a Chinese telecommunications executive. China, for its part, imposed an 80% tariff on all barley imported from Australia over the next five years in an apparent response to the Australian government's call for an independent inquiry into the origins of COVID-19.

Index Data (May 2020)

- The Dow Jones Industrial Average rallied by 4.66%.
- The S&P 500 Index increased by 4.76%.
- The NASDAQ Composite Index advanced by 6.89%.
- The MSCI ACWI (Net), used to gauge global equity performance, accelerated by 4.35%.
- The Bloomberg Barclays Global Aggregate Index, which represents global bond markets, improved by 0.44%.
- The Chicago Board Options Exchange Volatility Index, a measure of implied volatility in the S&P 500 Index also known as the "fear index", fell from 34.15 to 27.51.
- WTI Cushing crude oil prices, a key indicator of movements in the oil market, increased from $18.84 a barrel at the end of April to $35.49 on the last day in May.
- The U.S. dollar ended May at $1.23 against sterling, $1.11 versus the euro and at 107.83 yen.

Portfolio Review

The Growth Fund's ESG screens led to poor stock selection in the information technology, real estate and health care sectors in May.

The Income Fund's overweight to corporates helped as spreads tightened during the month. Selection within industrials and banks further contributed. An overweight to agency mortgage-backed securities (MBS) added; selection within specified pools provided an additional boost. The overweight to non-agency MBS, which continued to rebound after March's liquidity-induced selloff, contributed. Overweights to asset-based securities (ABS) and higher-quality commercial MBS (CMBS) also helped. The Income Fund's overweight to the long-term segment of the U.S. Treasury yield curve detracted as 30-year U.S. Treasury yields rose during the month. Western Asset Management gained on an overweight to credit sectors as spreads tightened in May. Overweights to energy and financials helped. An overweight to agency and non-agency MBS contributed. Duration was slightly long versus the benchmark and an overweight to the long-term segment of the yield curve detracted modestly. Income Research & Management gained on an overweight to corporates (industrials and financials). An overweight to higher-quality ABS helped, as did an underweight to U.S. Treasurys as all spread sectors outperformed government bonds. Selection within specified mortgage pools further contributed.

Manager Positioning and Opportunities

The Growth Fund employs a passive strategy designed to track the performance of the Russell 3000 Index, which represents the largest 3,000 U.S. companies and approximately 98% of the investable U.S. equity market, subject to such variation as may arise as a result of implementation of the social witness principles of the General Assembly of the Presbyterian Church (U.S.A.).

During the month, Western reduced the overweight to agency MBS. The Income Fund's duration positioning ended the month neutral to its benchmark, but remained overweight the long-term segment of the U.S. Treasury yield curve. Duration is a measure of risk in bond investing and indicates how price-sensitive a bond is to changes in interest rates. A long (overweight) duration stance indicates the portfolio duration is higher than that of the benchmark whereas a short (underweight) duration stance indicates a lower duration. Duration is measured in years and securities with longer durations are more sensitive to interest-rate changes. With yields near historic lows, the Fund's managers are likely to stay close to neutral until volatility subsides. It was overweight spread sectors in an effort to maintain liquidity and will likely remain so, while adjusting duration and yield-curve positioning as the market changes. The Income Fund's managers are taking a "follow the Federal Reserve" approach in maintaining exposure to investment-grade credit and agency MBS, as both are the initial two areas of support from the central bank.

Financial Glossary

Futures: Futures are a type of derivative contract obligating the buyer to purchase an asset (or the seller to sell an asset) at a predetermined future date and price.

Paycheck Protection Program (PPP): The Paycheck Protection Program is a loan offer by the U.S. government's Small Business Administration (SBA) designed to provide a direct incentive for small businesses to keep their workers on the payroll. SBA will forgive loans if all employees are kept on the payroll for eight weeks and the money is used for payroll, rent, mortgage interest, or utilities.

Spot trade: A spot trade is the purchase or sale of a foreign currency or commodity for immediate or "on the spot" delivery.

Index Glossary

The S&P 500 Index is an unmanaged, market-capitalization weighted index that consists of the 500 largest publicly-traded U.S. companies and is considered representative of the broad U.S. stock market.

The MSCI All Country World Index is a market-capitalization-weighted index composed of over 2,000 companies and is representative of the market structure of 48 developed and emerging-market countries in North and South America, Europe, Africa and the Pacific Rim. The Index is calculated with net dividends reinvested in U.S. dollars.

The Bloomberg Barclays Global Aggregate Bond Index an unmanaged market-capitalization-weighted benchmark, tracks the performance of investment-grade fixed-income securities denominated in 13 currencies. The Index reflects reinvestment of all distributions and changes in market prices.

The Chicago Board Options Exchange Volatility Index (VIX) tracks the expected volatility in the S&P 500 Index over the next 30 days. A higher number indicates greater volatility.

The Russell 3000 Index includes 3000 of the largest U.S. equity securities based on market cap and current index membership; it is used to measure the activity of the U.S. equity market.

The Bloomberg Barclays Intermediate U.S. Aggregate Bond Index is an unmanaged benchmark index composed of U.S. securities in Treasury, government-related, corporate, and securitized sectors with remaining maturities of less than 10 years.

The Dow Jones Industrial Average is a price-weighted average of 30 large, publicly owned companies based in the U.S. and traded on the New York Stock Exchange and the NASDAQ.

The NASDAQ Composite is a market capitalization-weighted index of approximately 3,000 common stocks listed on the Nasdaq stock exchange, including American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks, as well as limited partnership interests. The Nasdaq Composite is not limited to companies that have U.S. headquarters.

Important Information

The performance data quoted represents past performance. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. For performance data current to the most recent month end, please call 1-877-835-4531.

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To determine if the Funds are an appropriate investment for you, carefully consider the investment objectives, risk factors, charges and expenses before investing. This and other information can be found in the Funds’ full and summary prospectuses, which can be obtained by calling 1-877-835-4531. Read them carefully before investing.

There are risks involved with investing, including loss of principal. Current and future portfolio holdings are subject to risks as well. International investments may involve risk of capital loss from unfavorable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations. Narrowly focused investments and smaller companies typically exhibit higher volatility. Bonds and bond funds will decrease in value as interest rates rise. High-yield bonds involve greater risks of default or downgrade and are more volatile than investment-grade securities, due to the speculative nature of their investments. Emerging markets involve heightened risks related to the same factors as well as increased volatility and lower trading volume. Mortgage-backed securities are affected by, among other things, interest rate changes and the possibility of prepayment of the underlying mortgage loans. Mortgage backed securities are also subject to the risk that underlying borrowers will be unable to meet their obligations.

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- **Not FDIC Insured**
- **No Bank Guarantee**
- **May Lose Value**