



ecf Insights

ECF Endowment Management

First Quarter 2024

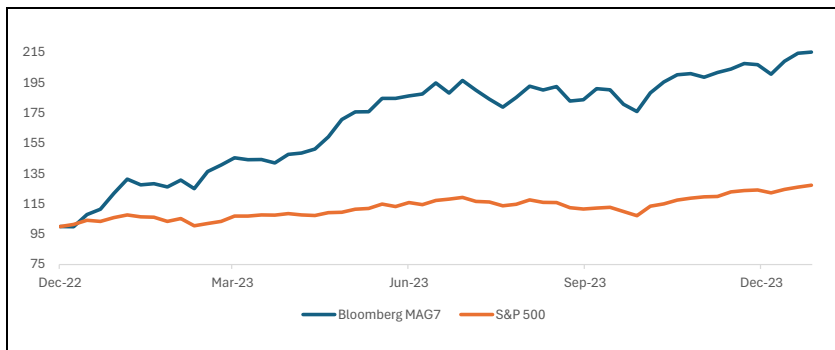
Will 2024 “pick up where we left off” in early 2022?

After the stock market hit a high in January 2022, excitement quickly faded as inflation and interest rates rose. The S&P 500 fell by 19% in 2022, its worst year since 2008. Even bonds, typically considered a safe haven, declined by 13%. As 2023 began, the threat of recession loomed, fueled by aggressive Fed rate hikes, persistent high inflation, and conflict in Eastern Europe.

In a surprising turn of events in 2023, markets demonstrated remarkable resilience as the Fed paused interest rate hikes and the US economy headed towards a soft landing, sparking a wave of optimism. The S&P 500 climbed the seemingly insurmountable “Wall of Worries,” soaring 36% from its October 2022 lows and achieving a 24% annual return in 2023.

By mid-January 2024, the markets not only bounced back but surpassed their highs from two years earlier. The vision that 2024 can “pick up where we left off” in 2022 began to emerge. Looking closer, however, there are at least two important differences between early 2022 and early 2024.

Chart 1: S&P 500 vs Bloomberg Magnificent 7 in 2023



Source: Morningstar, ECF

Endowment Tip

Are you planning to set up a new endowment or a new endowment fund?

Churches and others in this fortunate position have an opportunity to accomplish broader church goals while also taking all necessary steps to invest and oversee new endowment assets. You might wish to change how you talk about money or get new people involved in church leadership. This could be the time to address the needs of a broader community or improve how you budget.

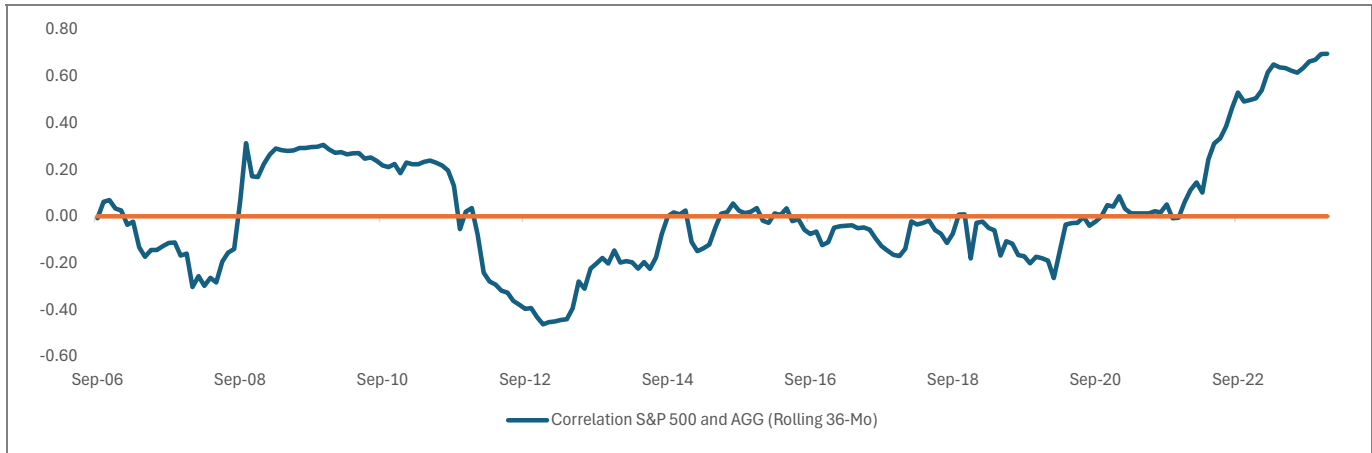
Our recent webinar, “**Are You Ready for New Endowment Gifts?**”, provides ideas and tips that can help your church. Watch the replay for a practical guide to setting up a new endowment or fund with guidance to inspire a renewed perspective on church goals.

Replay:

<https://episcopalparishes.org/?portfolio=finance-and-endowments>

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Chart 2: Correlation between stocks (S&P 500) and bonds (iShares US AGG Bond ETF) from 2006-2023, Rolling 36-mo



Source: Morningstar

Markets: Recovery Is Uneven

Sure, stocks, in general, recovered in 2023, but not all stocks shined equally. The 2023 market was characterized by certain segments significantly outpacing others. In fact, much of the market gain was concentrated in a small group of stocks. The leaders in the rapidly growing industry of Artificial Intelligence (AI) showed that company fundamentals were stronger than the headwinds from rising interest rates. Together these companies are known as the Magnificent 7 and include Apple, MSFT, AMZN, NVDA, Alphabet, TSLA, and Meta. They climbed 107% in 2023 (as per Bloomberg’s Magnificent 7 Index), outpacing the 24% from the S&P 500. (See Chart 1)

While the stock market had a strong recovery, the bond market's journey is still ongoing. Though the Federal Reserve's pause on interest rate hikes provided a boost, bonds haven't fully recovered from their losses in 2022. This is partly due to the still-elevated interest rate environment. In 2022, bonds declined 13% (Barclays US Aggregate), and despite a 5.5% return in 2023, they remain below their pre-crash levels.

Portfolios: Stock-Bond Correlations are Changing

Many portfolios bounced back in 2023, mirroring the market's climb, but it's worth noting that stocks and

bonds are now moving in the same direction. Two years ago, stocks and bonds moved in opposite directions – when one went up the other went down. However, the dramatic market movements over the last two years have shifted how asset classes behave relative to one another together, changing the correlations between them. Negative stock-bond correlations are now positive. This matters because diversification, the core principle of multi-asset investing, relies on these relationships.

Imagine you have two investments. If they move in lockstep (positively correlated), they won't offer much diversification. But if they move in opposite directions (negatively correlated) or don't move together at all (zero correlation), they can balance each other out, reducing portfolio performance variability (or risk). Traditionally, portfolios were built with the assumption that certain assets, like stocks and bonds, would dance to the beat of their own drums (zero correlation) or even counter each other's moves (negative correlation).

For a decade (November 2011 to November 2021), stocks (S&P 500) and bonds (iShares US AGG Bond ETF) largely maintained a negative correlation (see Chart 2), offering risk protection through diversification. However, recent market gyrations have rewritten the script. Since 2022, stocks and bonds have become unlikely allies, now moving in the same direction (positive correlation). This leaves portfolios feeling less shielded than before.

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Chart 3: Bond Performance in Years When Stocks Declined (1928-2023)

Year	Stock Return	Bond Return
1931	-43.3%	-2.3%
2008	-37.0%	13.1%
1937	-35.0%	1.6%
1974	-26.5%	5.7%
1930	-24.9%	6.7%
2002	-22.1%	12.9%
2022	-18.1%	-9.4%
1973	-14.7%	4.6%
2001	-11.9%	7.6%
1941	-11.6%	0.5%
1957	-10.8%	7.8%
1966	-10.1%	4.7%
1940	-9.8%	3.0%
2000	-9.1%	12.6%
1962	-8.7%	5.6%
1969	-8.5%	-0.7%
1929	-8.4%	6.0%
1932	-8.2%	8.8%
1946	-8.1%	1.0%
1977	-7.2%	1.4%
1981	-4.9%	9.5%
2018	-4.4%	1.2%
1990	-3.1%	9.7%
1934	-1.4%	9.0%
1953	-1.0%	3.2%
1939	-0.4%	4.5%

Source: Morningstar, S&P 500, US Treasury 5 year)

Although diversification is often associated with benefits in risk reduction, it actually has two benefits:

- *Risk Reduction*: Diversification helps smooth out portfolio performance bumps when assets are negatively correlated.
- *Capturing Returns*: When positively correlated assets climb together, diversification helps capture those gains.

When markets are on the rise, positive correlations between asset classes can lead to higher overall returns. However, when markets fall, positively correlated asset classes also fall in unison. While stocks have declined in 26 of the past 96 years (since 1928), the scenario where both stocks and bonds fall together is surprisingly rare. As Chart 3 shows, this has only occurred in three of those declining years (1931, 2022, and 1969). While it's important to consider this possibility, history suggests it's more of an outlier than the norm.

While market prices might suggest that 2024 is a simple case of “pick up where we left off” in early 2022, a look under the surface reveals a vastly different market. A few companies lead stock market returns, and stocks and bonds are now moving in sync. Will these differences erode over time, or will they be a feature of the future? Let’s watch together over 2024.

Upcoming Events

Early March:

Join ECF endowment experts at the annual conference of the Episcopal Parish Network in Houston on March 6-9, where ECF is proud to be leading the Endowments and Finance Pre-conference. Sessions on March 6 will focus on “**Forward-Looking Endowment Leadership,**” while March 7 will feature “**Case Studies: Inspiration for Endowment Use.**”

Register at

<https://web.cvent.com/event/b3e0a925-9b19-439e-915c-7bdf0f405561/summary>.

April 23, 2-3pm (ET):

Save the date for the live ECF/State Street Q1 2024 performance review for investors in our individually managed accounts. A recording will be available after the call

Early May:

Be on the lookout for our recorded ECF/State Street Q1 2024 performance review for investors in our pooled funds .



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