IDAHO ENDOWMENT FUND
INVESTMENT BOARD

Presentation to Economic Outlook and Revenue Assessment Committee

January 5, 2023

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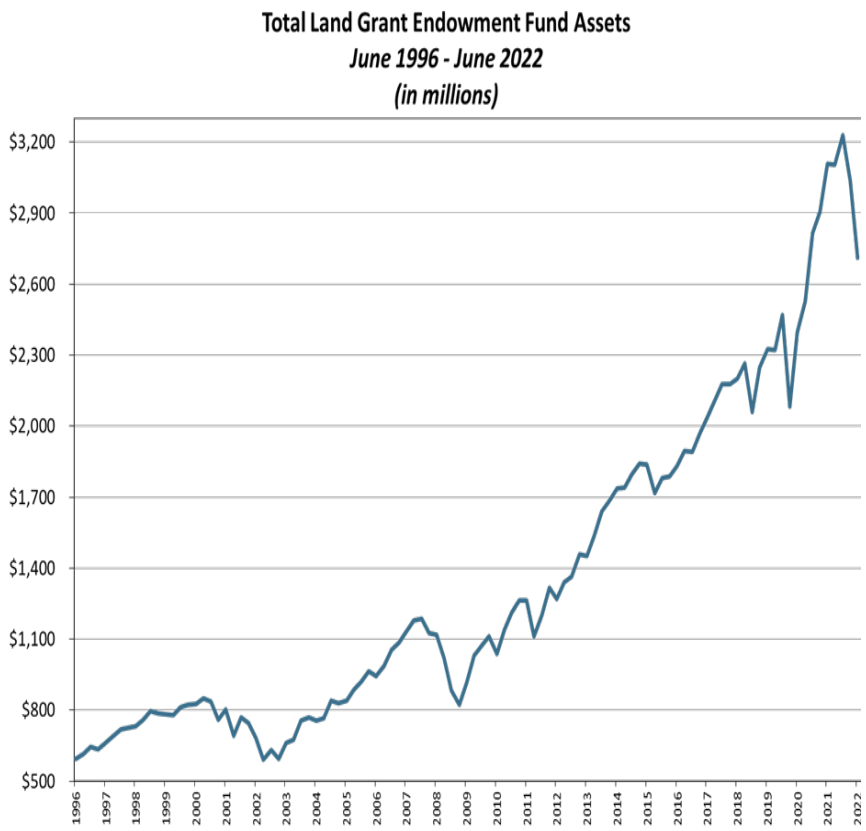
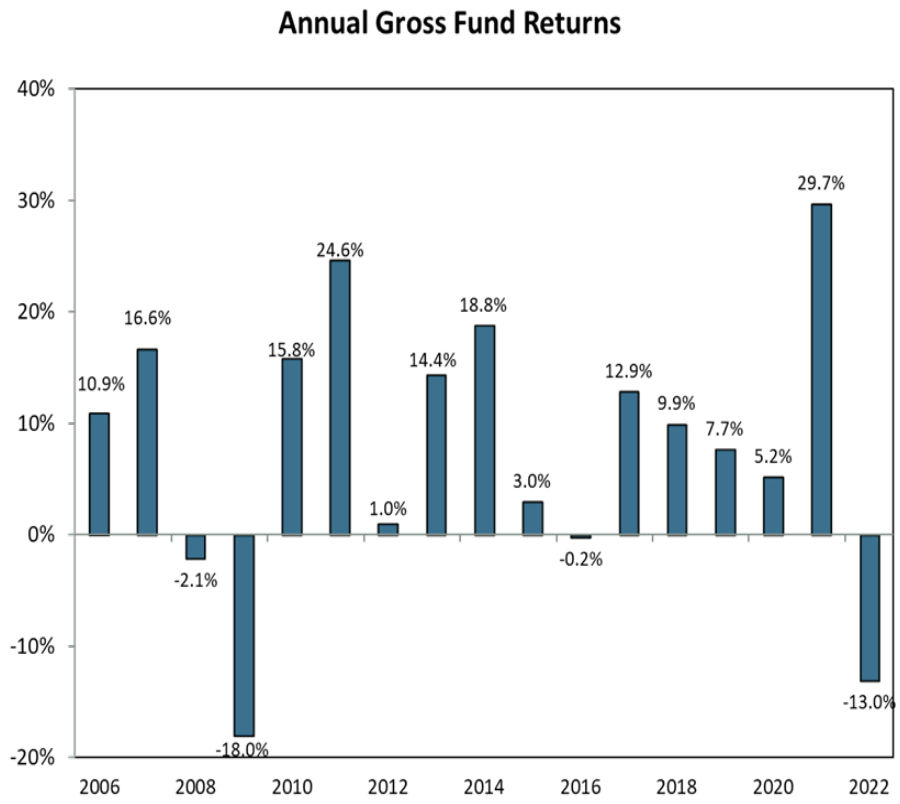
Manager of Investments
Endowment Fund Investment Board

Endowment Fund Investment Board

After big gains in FY2021, FY2022 was a challenging year for the Endowment Fund.





Callan Periodic Table of Investment Returns

Nearly every asset class is down in 2022.

Annual Returns		Monthly Returns										
2020	2021	Jan 2022	Feb 2022	Mar 2022	Apr 2022	May 2022	Jun 2022	Jul 2022	Aug 2022	Sep 2022	Oct 2022	YTD 2022
Small Cap Equity 19.96%	Large Cap Equity 28.71%	Emerging Market Equity -1.89%	Small Cap Equity 1.07%	Real Estate 4.47%	High Yield -3.56%	Dev ex-U.S. Equity 0.83%	U.S. Fixed Income -1.57%	Small Cap Equity 10.44%	Emerging Market Equity 0.42%	High Yield -3.97%	Small Cap Equity 11.01%	High Yield -12.53%
Large Cap Equity 18.40%	Real Estate 26.09%	Global ex-U.S. Fixed Income -1.96%	High Yield -1.03%	Large Cap Equity 3.71%	U.S. Fixed Income -3.79%	U.S. Fixed Income 0.64%	Global ex-U.S. Fixed Income -4.50%	Large Cap Equity 9.22%	Small Cap Equity -2.05%	U.S. Fixed Income -4.32%	Large Cap Equity 8.10%	U.S. Fixed Income -15.72%
Emerging Market Equity 18.31%	Small Cap Equity 14.82%	U.S. Fixed Income -2.15%	Global ex-U.S. Fixed Income -1.11%	Small Cap Equity 1.24%	Real Estate -5.48%	Emerging Market Equity 0.44%	Emerging Market Equity -6.64%	Real Estate 7.96%	High Yield -2.30%	Global ex-U.S. Fixed Income -5.87%	Dev ex-U.S. Equity 5.51%	Small Cap Equity -16.86%
Global ex-U.S. Fixed Income 10.11%	Dev ex-U.S. Equity 12.62%	High Yield -2.73%	U.S. Fixed Income -1.12%	Dev ex-U.S. Equity 1.16%	Emerging Market Equity -5.56%	High Yield 0.25%	High Yield -6.73%	High Yield 5.90%	U.S. Fixed Income -2.83%	Large Cap Equity -9.21%	Real Estate 2.99%	Large Cap Equity -17.70%
Dev ex-U.S. Equity 7.59%	High Yield 5.28%	Dev ex-U.S. Equity -4.41%	Dev ex-U.S. Equity -1.56%	High Yield -1.15%	Dev ex-U.S. Equity -6.57%	Large Cap Equity 0.18%	Small Cap Equity -8.22%	Dev ex-U.S. Equity 4.97%	Large Cap Equity -4.08%	Dev ex-U.S. Equity -9.26%	High Yield 2.60%	Dev ex-U.S. Equity -22.16%
U.S. Fixed Income 7.51%	U.S. Fixed Income -1.54%	Large Cap Equity -5.17%	Real Estate -2.47%	Emerging Market Equity -2.26%	Global ex-U.S. Fixed Income -6.83%	Small Cap Equity 0.15%	Large Cap Equity -8.25%	U.S. Fixed Income 2.44%	Dev ex-U.S. Equity -4.67%	Small Cap Equity -9.58%	Global ex-U.S. Fixed Income -0.14%	Global ex-U.S. Fixed Income -23.98%
High Yield 7.11%	Emerging Market Equity -2.54%	Real Estate -5.75%	Emerging Market Equity -2.99%	U.S. Fixed Income -2.78%	Large Cap Equity -8.72%	Global ex-U.S. Fixed Income 0.01%	Real Estate -8.69%	Global ex-U.S. Fixed Income 1.92%	Global ex-U.S. Fixed Income -4.99%	Emerging Market Equity -11.72%	U.S. Fixed Income -1.30%	Real Estate -27.81%
Real Estate -9.04%	Global ex-U.S. Fixed Income -7.05%	Small Cap Equity -9.63%	Large Cap Equity -2.99%	Global ex-U.S. Fixed Income -3.20%	Small Cap Equity -9.91%	Real Estate -4.35%	Dev ex-U.S. Equity -9.41%	Emerging Market Equity -0.25%	Real Estate -6.49%	Real Estate -12.42%	Emerging Market Equity -3.10%	Emerging Market Equity -29.42%

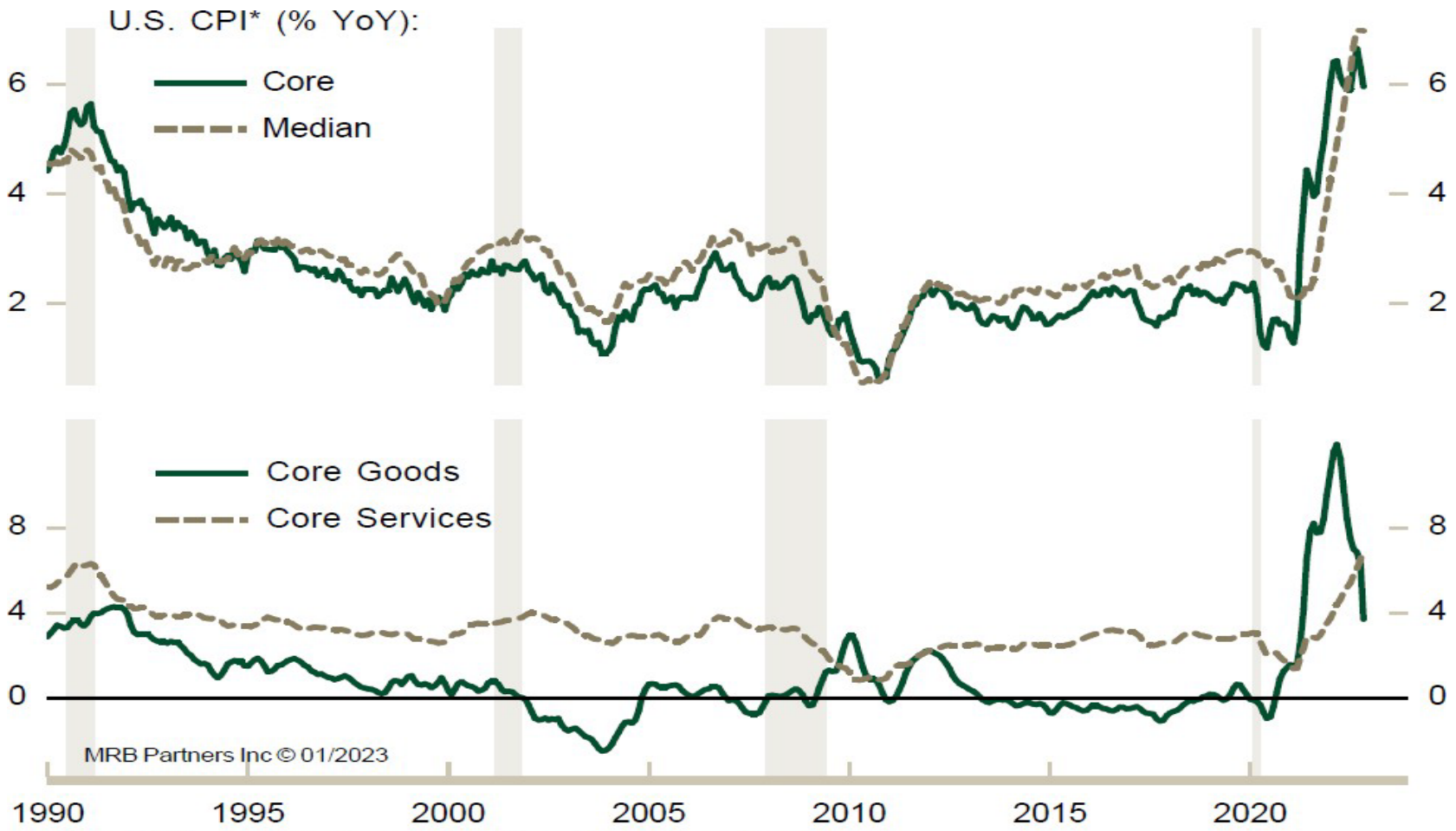
Sources: ● Bloomberg Aggregate ● Bloomberg Corp High Yield ● Bloomberg Global Aggregate ex US ● FTSE EPRA Nareit Developed ● MSCI World ex USA ● MSCI Emerging Markets ● Russell 2000 ● S&P 500

Financial Markets Had A Challenging 2022

- Massive fiscal and monetary stimulus surrounding COVID-19, supply chain issues and the war in Ukraine drove significant increases in inflation.
- The Federal Reserve pivoted from monetary accommodation to fighting inflation by increasing the fed funds rate and shrinking its balance sheet. Higher interest rates and recession fears have hurt both the bond and equity markets. The U.S. economy is slowing, but so far it has remained resilient.
- China's economy contracted due to its COVID-zero policy and a new regulatory regime focused on "common prosperity."
- Europe's economy has been hit hard by high energy prices.

Efforts to Control Inflation Have Driven Financial Markets

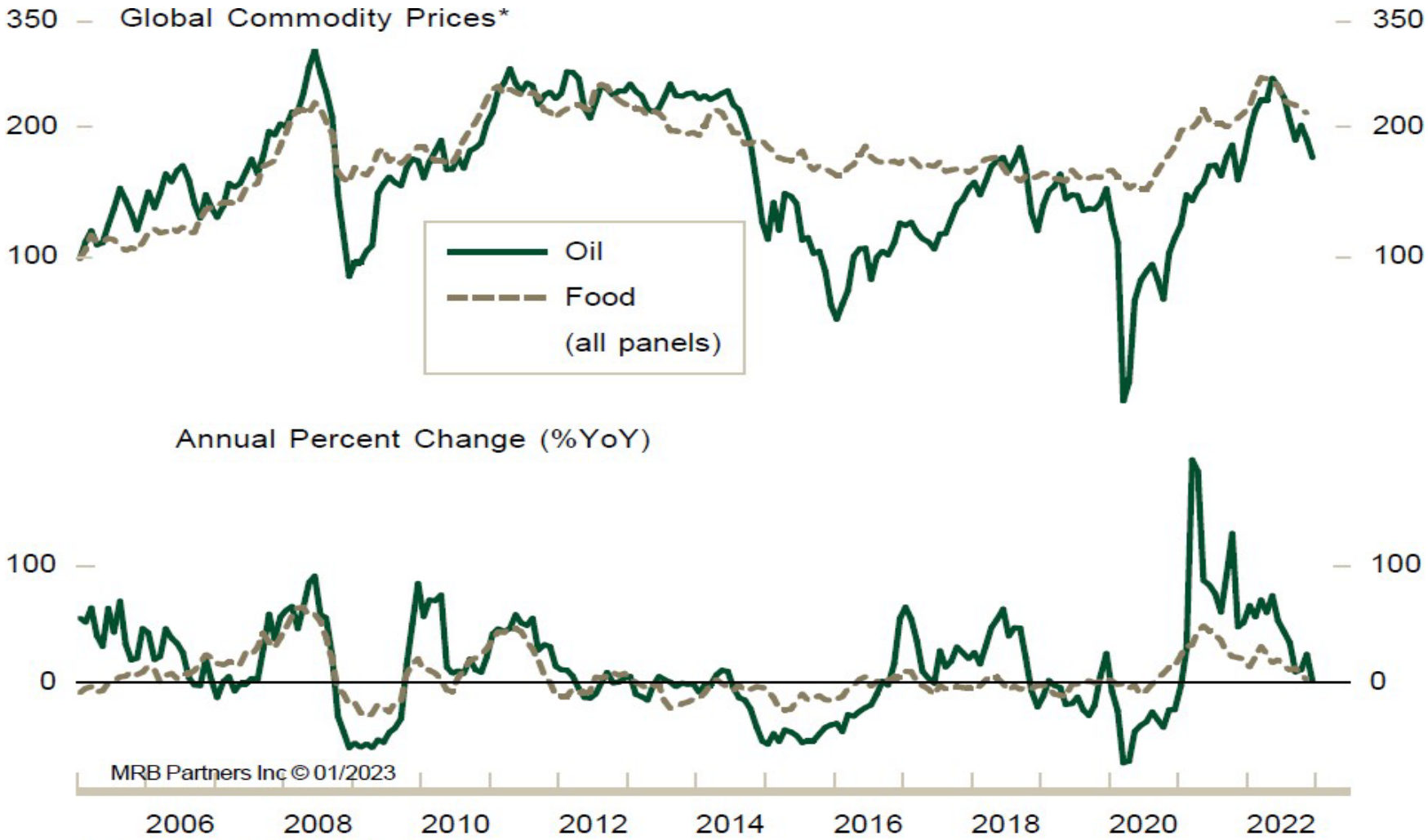
Goods prices have softened. Moderating service prices are the key to taming inflation.



* Core excludes food & energy, smoothed; source: Bureau of Labor Statistics
Note: Shaded for NBER-desingated U.S. recessions

Commodity Prices Have Started to Roll Over

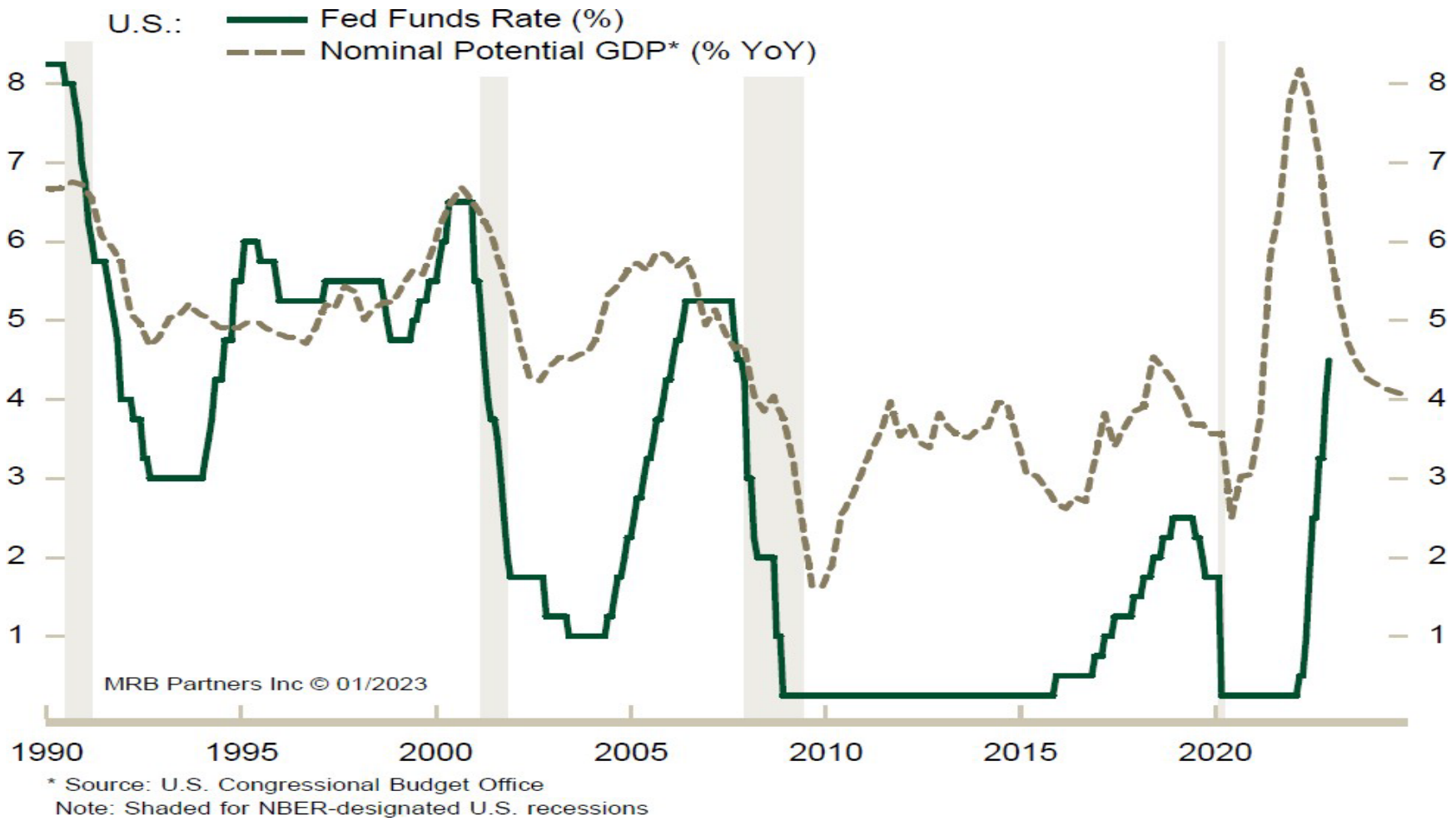
This should help ease inflationary pressures.



* Source: The Economist via Macrobond
Note: Panel 1 is rebased

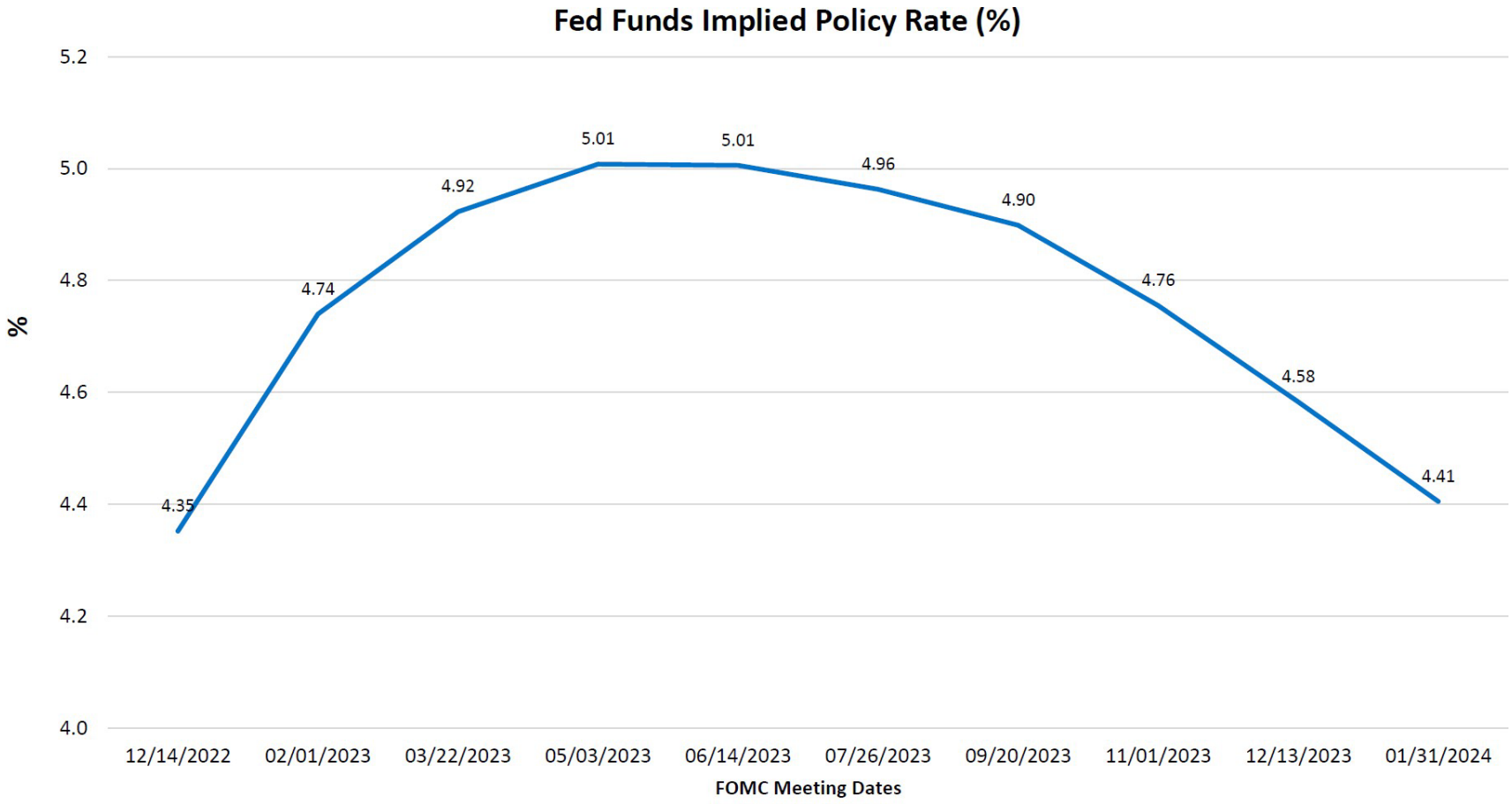
The Federal Reserve is Committed to Bringing Down Inflation

Inflation is acutely painful for households struggling to pay for food, housing, transportation and other basic needs. The Federal Reserve has increased the Fed funds rate aggressively and started shrinking its balance sheet.



The Federal Reserve Currently Plans to Keep Rates High Through 2023

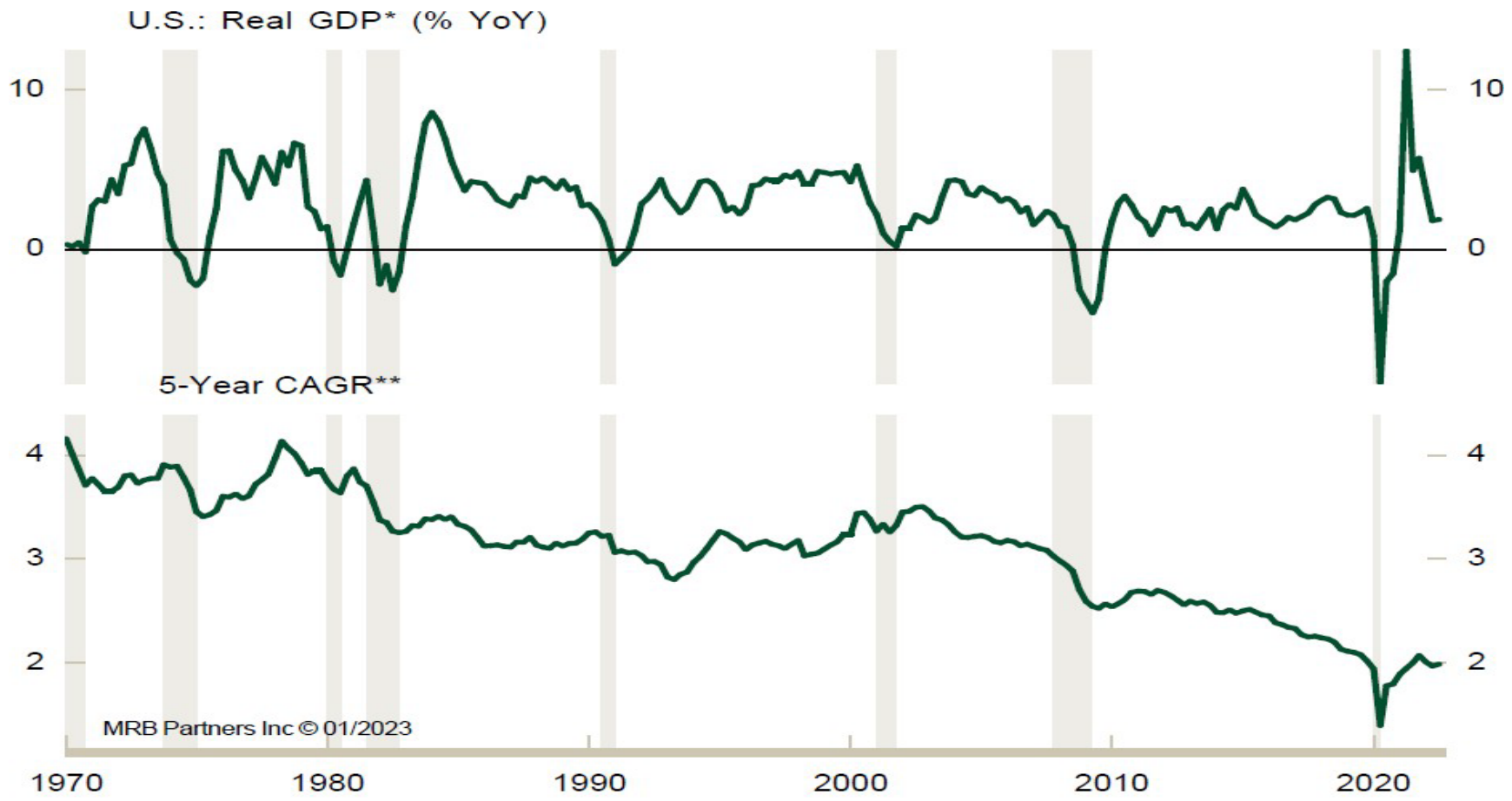
The Fed funds rate is currently expected to peak in early 2023 at around 5.0% and remain "restrictive" until it is clear inflation is under control.



As of December 5, 2022
Source: Bloomberg, DoubleLine
Implied Policy rates are based on Fed Fund Futures provided by Bloomberg's World Interest Rate Probability (WIRP) Monitor.

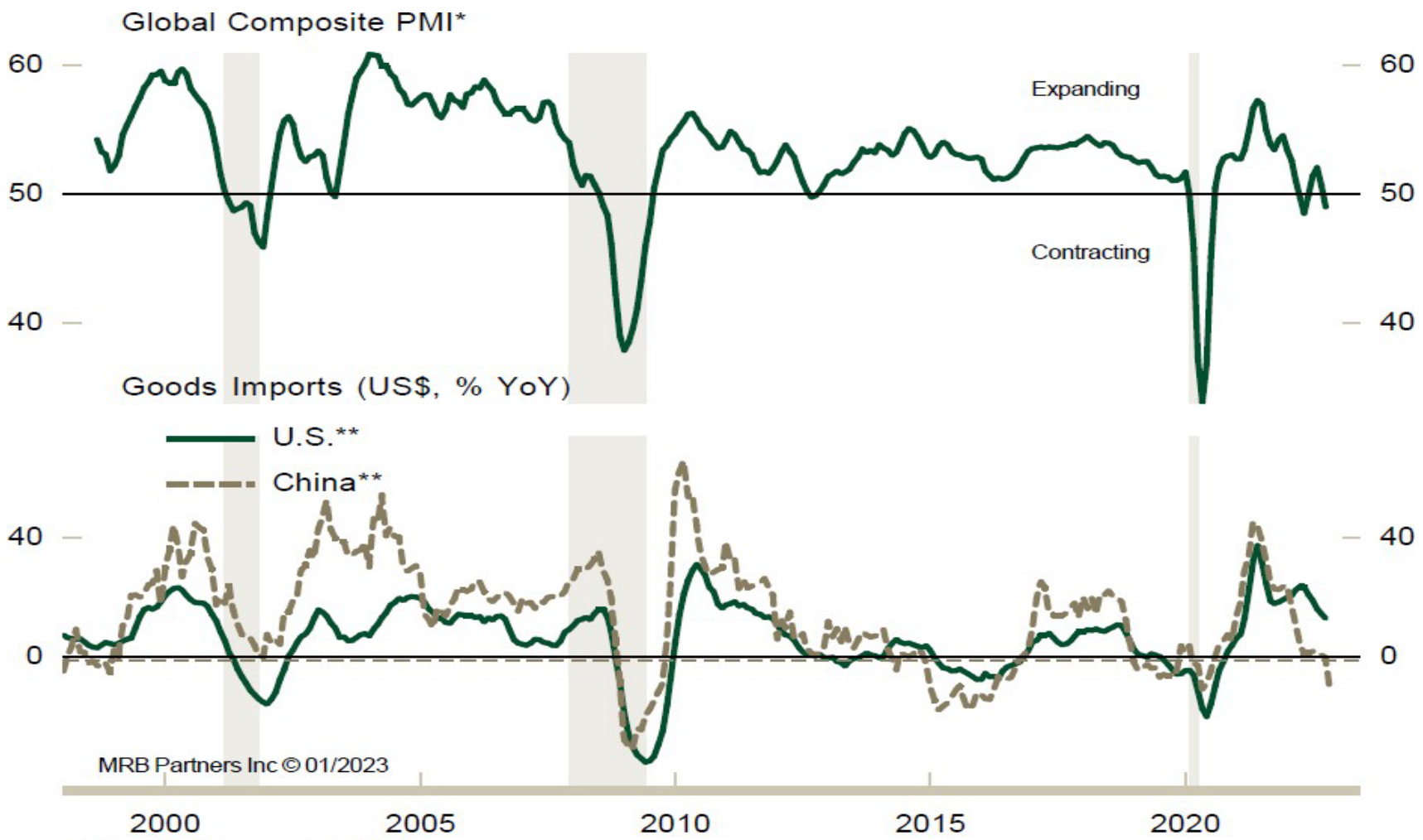
U.S. Real GDP is Slowing

The longer the Fed keeps interest rates in "restrictive" territory, the greater the probability of a recession. The Fed projects GDP growth of only 0.5% in 2023.



* Source: U.S. Bureau of Economic Analysis
**: Cagr=compound annual rate
Note: U.S. Bureau of Labor Statistics
** Smoothed; source: The Conference Board
Note: Shaded for NBER-desingated U.S. recessions

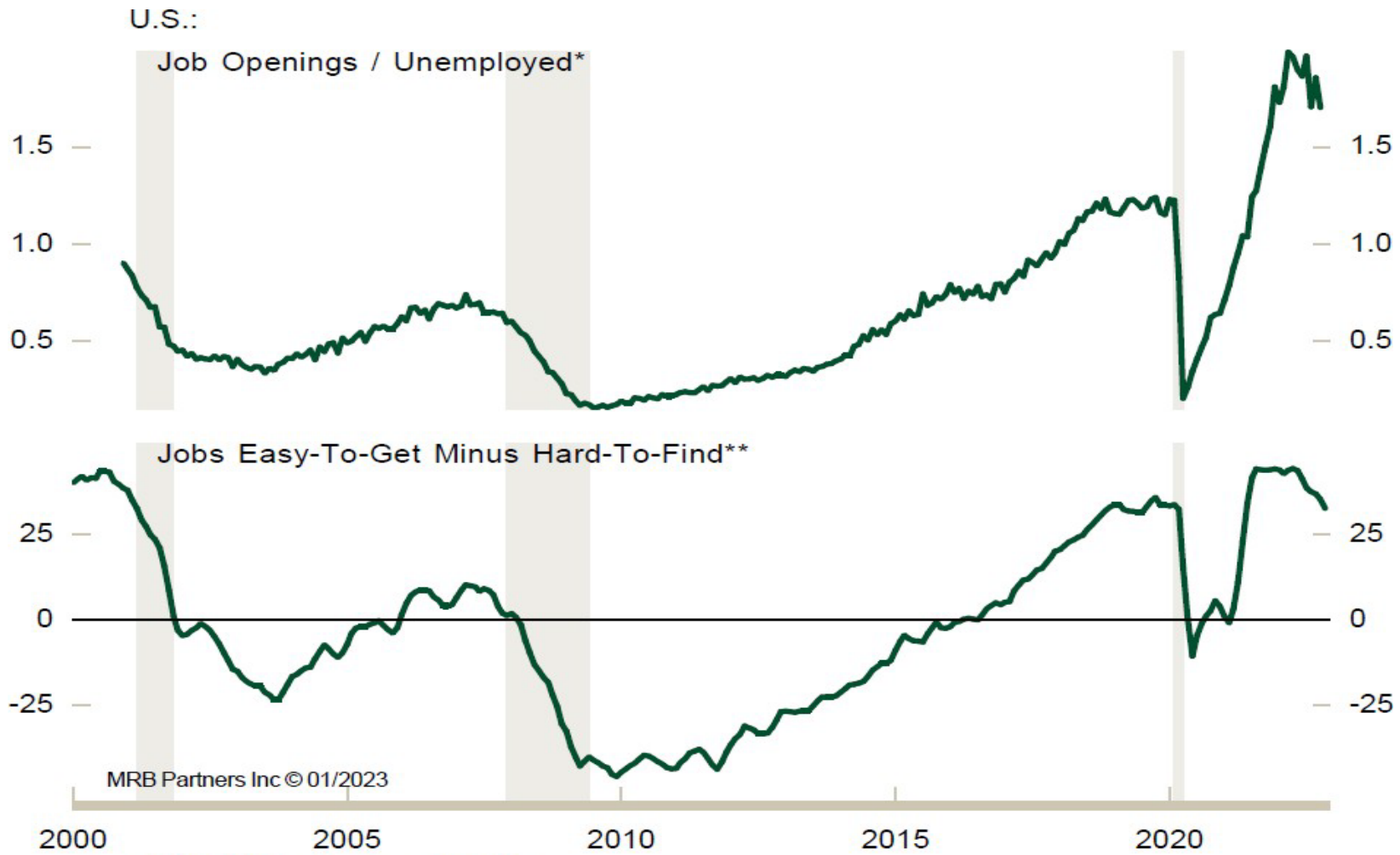
Global Manufacturing is Slowing



* Smoothed; source: IHS Markit
** Smoothed; source: Macrobond
Note: Shaded for NBER-desingated U.S. recessions

The U.S. Jobs Market Remains Strong but Expected to Soften

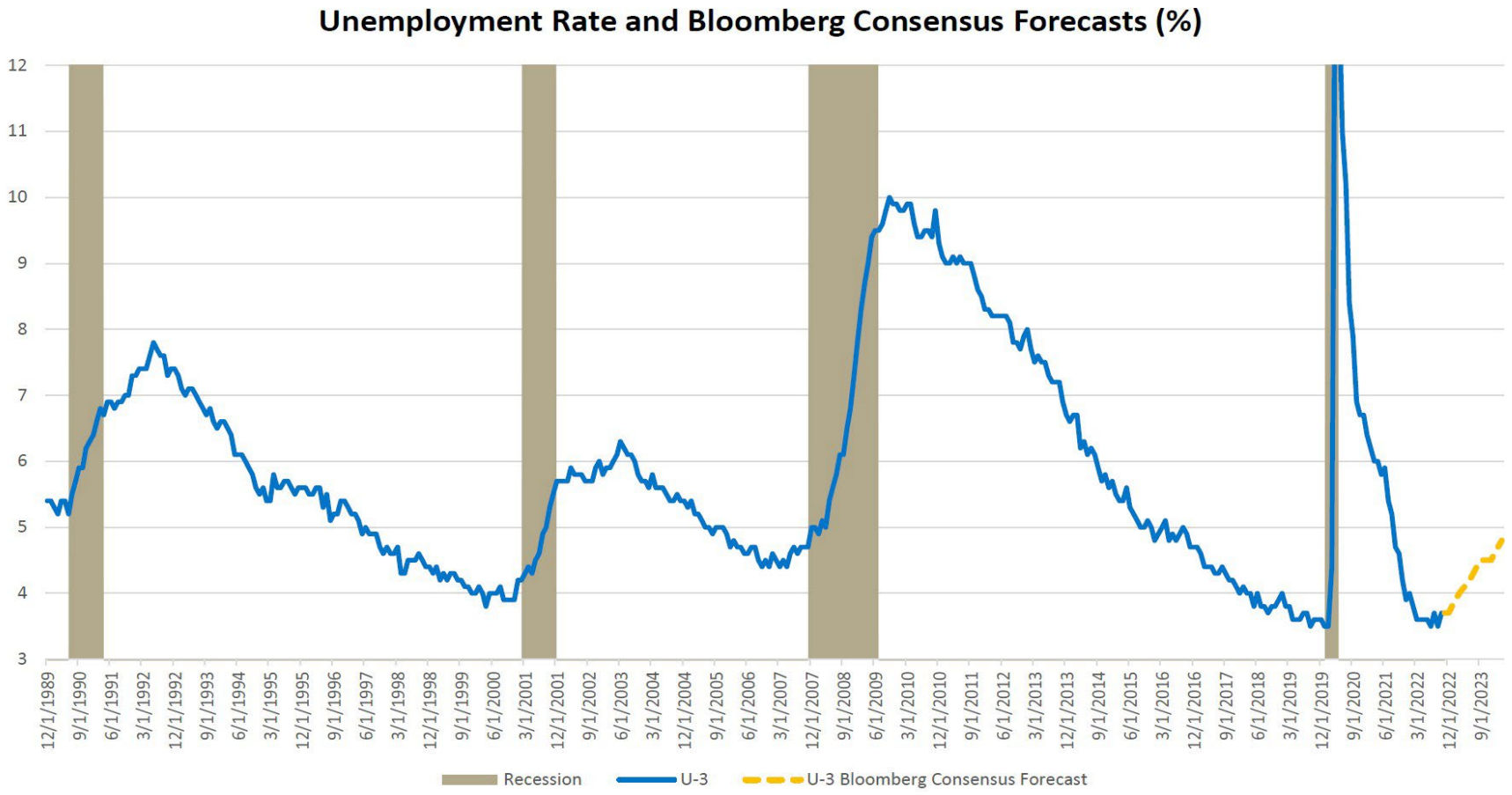
There are still nearly 1.8 job openings for every person looking for work.



* Smoothed; U.S. Bureau of Labor Statistics
** Smoothed; source: The Conference Board
Note: Shaded for NBER-desingated U.S. recessions

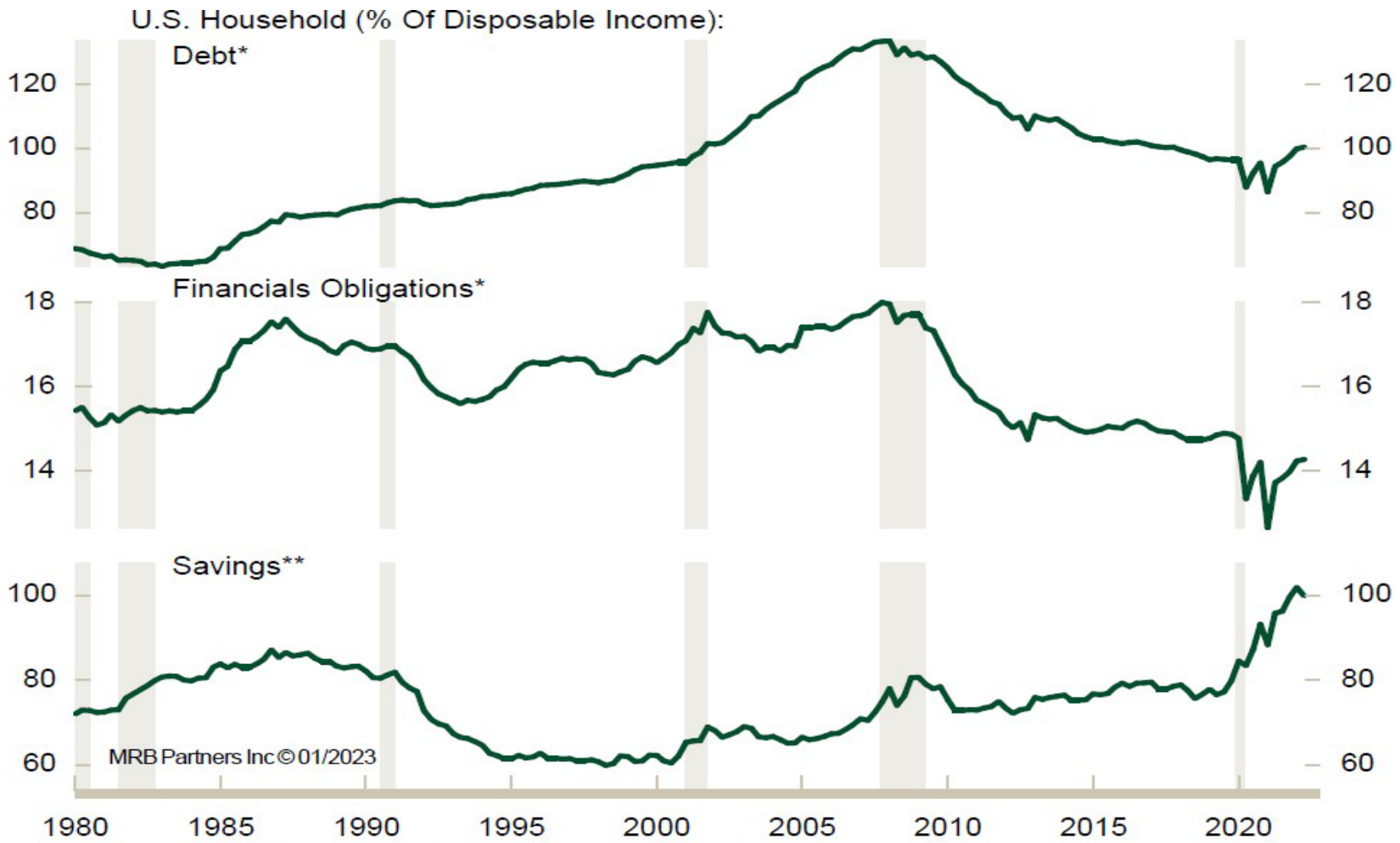
The U.S. Jobs Market Remains Strong but Expected to Soften

The unemployment rate is 3.7% as of November 2022, but expected to increase to around 5.0%.



Source: Bloomberg, DoubleLine

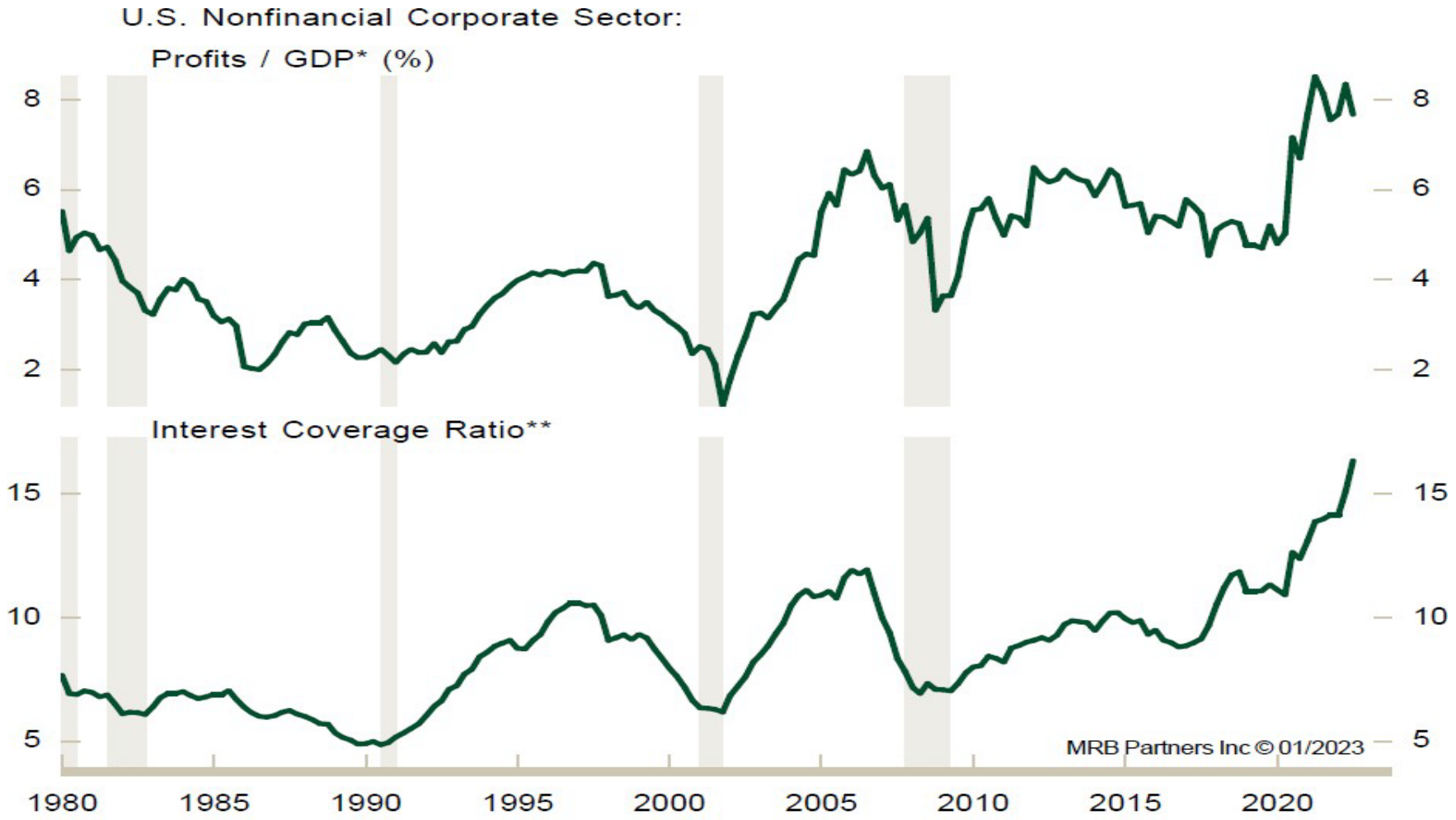
The U.S. Consumer is Financially Healthy But Inflation is Starting to Bite



* Sources: Federal Reserve and Bureau of Economic Analysis
** Checkable and time deposits, short-term investments and money market funds
Note: Shaded for NBER-designated U.S. recessions

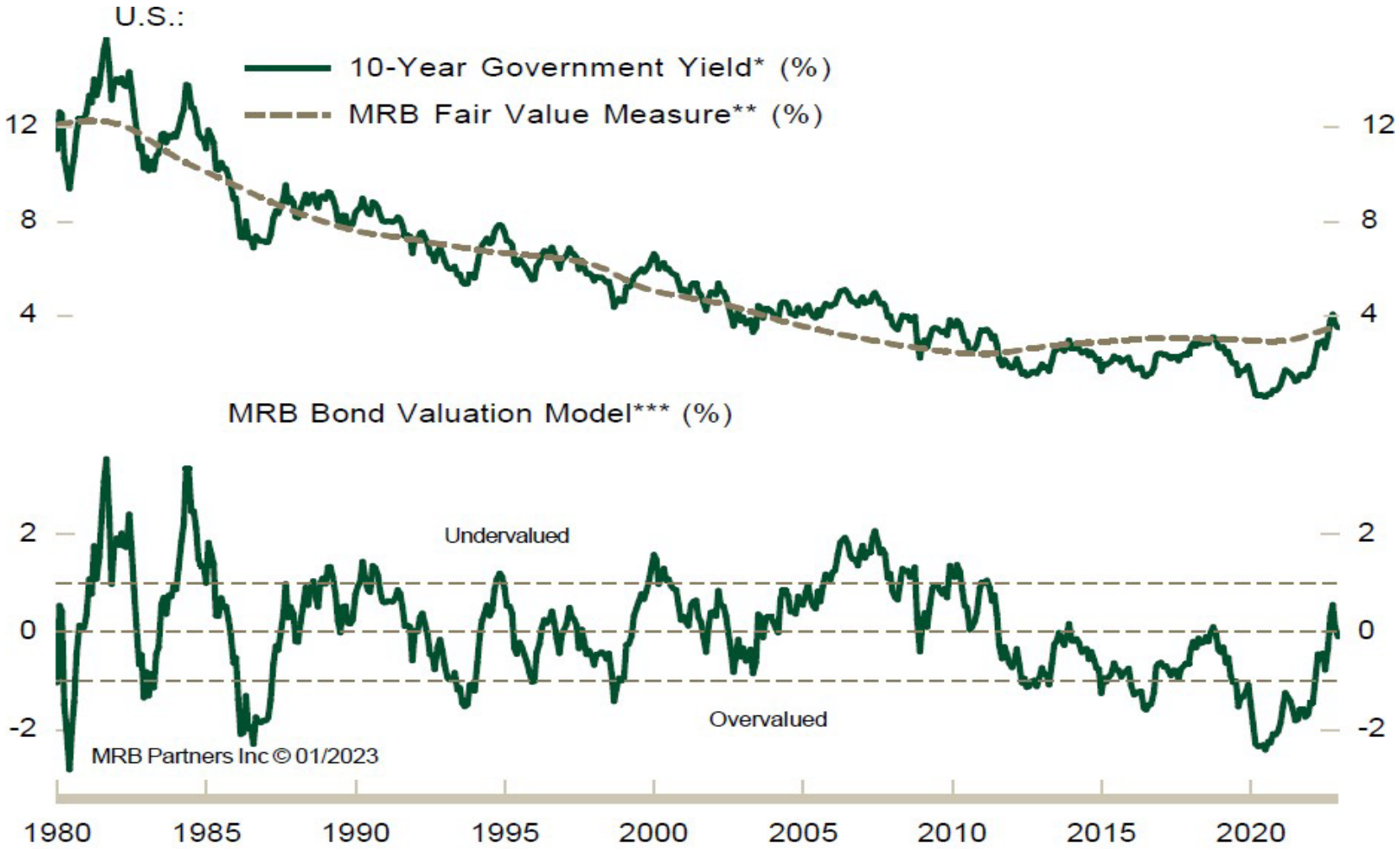
Corporate Finances Remain Solid

Refinancing at higher interest rates will create challenges down the road.



* Source: U.S. Bureau of Economic Analysis
** Earnings before interest, taxes and depreciation relative to miscellaneous interest expense
Sources: U.S. Bureau of Economic Analysis and Federal Reserve
Note: Shaded for NBER-desingated U.S. recessions

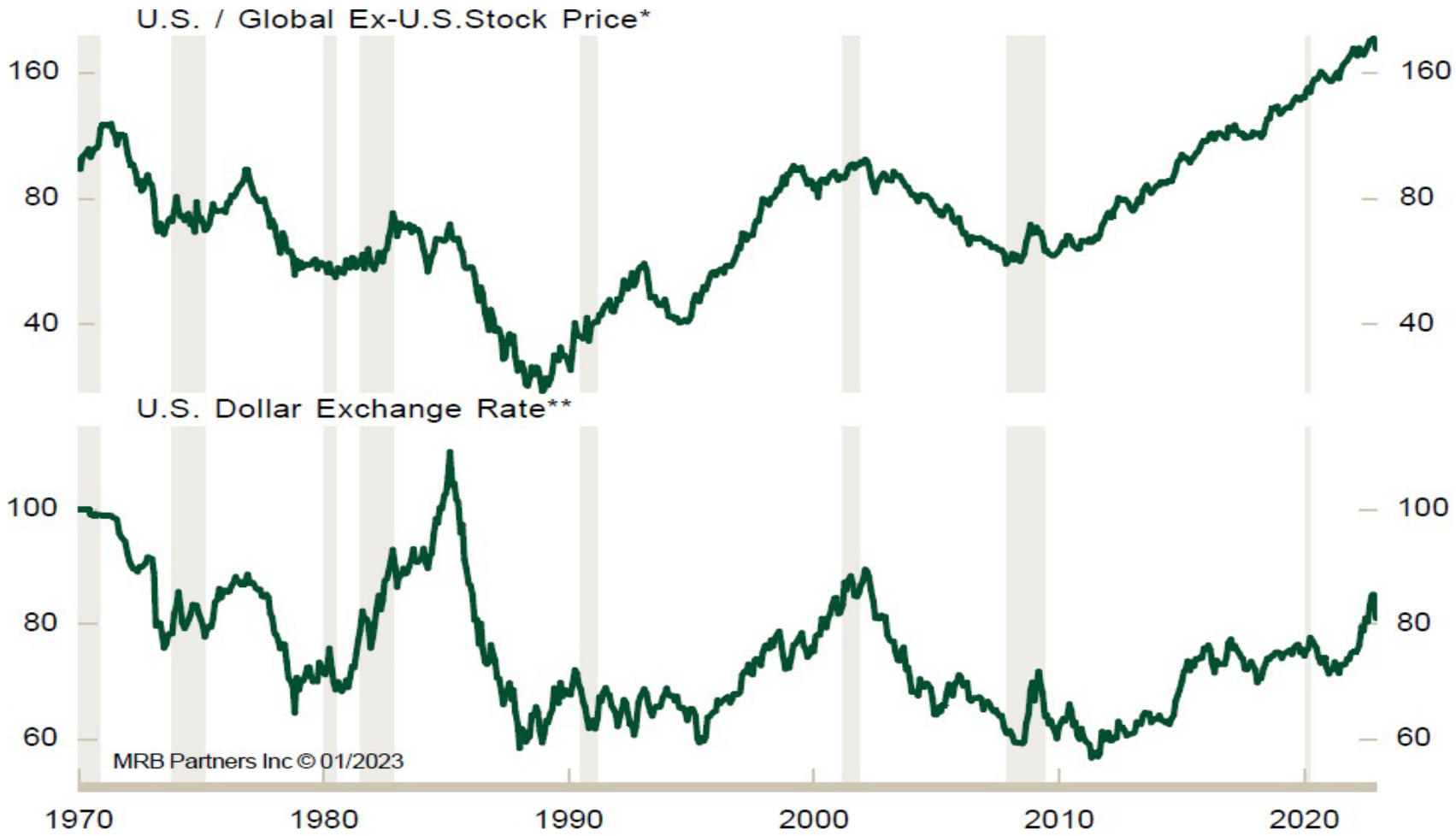
U.S. Treasury Yields Have Risen Significantly And Appear Fairly Valued



* Source: Macrobond
** Includes long-term economic growth and inflation measures
*** 10-year government bond yield minus MRB Fair Value Measure

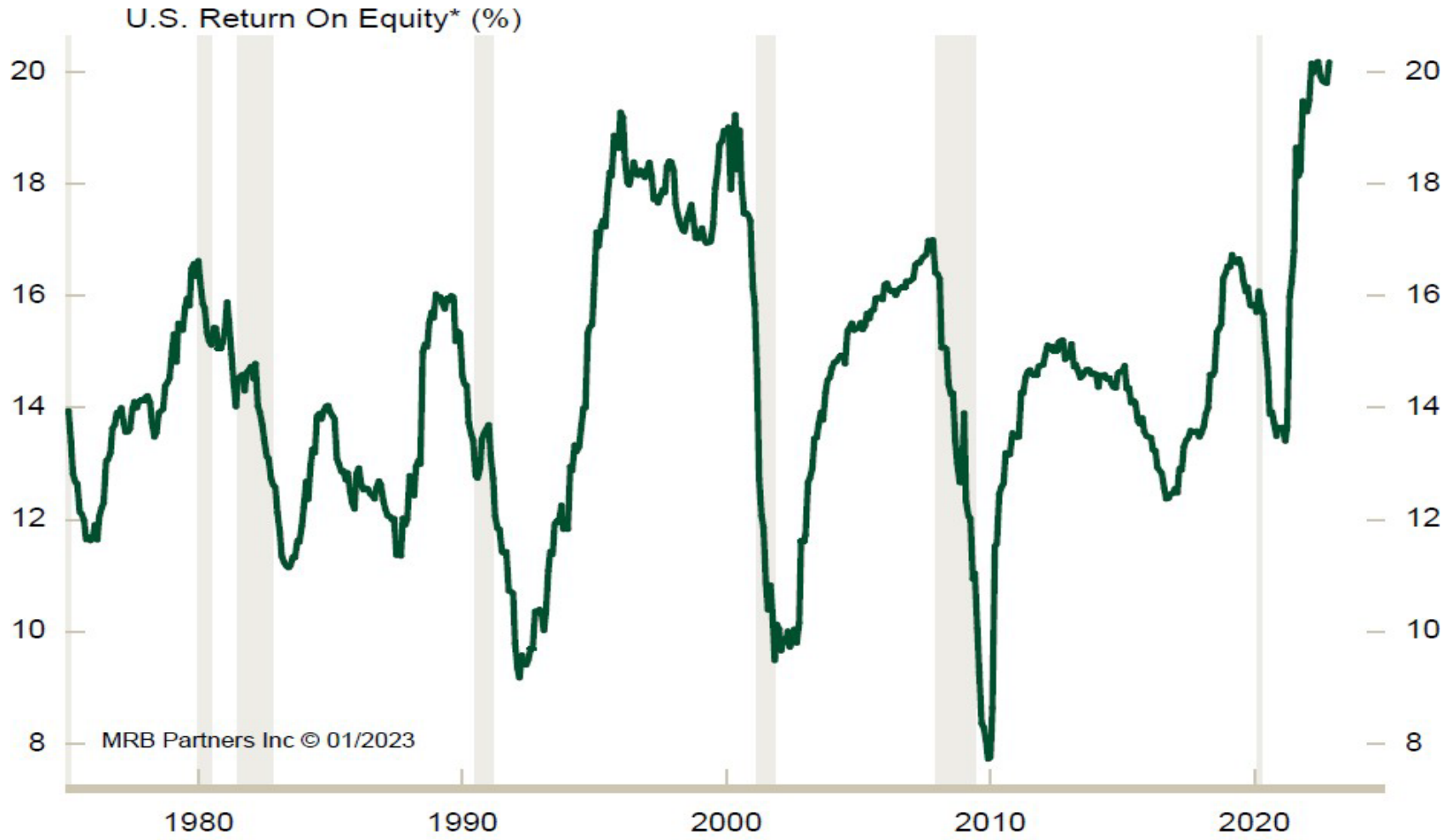
The Dollar and U.S. Relative Equity Performance are Highly Correlated

Stronger global growth would result in a weaker dollar and help international stocks.



* U.S. dollars; rebased; source: MSCI
** Weighted dollar index; source: MSCI
Note: Shaded for NBER-desginated U.S. recessions

Elevated Return on Equity Signals Risk for U.S. Stocks



* Source: MSCI
Note: Shaded for NBER-desingated U.S. recessions

Key Considerations

- The U.S. and global economies are slowing as central banks remove fiscal accommodation and fight inflation.
- Tighter monetary policy in the U.S. will likely lead to a recession and a further decline in risky assets in anticipation of a recession at some point in 2023 or 2024. Corporate profits/margins will come under pressure. U.S. inflation should continue to slow, but not quickly enough to avoid an economic downturn. The Federal Reserve will likely remain restrictive too long.
- If a recession does occur it will likely be mild because we are starting with strong employment, no obvious private sector imbalances and excess savings that have accumulated over the course of the pandemic. Idaho would likely see less of an impact given its economic vitality.
- Equity prices are likely to fall further if we have a recession. Longer-term investment returns are expected to improve, however, due to higher bond yields and more attractive equity valuations.
- Chinese policymakers recently announced plans to abandon the COVID-zero policy and may ease other policies in 2023 to support the economy. It remains unclear whether these policies will merely stabilize economic activity or result in a significant acceleration in growth.
- Europe is facing stronger near-term headwinds than the U.S. economy, but stabilization of energy markets would provide a strong catalyst for improvement. Germany is investing in floating LNG terminals and considerable investment is being made across Europe in renewable energy. A resolution to the war in Ukraine would be very beneficial.
- Geopolitical tensions with Russia and China remain an important wildcard.