

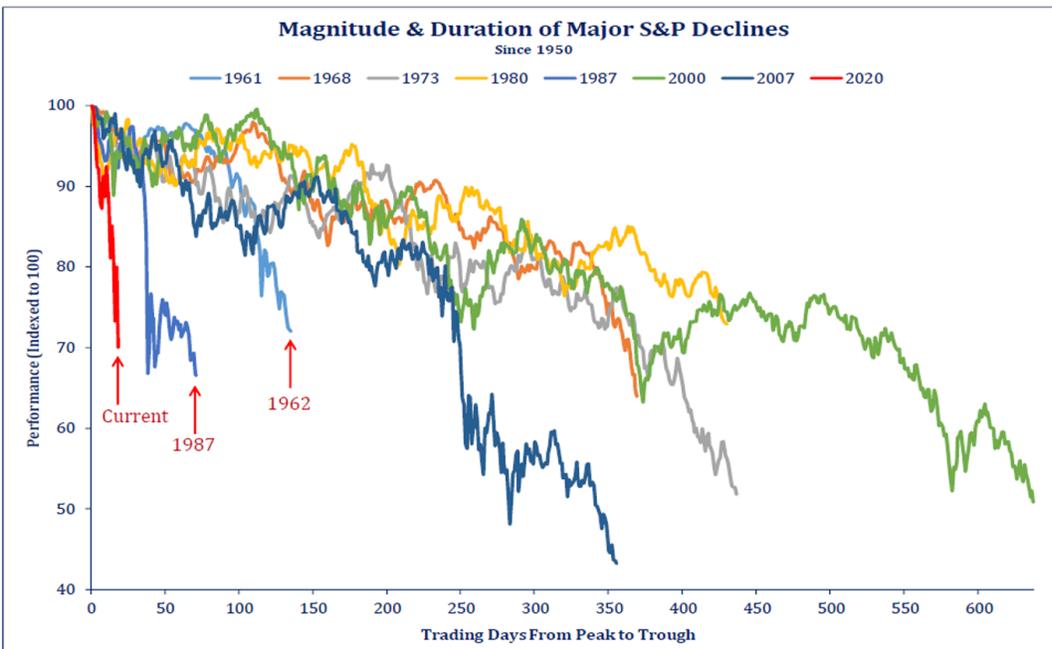
**Community Foundation for Greater Buffalo**  
**March 2020 - Market Conditions and Stewardship of Assets**

Presently, we are in the midst of an extraordinarily difficult time that combines a significant threat to health, economic well-being and challenges our ability to maintain sufficient resources to support our community through the current crisis while also preserving our ability to provide support for future needs.

The Community Foundation has long pursued a strategy that is built on balance, diversification and a high level of liquidity. This allows us to fund current needs while also prudently capitalizing on the extraordinary long-term opportunities that are created during times of great upheaval.

This document summarizes our views of current market conditions and our strategy for allocating the Foundation’s long-term assets.

*Market Conditions*



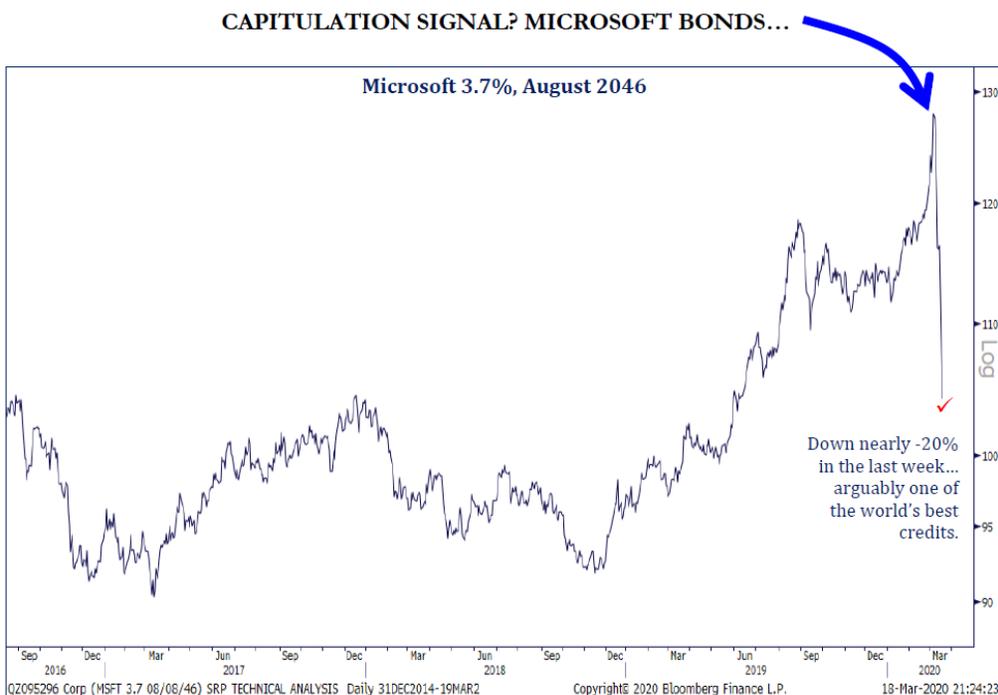
Source: Strategas Research Partners

This chart was produced as of March 17, 2020 and reflects the largest equity market declines since 1950. While we are not currently experiencing the largest decline in terms of magnitude, it has been the most rapid. In our view, there are a number of factors worth considering.

- There is now an extremely wide range of near term economic/business outcomes – market volatility and downward pressure are entirely logical from this perspective.

- Changes in market structure – i.e. the dominance of computer driven trading, reduction in the significance of fundamental active management and other factors are contributing to volatility and extraordinary levels of mispricing even when considering a highly pessimistic outlook for business conditions.
- We are seeing a reaction from the active management community – several very capable (and typically inaccessible) firms are accepting capital in some cases for the first time in years. This too has occurred at an unusually rapid pace. Limiting the following to the non-promotional firms, figures such as 20 to 30% projected multi-year IRRs and “historic discounts to fair value” have been mentioned.
- Market panics are highly charged climates and the combination of threats to everyone’s health, a severe economic contraction and increasingly unstable capital markets are a recipe for prices that reflect economic outcomes that have virtually no chance of occurring. This is where massively outsized and asymmetric opportunities for rigorous and patient long-term investors are born.

To illustrate the nature of market pricing, the following chart provides a recent snapshot of the performance of Microsoft bonds.



Source: Strategas Research Partners

### *Portfolio Strategy*

While ideas such as the “world muddles through” and “this too shall pass” provide essential perspective regarding the importance of remaining committed to long-term outcomes, we also believe that it is important to consider scenarios where the impact of Covid-19 lasts for as long

as 24 months. This is not a reference to a continuing shutdown of our economy but rather the idea that there will be continuing negative implications related to both the disease and the steps to stop its transmission.

The implications of the more negative scenarios are as follows:

- Exposure to investments where balance sheet strength, the need for access to the capital markets or other factors that depend on a more rapid return to normal should be approached with great caution.
- The dysfunction of markets tends to significantly reduce the expected benefits of portfolio diversification. The Foundation will continue to have sufficient access to cash in order to fund the community's needs as we go through this difficult period.
- Assuming equity portfolios are constructed with the potential for an extended period of economic impact, we currently see a wide array of securities that are trading with exceptional asymmetry. This is a reference to exceptionally large expected returns in the base case and compelling returns in downside cases. It is for this reason that the Foundation intends to maintain its pre-crisis equity exposure.

This leads to an approach that is somewhat similar to that which the Foundation pursued during the 2007-09 Global Financial Crisis. The Foundation's investment advisor, Colonial Consulting has been actively pursuing the following.

- 1) Close monitoring of all managers – this is focused on portfolio actions, written reports and conference calls. They are looking for calm, thoughtful behavior.
- 2) Closely monitor portfolios for allocations compared to policy – Colonial has robust systems that allow them to monitor performance daily. Under normal conditions, this information is used to assess the degree of long-term thinking of managers and risk factors in the portfolio. Presently, it is also being used to determine portfolio exposures for the purpose of informing the Foundation when it would be advisable to redeploy capital based on market opportunities.
- 3) Reach out to exceptional and generally inaccessible managers with the goal of obtaining capacity that can be used to upgrade the portfolio. The Foundation continues to benefit from the use of this strategy just over ten years ago in the Global Financial Crisis.

The ideas of discipline, balance, diversification and a risk-aware but opportunistic view have long been tenets of the Foundation's strategy. Looking back at prior periods of weak market conditions provides perspective regarding the effectiveness of this approach.

**Foundation Pool's Largest Drawdowns – Recovery Period – Since 1998**

<u>Drawdown Period</u>	<u>Drawdown</u>	<u>Return Relative to S&amp;P 500</u>	<u>Time Until High Water Mark Regained</u>	<u>Annualized 5 Year Return From Peak</u>
5-1998 to 8-1998	-14.3%	+ 1.1%	8 Months	+ 0.4%
9-2000 to 9-2002	-18.8%	+ 25.9%	13 Months	+ 4.2%
11-2007 to 2-2009	-32.8%	+ 18.2%	20 Months	+ 2.5%
5-2011 to 9-2011	-12.3%	+ 4.0%	11 Months	+ 5.1%
6-2015 to 2-2016	-10.8%	- 2.4%	10 Months	NA
10-2018 to 12-2018	-9.5%	+ 4.0%	4 Months	NA

Over these six timeframes, the portfolio generated significant interim losses. In all but one, the portfolio outperformed the equity markets as measured by the S&P 500. Furthermore, in four of these instances, the portfolio recovered 100% of the decline in market value in less than a year. Finally, in each of the four periods where at least five years has passed since a market peak, the portfolio generated a positive five year annualized return from the prior peak.