



MISSOURI  
BAPTIST FOUNDATION

GREAT COMMISSION • GREAT INVESTMENT

# Asset Class Definitions/Manager Selection Criteria

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# Asset Class Definitions

The following pages help define in detail each asset class as understood by MBF.

❖ Global Stocks

❖ Benchmark: MSCI ACWI (All Country World Index)

❖ Private Equity

❖ Benchmark: Cambridge PE Index

❖ Equity Exposure

❖ Benchmark: HFN L/S (Long/Short)

❖ Fixed Income

❖ Benchmark: Barclays Intermediate Gov't/Credit

❖ Diversifying Strategies

❖ Benchmark: REIT, MLP, CTA, Distressed

❖ Real Assets

❖ Benchmark: CPI plus 3%

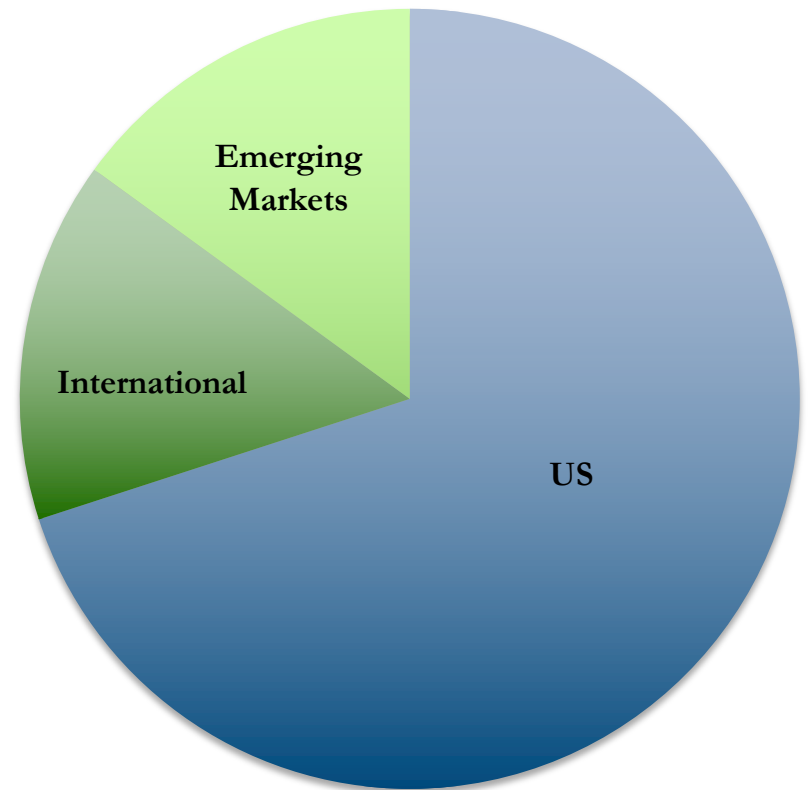
# Global Stocks

## ➤ **Definition**

- Ownership in publicly traded companies
- A market-weighted combination of U.S. and Non-U.S. markets

## ➤ **Strategic Role**

- Key rationale for adopting global equity framework is to exploit greater opportunity set in global markets
- Global equity market correlations have increased, rendering regional decision less important
- Global equity is a recognition of stronger long-term economic growth outside of the U.S. and a broadening of the opportunity set for asset managers



# Global Stocks

## ➤ **What We Believe**

- Global markets offer the best opportunities for long-term growth
- Market valuation affects long-term return
- Equity markets are always changing, sometimes efficient, and sometimes inefficient
- Finding active manager skill is difficult but possible
- Biblically responsible investing aligns holdings with our belief
- Freedom is essential, so totalitarian regimes like China and Saudi Arabia are avoided.

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Social screening

## ➤ **How We Implement**

- Benchmark is the MSCI All Country World Index
- Core – satellite model can be utilized to take advantage of both passive and active benefits

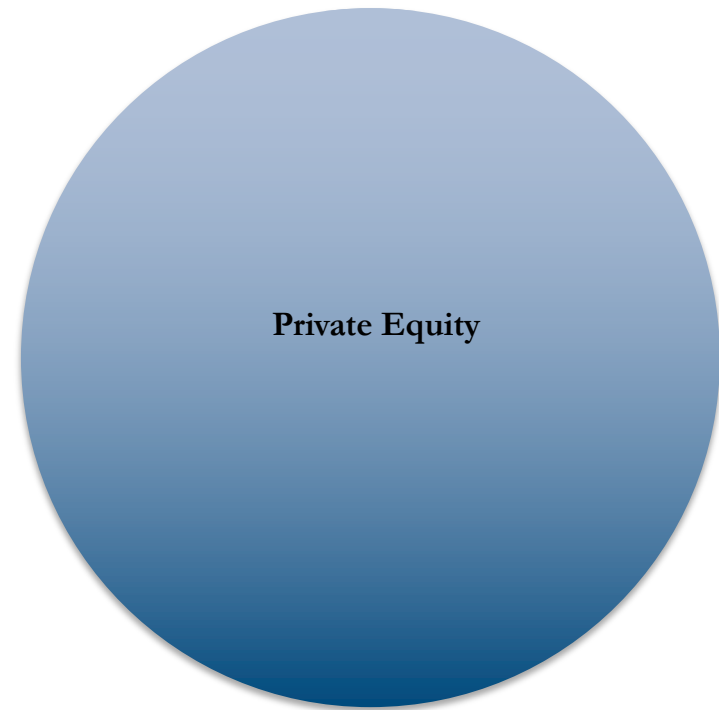
# Global Stocks (Private Equity)

## ➤ **Definition**

- Ownership in private equity and venture capital funds
- Long-term accredited funds only

## ➤ **Strategic Role**

- Higher potential returns than public stock markets
- Increased risk profile due to age of companies
- Commonfund investments (from prior advisory firm) to be liquidated upon expiration dates, but other funds may be accepted.



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# Global Stocks (Private Equity)

## ➤ **What We Believe**

- Private Equity and Venture Capital Funds may offer a premium return profile over traditional Capital Markets like Stocks
- Finding active manager skill is difficult but possible
- Biblically responsible investing is more difficult to find in this space, but not impossible

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Performance incentive fees

## ➤ **How We Implement**

- Funds are becoming available that deliver Christian Impact and meet the Biblically responsible investment standard.

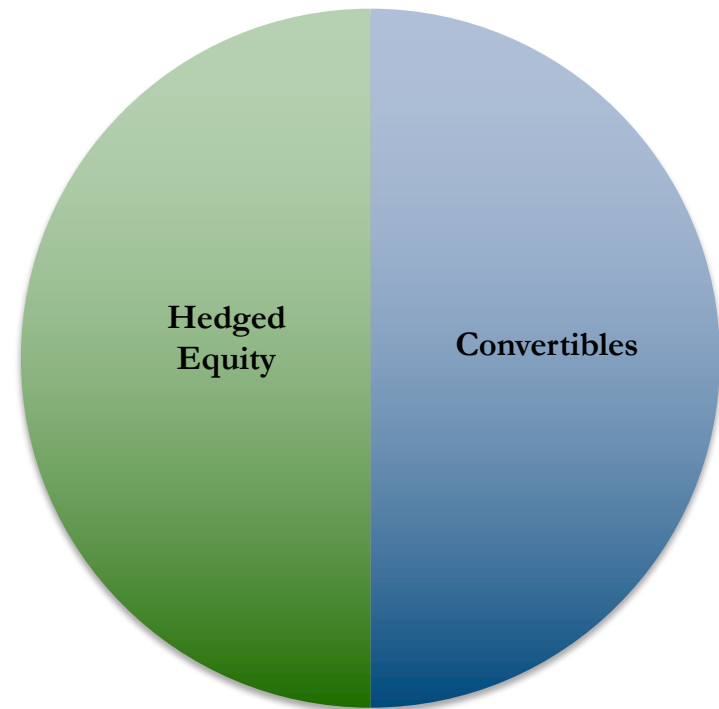
# Global Stocks (Equity Exposure)

## ➤ **Definition**

- Alternative to stock market long-only
- Investment includes Hedged Equity and Convertible Bonds

## ➤ **Dual Strategic Role**

- We seek long-term market return with much lower volatility in Hedged Equity
- Convertibles offer upside potential, less volatility than long-only, and more liquidity than hedged equity



# Global Stocks (Equity Exposure)

## ➤ **Characteristics**

- Medium or average volatility; ideally about half standard deviation of Russell 3000 index
- Same global exposure as equities

## ➤ **Implementation**

- Emphasis on active management
- Fund of Fund approach to hedged equity allows for diversification and oversight

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Overlapping fund of fund management fees
- Transaction costs

## ➤ **Risks**

- Underperformance in up markets will be a risk borne in this strategy
- Manager inability to capture “short” book alpha



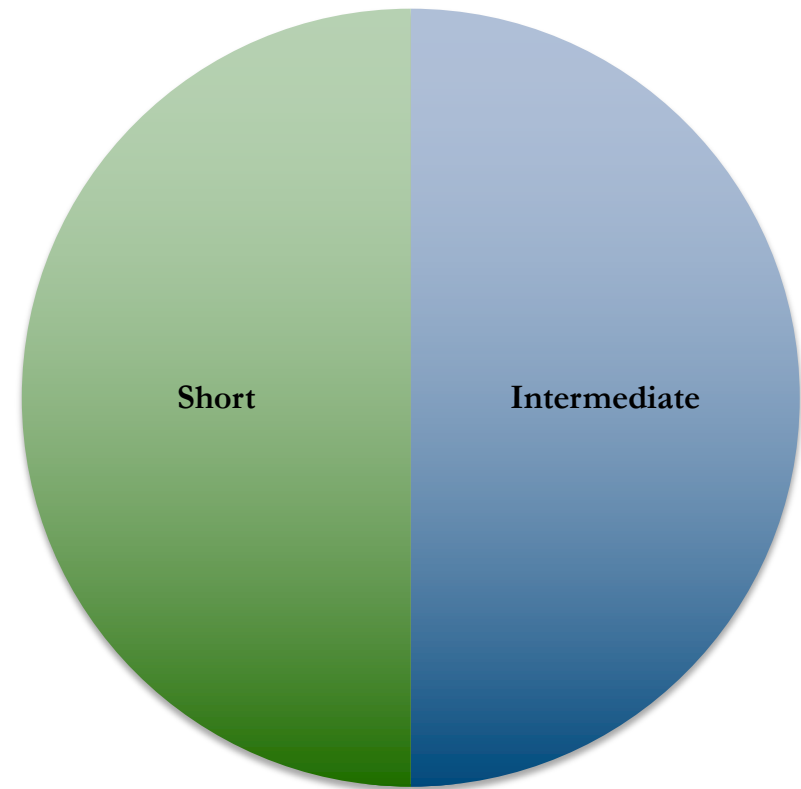
# Fixed Income

## ➤ **Definition**

- The debt obligations of companies and government entities of the U.S., issued in U.S. Dollars
- Intermediate and short-term Duration only, with very limited and specific long-term exposure, and A rated or better credit average quality

## ➤ **Strategic Role**

- Hedge against stock market volatility
- Current income
- Provide current improvement in the total portfolio's risk/return
- Possibility of return enhancement through active management



# Fixed Income

## ➤ **Characteristics**

- Medium or average volatility
- Two distinct strategies – Intermediate and Short Duration

## ➤ **Implementation**

- Active management, utilizing two separate investment managers

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Custody costs
- Transaction costs

## ➤ **Risks**

- The primary risk associated with bond returns is volatility related to unexpected changes in inflation, the business cycle, interest rates, and the availability of credit
- Duration risk is managed by employing intermediate and short-term strategies only

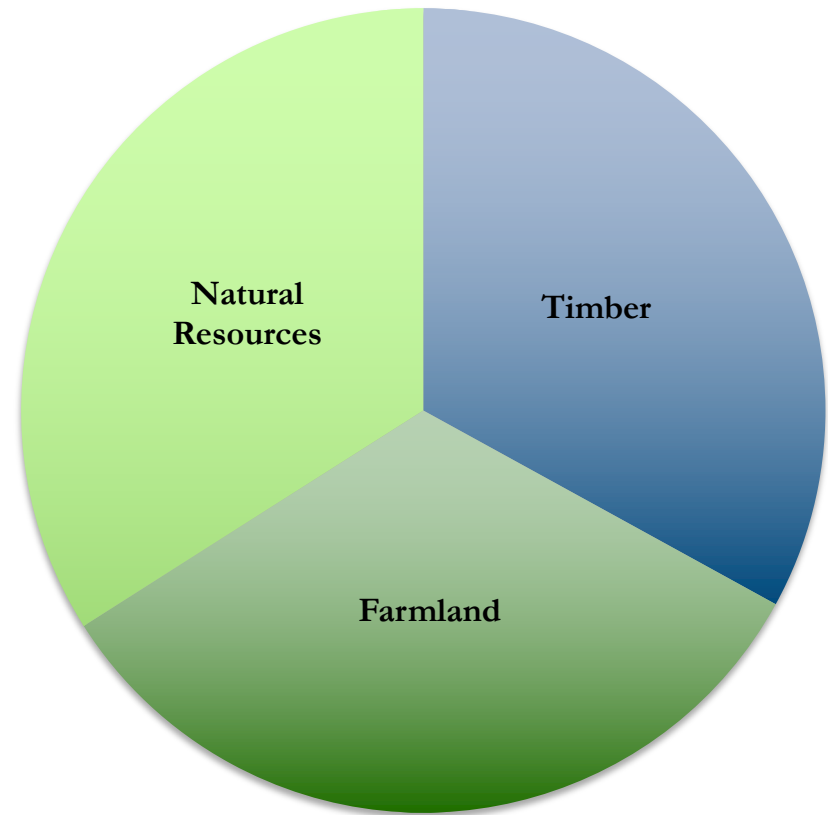
# Real Assets

## ➤ **Definition**

- Physical, tangible assets such as real estate, timber, farmland, energy, metals, commodities

## ➤ **Strategic Role**

- Low correlation to typical capital markets
- Hedge against high inflation
- Current income
- Provide current improvement in the total portfolio's risk/return tradeoff
- Possibility of return enhancement through active management



# Real Assets

## ➤ **Characteristics**

- Medium or average volatility
- Long-term in nature; generally, five years minimum
- Income producing

## ➤ **Implementation**

- Emphasis on active management
- Diversify amongst several general partners

## ➤ **Operations**

- Investment is usually through limited partnerships
- Pricing and performance information is usually slower than other investments

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Custody costs

## ➤ **Risks**

- Liquidity is the biggest concern, as investments are unavailable for 3-7 years
- Manager skill is imperative, so the risk of underperformance is large
- Global economy collapse

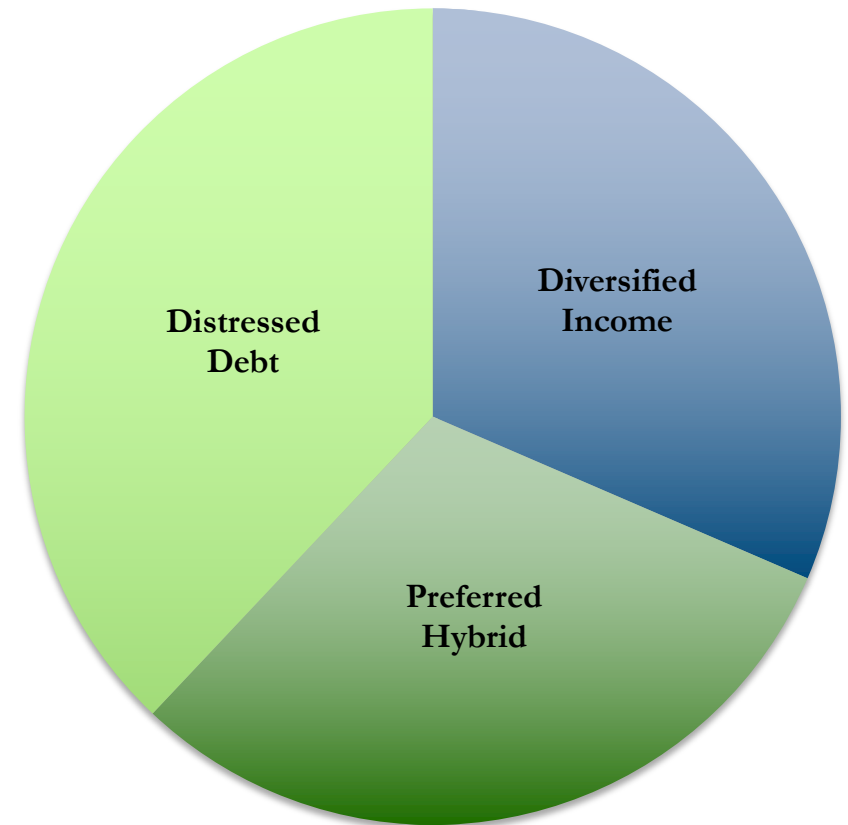
# Diversifying Strategies

## ➤ **Definition**

- We are attempting to find assets that are uncorrelated to the equity and traditional fixed markets.

## ➤ **Strategic Role**

- Current Income
- Hedge against equity and fixed volatility
- Provide current improvement in the total portfolio's risk/return tradeoff at same levels of risk
- Possibility of return enhancement through active management



# Diversifying Strategies

## ➤ **Characteristics**

- Medium or average volatility
- Wide variety of assets
- Income producing

## ➤ **Implementation**

- Emphasis on active management
- Find asset classes that are absolute return in nature with limited volatility

## ➤ **Costs Ranked in Order of Magnitude**

- External management fees
- Transaction costs

## ➤ **Risks**

- Underperformance versus traditional asset classes
- Poor manager performance
- Limited liquidity

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# Investment Manager Selection and Retention

## Overview

MBF recognizes that the successful selection of active investment managers is part art and part science.

We know and expect that our managers will underperform their respective benchmarks at various times, so the following guidelines will attempt to outline a **process** for hiring, retaining and removing investment managers.

# Investment Manager Selection and Retention

## Process Outline

### ➤ Hiring an Active Manager - Qualitative

- We prefer a 100% employee-owned organization mainly or solely focused on a single strategy that is client-focused with accessible portfolio managers (not just marketing staff) and has a stable and transparent (AIMR compliant) track record. Assets managed by the firm and the portfolio manager structure should be stable.
- Manager fees should be a major factor and we expect fees to be competitive. Currently, active equity manager fees are between approximately 0.50%-1.00% annually and active fixed manager fees are approximately 0.25% per year.
- Any manager should be willing to comply with MBF's Investment Policy and have full knowledge of our desire for active Biblically responsible investing (BRI) screening.

### ➤ Hiring an Active Manager - Quantitative

#### ➤ Equity Manager

- The most recent three-year track record should be favorable to the respective benchmark for the following – return, information ratio and universe rank. We will also investigate five- and ten-year records to know how the manager has performed in various market conditions.
- The manager must show the ability to protect the portfolio in down markets as well, so downside ratio for three, five and ten-year periods should be favorable (less than 100%).

#### ➤ Fixed Income Manager

- The most recent three-year record should be examined for risk. The manager should be able to demonstrate a consistent ability to achieve return near the benchmark with less risk (standard deviation).



# Due Diligence Criteria: Mutual Funds & SMA's

## Quantitative Measures

- **Cumulative Return vs Benchmark – 5 Years**
- **Risk/Return – 5 Years**
  - Standard Deviation
  - Return
  - Sharpe Ratio
  - Maximum Drawdown
  - Up/Down Capture
  - Alpha & Beta
- **Static**
  - Calendar Years
  - 1, 3, 5, 7, & 10 Years vs. Benchmark
- **Universe Rankings (PSN and/or Morningstar)**
  - 10 Year Returns (w/ 3-year rolling periods)
  - 3 Year Static (using 'Risk/Return – 5 Years' above statistics)

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# Due Diligence Criteria: Mutual Funds & SMA's

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## Qualitative Measures

- **Ownership structure explained**
- **Measure depth and experience of management and portfolio manager(s)**
- **Understandable and repeatable process**
- **Direct discussion with top management and portfolio manager(s)**
- **Fee discussion – compare to universe and determine if negotiable**

# Due Diligence Criteria: Alternatives

## Quantitative Measures

- **Cumulative Return vs Benchmark – 5 Years**
- **Risk/Return – 5 Years**
  - Standard Deviation
  - Return
  - Sharpe Ratio
  - Maximum Drawdown
  - Up/Down Capture
  - Alpha & Beta
- **Static**
  - Calendar Years
  - 1, 3, 5, 7, & 10 Years vs. Benchmark
- **Universe Rankings (PSN and/or Morningstar)**
  - 10 Year Returns (w/ 3-year rolling periods)
  - 3 Year Static (using 'Risk/Return – 5 Years' above statistics)

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# Due Diligence Criteria: Alternatives

## Qualitative Measures

- **Ownership structure explained**
- **Measure depth and experience of management and portfolio manager(s)**
- **Operational soundness**
  - Legal review
  - Valuation Policy
  - Fund Administrator Review
  - Audited Financials Review
- **Direct discussion with top management and portfolio manager(s)**
- **Fee discussion – compare to universe and determine if negotiable**

# Investment Manager Selection and Retention

## Process Outline

### ➤ **Terminating a Manager - Qualitative**

- Whenever there is a significant event (firm ownership, portfolio manager change, staff defections, change in strategy, negative news, inability to abide by screening requirements), the consultant will report to the investment committee immediately.

### ➤ **Terminating a Manager - Quantitative**

- **Equity Manager** – When a manager underperforms for two consecutive years, they will be required to report to the committee to explain. The manager will then be placed on “watch” and a formal search will begin to find a replacement. The “watch” manager will be allocated special attention by the consultant and committee. Three-year track records favorable to the benchmarks are required, so the committee should be prepared to terminate as soon as a manager fails to comply.
- **Fixed Income Manager** – The same rules as equity managers apply, but emphasis will be placed on risk measurements such as standard deviation and beta. Our active fixed income manager must be able to control risk, so a “watch” will be placed on the manager if they fail to comply in any two-year consecutive period.

# OCC Process for Private Investment Reporting

1. Receive statement from custody agent and post to our performance reporting vendor Clearwater Analytics. No reported returns from managers are posted; only custody statements.
2. Record any capital call or distributions in real time to Clearwater.
3. Review audited financials. Use to check custody return.
4. Document all meetings (in-person or conference call) with managers.
5. Cross-check process during annual CEFEX audit.



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