Market Commentary

New Covenant Funds

Fourth Quarter 2021

SEI New ways. New answers.®

- The fourth quarter began in the shadow of September's selloff. Equities vaulted higher through mid-November before managing a choppy climb to finish the year.
- U.S. stocks were the top-performing major market for the fourth quarter and the full calendar year. The U.K. and Europe also performed quite well over both time frames, while China was down steeply for the quarter and year.
- In our view, ultra-low interest rates in the face of higher inflation and above-average growth may force central banks to adopt more aggressive policies than market participants currently envision.

Economic Backdrop

Sky-high COVID-19 cases, a volatile equity-market rally, and worry over rising interest rates can describe both the first and last weeks of 2021. An obvious difference between those two timeframes is that the prospect of widespread vaccination became reality, dealing a sharp blow to the severity of illness among the infected. A towering nine billion vaccine doses were administered worldwide through the end of 2021, rendering roughly 49% of the global population fully vaccinated.

Turning to financial markets, the fourth quarter began in the shadow of September's selloff, which was the most extended shakeout of 2021. After recovering in October, equities vaulted higher through mid-November before unrestrained inflation, tightening central-bank policy and the emergence of the Omicron variant combined for a choppy climb to finish the year.

U.S. stocks were the top-performing major market for the fourth quarter and the full calendar year. The U.K. and Europe also performed quite well over both time frames. Hong Kong and Japan had significant losses in the three-month period; Japan was up modestly in 2021, while Hong Kong had a full-year decline. Brazil and China were down steeply for the quarter and the year, with China delivering the deepest loss among major markets in 2021.

Across the U.S., U.K. and eurozone, short-to-medium-term government bond rates increased during the fourth quarter, while long-term rates declined, resulting in flatter yield curves.

Within fixed income, fourth-quarter performance mirrored the full year: inflation-indexed bonds were the top performers, followed by high yield. Most other sectors were mildly negative given the impact of rising rates, but global bonds were down by more due to currency effects. Local-currency emerging-market debt had the steepest losses for the quarter and year.

The U.S. dollar continued to strengthen against most other currencies during the fourth quarter, capping off a 6.7% full-year increase according to the U.S. Dollar Index (DXY). Commodity prices were dealt a minor setback in the fourth quarter after a steep ascent for the first nine months of 2021. The Bloomberg Commodity Index declined 1.6% during the quarter but gained 21.1% for the full year.

The U.S. Congress voted to raise the debt ceiling (that is, the federal government's borrowing limit) twice during the fourth quarter—first with an October stopgap hike of $480 billion, and then with a December increase of $2.5 trillion—which is expected to cover spending through early 2023.

President Joe Biden signed the Infrastructure Investment and Jobs Act—a multi-year infrastructure funding bill—into law during November. The initiative appropriated $1.2 trillion (including $550 billion above baseline spending), with nearly $300 billion of new spending to fund transportation projects over the next decade, another $65 billion apiece dedicated to broadband internet and power grid projects, and $55 billion reserved for water infrastructure.

The U.K. government's autumn budget traded improved benefits for tax increases. It proposed a reduction in the universal credit taper rate for low-income workers (from 63% to 55%, meaning that the credit will phase out more slowly) and an annual £500 increase in work allowances. Brick-and-mortar stores will also see more relief via a temporary 50% cut in business rates and no increase in 2022. On the revenue side, a 1.25% bump in national insurance contributions was scheduled to begin in the spring, and a long-telegraphed increase in the corporation tax remained set for 2023.

Germany's new governing coalition came together in late November. The center-left Social Democrats (SPD) secured 25.7% of ballots cast in the September election, while the progressive environmentalist Greens won 14.8% and pro-business Free Democrats (FDP) received 11.5% of the votes. As of December, SPD leader Olaf Scholz heads the government as chancellor, while FDP leader Christian Lindner serves as finance minister.

The coalition has coalesced around an ambitious series of climate-centric policy pledges, including new commercial and residential construction that host solar-power production capabilities; additional support for seaborne wind farms; and a targeted 15 million electric vehicles in service by 2030 along with the necessary charging infrastructure. The German housing market is also set to benefit from the coalition's plan to build 400,000 new apartments per year, with one-quarter of the project financed by government funds. However, questions have been raised about how the government will fund its goals given that Germany's "debt brake" will be re-instated in 2023 (limiting government borrowing to 0.35% of GDP) and that the FDP extracted a commitment to refrain from imposing new or increased taxes (in order to join the coalition).

In China, while Evergrande dominated concerns about the viability of real estate companies earlier in 2021, Fantasia Holdings Group—a much smaller developer—defaulted on a $206 million bond payment at the beginning of October. Evergrande held out until December before defaulting along with Kaisa, another large developer. The Chinese government appeared to support a plan for Evergrande to negotiate reduced repayments on its offshore bonds with international creditors.

Following its annual Central Economic Work Conference in December, Beijing stated that its top priority for 2022 would center on economic stabilization with a heavy focus on financial restraint.

Central Banks

- The Federal Open Market Committee (FOMC) shared in early-November a timeline to reduce its asset-purchase program by June. Yet by the end of November, Federal Reserve (Fed) Chair Jerome Powell expressed in testimony to the Congress that high inflation could drive the FOMC to reduce asset purchases at an accelerated pace. Indeed, following its mid-December meeting, the FOMC indicated that it intends to conclude asset purchases by March; its latest Summary of Economic Projections points to a commencement of rate hikes in 2022. Powell was nominated to serve a second term as Fed Chair by President Biden during November.

- The Bank of England (BOE) became the first major central bank to increase rates since the pandemic began; its Monetary Policy Committee (MPC) voted 8-to-1 in favor of raising the bank rate by 15 basis points (bps) to 0.25% in mid-December. The MPC's inflation forecast for spring 2022 jumped to 6% at its December meeting from 5% at its prior monthly meeting.

- Following its mid-December meeting, the European Central Bank (ECB) announced that its Pandemic Emergency Purchase Programme (PEPP) would conclude by March 2022. However, the central bank said it would rely on its long-standing Asset Purchase Programme to provide monetary support when needed, and does not anticipate an increase in benchmark rates during 2022. The ECB raised its inflation projection to 3.2% for 2022 and 1.8% thereafter as actual inflation hit a record 4.9% year over year in November.

- The Bank of Japan (BOJ) announced at its mid-December meeting that it would revert purchases of corporate bonds and commercial paper to pre-pandemic levels beginning in April. The central bank kept its rate targets on hold, however, with its short-term interest rate at -0.1% and its 10-year government bond yield target near 0%.

- The People's Bank of China (PBOC) lowered its reserve requirement ratio—which dictates the amount of money banks are required to hold in reserves—by 50 bps to 8.4% in early December, freeing up nearly $188 billion for lending activity. Later in the month, the PBOC cut its one-year loan prime rate by 5 bps to 3.8%.

Index Data for Fourth Quarter 2021

- The Dow Jones Industrial Average surged by 7.87%.
- The S&P 500 Index lifted by 11.03%.
- The NASDAQ Composite Index jumped by 8.45%.
- The MSCI ACWI (Net), used to gauge global equity performance, increased by 6.68%.
- The Bloomberg Barclays Global Aggregate Index, which represents global bond markets, moderated by 0.67%.
- The Chicago Board Options Exchange Volatility Index (VIX), a measure of implied volatility in the S&P 500 Index that is also known as the "fear index," fell, moving from 23.1 to 17.2.
- WTI Cushing crude-oil prices, a key indicator of movements in the oil market, gained from $75.03 a barrel on the last day in September to $75.21 on December 31.
- The U.S. dollar moved to $1.35 versus sterling, $1.14 against the euro and 115.10 yen.

Portfolio Review

Results in the Growth Fund were positive during the quarter. The environmental, social and governance screen (ESG) led to a favorable overweight to information technology stocks. Strong stock selection within information technology, communication services and health care enhanced returns. The Growth Fund's underweight to low-quality stocks contributed.

The Income Fund suffered from an overweight to corporates and negative security selection. Other detractors included an overweight to asset-backed securities (ABS); a higher-quality bias within commercial mortgage-backed securities (CMBS); and negative security selection within financials and industrials. Contributors included an underweight to agency mortgage-backed securities (MBS); an overweight to 30-year bonds; and security selection within energy. Western Asset Management suffered from overweights to ABS and corporate bonds. Western's allocation to dollar denominated sovereign bonds in Latin America also dragged returns. Selection within CMBS and an underweight to agency MBS boosted performance. Income Research & Management suffered from overweights to corporates, ABS and CMBS. Contributors included an underweight to agency mortgage-backed securities. IRM's security selection within energy was favorable.

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.).

Fixed-income markets have signaled improved growth prospects on the tail of higher interest rates in addition to increased stimulus and infrastructure spending that should result in higher deficits and more U.S. Treasury issuance. Inflation expectations are higher in the short term than in the long term. Inflation expectations have risen above the Fed's target and rest at their highest levels in over a decade. We share the Federal Reserve's sentiment that higher short-term inflation will likely be transitory. Securitized sectors remain attractive in our view, especially agency mortgage-backed securities. The Income Fund's duration positioning began the quarter slightly neutral the benchmark, but ended the period slightly underweight. 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 corporate bonds as managers viewed them as a better relative value despite higher prices than last year.
Within the long-term overweight to securitized sectors, commercial MBS and ABS were the largest allocations while the agency MBS allocation was close to that of the benchmark. An overweight to off-benchmark non-agency MBS remained as the sector continued to trade at attractive spreads.

The New Covenant Balanced Growth Fund invests about 60% of its assets in the Growth Fund and 40% in the Income Fund. The New Covenant Balanced Income Fund invests about 35% of its assets in the Growth Fund and about 65% in the Income Fund.

Financial Glossary:

Asset Purchase Programme (APP): The ECB's APP is part of a package of non-standard monetary policy measures that also includes targeted longer-term refinancing operations, and which was initiated in mid-2014 to support the monetary policy transmission mechanism and provide the amount of policy accommodation needed to ensure price stability.

Duration: Duration is a measure of the sensitivity of the price of a bond or other debt instrument to a change in interest rates.

Federal-funds rate: The federal-funds rate is the interest rate at which a depository institution lends immediately-available funds (balances at the U.S. Federal Reserve) to another depository institution overnight in the U.S.

Pandemic Emergency Purchase Programme (PEPP): PEPP is a temporary asset purchase programme of private and public sector securities established by the ECB to counter the risks to monetary policy transmission and the outlook for the euro area posed by the COVID-19 outbreak.

Universal Credit Taper Rate: The taper rate is the amount of Universal Credit payments that claimants lose, as they work and earn more above a certain threshold - known as the work allowance.

Index Glossary:

The Bloomberg Commodity Index is composed of futures contracts and reflects the returns on a fully collateralized investment in the Index. This combines the returns of the Index with the returns on cash collateral invested in 13-week (3-month) U.S. Treasury bills

The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and NASDAQ.

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 NASDAQ Composite Index is an unmanaged, market-capitalization weighted index that consists of all securities listed on the NASDAQ exchange. It is often used to gauge performance of global technology stocks.

The MSCI All Country World Index (MSCI ACWI) 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 Global Aggregate Bond Index (formerly Lehman Brothers Global Aggregate 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.

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.

This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice regarding the Funds or any stock in particular, nor should it be construed as a recommendation to purchase or sell a security, including futures contracts. There is no assurance as of the date of this material that the securities mentioned remain in or out of New Covenant Funds.

For those New Covenant Funds which employ the “manager of managers” structure, SEI Investments Management Corporation (SIMC) has ultimate responsibility for the investment performance of the Funds due to its responsibility to oversee the sub-advisers and recommend their hiring, termination and replacement. SIMC is the adviser to the New Covenant Funds, which are distributed by SEI Investments Distribution Co. (SIDCO). SIMC and SIDCO are wholly owned subsidiaries of SEI Investments Company.

To determine if the Fund(s) are an appropriate investment for you, carefully consider the investment objectives, risk factors and charges and expenses before investing. This and other information can be found in the Fund's prospectus, and if available, the summary prospectus, which can be obtained by calling 1-877-835-4531. Read the prospectus 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. Emerging markets involve heightened risks related to the same factors as well as increased volatility and lower trading volume. 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. 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.

Diversification may not protect against market risk. There is no assurance the objectives discussed will be met. Past performance does not guarantee future results Index returns are for illustrative purposes only and do not represent actual portfolio performance. Index returns do not reflect any management fees, transaction costs or expenses. One cannot invest directly in an index.

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