Market Commentary

New Covenant Funds

March 2022

- Global equities delivered their poorest quarterly performance since early 2020. Global bonds fared worse, tumbling by the most since late 2016. By contrast, commodities had their strongest quarter in at least 30 years.
- U.K. stocks earned a positive return for the quarter, while the U.S., Japan and Europe sunk into negative territory. Chinese equities had steep double-digit losses.
- One of the greatest mistakes an investor can commit is to panic and make indiscriminate changes for fear of losing money. In periods of unusual stress, a clear philosophy and process can help guide calm, rational, long-term decision making.

Economic Backdrop

Investors faced inhospitable conditions on multiple fronts during the first three months of 2022. Global equities delivered their poorest quarterly performance since early 2020—bottoming in mid-March before mounting a sharp partial recovery. Global bonds fared worse, tumbling by the most since late 2016.

U.K. stocks earned a positive return during the quarter, outpacing other major markets. Hong Kong was slightly negative, while the U.S., Japan and Europe had steeper losses.

Mainland Chinese equities bounced higher after plummeting from mid-February to mid-March, but still finished the quarter with double-digit losses. The selloff in Chinese equities was most severe in technology companies, forcing Vice Premier Liu He—China's top economic advisor—to pledge that the government would take a "standardised, transparent and predictable" approach to the regulation of technology; this comes after more than a year of interventions. Beijing also made broader overtures to soothe investors, including prioritising the stability of capital markets, supporting overseas stock listings, and pledging to manage the risks associated with solvency issues plaguing property developers.

Meanwhile, with commodities markets having been the epicentre of the financial fallout from Russia's attacks on Ukraine, commodities had their strongest quarter in at least 30 years. The price of natural gas spiked by more than 50%, while West-Texas Intermediate and Brent crude-oil prices both climbed by over 30%. The price of wheat also increased by more than 30%. Commodity-producing nations, therefore, were the first quarter's big winners, led at a distance by Latin American equities' double-digit gains.

On the other side of the spectrum was Russia—the greatest loser by a wide margin—as its aggression against Ukraine opened the door to an expansive set of coordinated economic restrictions, imposed rapidly and with a high degree of uniformity across Western powers. The country's banishment from global financial systems translated into massive declines in the value of Russian securities.

Government bond rates increased across maturities in the U.S., U.K., and eurozone during the first quarter. Shorter-term rates climbed by more than longer-term rates, leading to flatter yield curves across the three jurisdictions. An inversion of U.S. Treasury rates that began at the long end of the yield curve in late 2021 broadened in March to include the 3-year/10-year segment of the curve as well.

Bonds delivered an array of negative performances as interest rates climbed (yields and prices have an inverse relationship). Inflation-indexed securities had relatively mild declines, while emerging-market debt and investment-grade corporates tumbled dramatically. The longest-term government bonds in advanced economies posted double-digit losses.

In the immediate aftermath of the invasion, the European Commission, France, Germany, Italy, the U.K., Canada, and the U.S. committed to taking several actions including removing Russian banks from the SWIFT (Society for Worldwide Interbank Financial Telecommunication) messaging system for financial payments; blocking the Russian Central Bank from deploying its international reserves; limiting the sale of citizenship to wealthy Russians; and launching a transatlantic task force to freeze the assets of sanctioned entities.

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The imposition of these coordinated sanctions has effectively blocked Russian entities from trade in major foreign currencies. The Russian Central Bank was forced to increase its benchmark rate by a considerable 10.5%, to 20.0%; offer unlimited liquidity support to banks as they faced runs; raise capital controls on exporters and residents; and shutter its financial markets.

By mid-March, the EU had instituted a broad ban on investments in Russia as well as exports to and imports from the country (although imports of Russian metals and energy are still permitted). Russian state-controlled companies across an array of industries are blocked from trading with the EU, while prominent Russian individuals (including business executives, media personalities and oligarchs) faced asset freezes and travel bans.

The U.S. went a step further in banning all new purchases of Russian energy imports, allowing a 45-day wind-down period for existing agreements.

Also in mid-March, Russia legalised the nationalisation of more than 500 airplanes leased to Russian airlines by Western companies. This came after an early-March move to restrict the export of more than 200 products and raw materials until the end of 2022; although its chief commodity exports were not included.

More recently, Russia began to demand ruble payments for gas exports to Europe instead of accepting U.S. dollars or euros, sending European gas prices soaring. The Group of 7 (G7) explicitly rejected the Russian demand in late March. At the end of the quarter, Russia's Transneft—the largest oil pipeline network in the world—alerted local oil-producing companies that it would cap acceptance of oil that had not already been sold as storage capacity was full.

The European Commission announced in mid-March that the electricity grids of Ukraine and Moldova were now synchronised with that of Continental Europe rather than with Russia; this was done in an effort to help the two countries reduce their dependence on Russia and improve their electricity system reliability.

Central Banks

- The Federal Open Market Committee (FOMC) voted to increase the federal-funds rate by 0.25% in mid-March—its first rate hike since December 2018—after making a final $30 billion round of new asset purchases. The central bank had released a statement in January outlining principles for reducing the size of its balance sheet and stated in March that it "expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities at a coming meeting." Its latest quarterly Summary of Economic Projections, released in conjunction with its March policy statement, showed a decline in the median real gross domestic product (GDP) projection for 2022 (to 2.8% from 4.0% in December) as well as an increase in broad inflation expectations for 2022 (to 4.3% from 2.6%) and smaller increases for anticipated inflation in 2023 and 2024. The median outlook for the federal-funds rate increased to 1.9% for 2022 (from 0.9% in December) and 2.8% for 2023 (from 1.6%).

- The European Central Bank (ECB) announced plans following its mid-March meeting to conclude its Asset Purchase Programme in the third quarter after decreasing net purchases from €40 billion in April to €30 billion in May, and then to €20 billion in June. The final net purchases under the Pandemic Emergency Purchase Programme (PEPP) concluded during the first quarter. Following Russia's invasion of Ukraine, ECB President Christine Lagarde pledged that the ECB "will ensure smooth liquidity conditions and access of citizens to cash," and that it "stands ready to take whatever action is needed to fulfil its responsibilities to ensure price stability and financial stability in the euro area."

- The Bank of England's (BoE) Monetary Policy Committee (MPC) issued three consecutive rate hikes—first in December 2021, then in early February, and finally in mid-March—bringing the bank rate to 0.75%. MPC members voted unanimously in February to begin reducing the size of the BoE's balance sheet by ceasing to re-invest proceeds from its asset-purchase program and through corporate bond sales. The wind-down cannot be completed any earlier than toward the end of 2023.

- The Bank of Japan's (BOJ) policy orientation was unchanged following its mid-January and late-March meetings, with its short-term interest rate at -0.1% and the 10-year government-bond-yield target near 0%, as the country's inflation pressures remained subdued relative to other major developed economies. The global rise in long-term bond yields compelled the BOJ to make standing offers of unlimited 5-to-10-year Japanese government bond (JGB) purchases as the 10-year yield touched 0.25% in late March, reaching a six-year high. Previously, the BOJ announced that it would revert purchases of corporate bonds and commercial paper to pre-pandemic levels beginning in April.

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Index Data (March 2022)

- The Dow Jones Industrial Average diminished by 4.10%.
- The S&P 500 Index fell by 4.60%.
- The NASDAQ Composite Index decreased by 8.95%.
- The MSCI ACWI (Net), used to gauge global equity performance, deteriorated by 5.36%.
- The Bloomberg Global Aggregate Index, which represents global bond markets, declined by 6.16%.
- The Chicago Board Options Exchange Volatility Index, a measure of implied volatility in the S&P 500 Index also known as the “fear index”, advanced from 17.22 to 20.56.
- WTI Cushing crude oil prices, a key indicator of movements in the oil market, surged from $75.21 a barrel at the end of December to $100.28 on the last day in March.
- The U.S. dollar ended the month at $1.31 against sterling, $1.11 versus the euro and at 121.70 yen.

Portfolio Review

Results in the Growth Fund were negative during the quarter. The environmental, social and governance screen (ESG) led to an unfavorable underweight to energy stocks. Stock selection within financials and health care enhanced returns. The Growth Fund’s underweight to low-quality stocks contributed.

During the quarter, the Fund suffered from an overweight to corporate bonds. Other detractors included an overweight to asset-backed securities (ABS); an underweight to taxable municipals bonds; a small allocation to non-U.S.-dollar currencies; allocations to hard and local currency debt; exposure to high-yield bonds; and a higher-quality bias within commercial MBS. The Fund gained on an overweight to the long-term segment of the U.S. Treasury yield curve. Other contributors included an overweight to non-agency mortgage-backed securities (MBS); selection within collateralized loan obligation (CLO) market; and an underweight to agency MBS. Western Asset Management suffered due to its long duration posture. Corporate credit exposure was negative. Off-benchmark allocations to non-U.S. dollar-denominated currencies hurt. An allocation to agency MBS helped, as did an overweight to the long-term segment of the U.S. Treasury yield curve. Income Research & Management benefited from strong selection within consumer non-cyclical and transportation. An underweight to agency MBS contributed. An overweight to and poor selection in ABS and commercial MBS anchored returns.

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. Inflation expectations are higher in the short term and 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:

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.

Index Glossary:

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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 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.

The Bloomberg 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.

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 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.

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- **Not FDIC Insured**
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- **May Lose Value**

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