Verger Responds to Key Questions
March 31, 2020

1. What is Verger's level of comfort with liquidity in client portfolios and the underlying managers? What about the liquidity of the overall markets?

We are comfortable with the liquidity available to meet client needs. While we are exercising prudence, we have been diligent in building a portfolio over the past several years that provides ample liquidity and allows us to exploit opportunities as they present themselves. Additionally, the hedge overlay strategy utilized at Verger Capital Management (Verger) has produced cash as we have been actively monetizing many of our hedge positions over the past few weeks[1]. We are in frequent contact with our managers who are performing as expected and have not indicated any concerns with their own liquidity. We have also used the price dislocation in certain markets as an opportunity to fund new managers and strategies. One example of our ability to move quickly is an investment we completed with a manager that invests in closed-end debt funds where the underlying assets are trading at significant discounts to the underlying net asset value. This opportunity similarly presented itself in the wake of the 2008 financial crisis and our close relationship with the manager is allowing us to move quickly and take advantage of the dislocation while it lasts. We believe this investment provides us with the unique opportunity to earn equity-like returns with credit-like risk. In addition, we have added capital to one of our long/short equity managers as we believe this to be an attractive entry point. We feel confident that our existing private managers who have dry powder will be opportunistically calling capital to make new investments at attractive prices as many markets have re-priced.

Unlike the crisis of 2008 – 2009, we are not seeing the deterioration of liquidity in the broader markets, and the Fed (having learned from the last crisis) is working hard to keep things moving in an orderly fashion. While liquidity has not been an issue thus far, we will continue to monitor and make adjustments as needed.

2. If you needed cash right now, what would you sell?

Verger's managed portfolios have a strong liquidity position allowing access to capital across all major asset categories including equities, absolute return, real assets, and fixed income. This allows us to maintain our long-term strategic asset allocation targets and continue to shift capital to assets we feel are undervalued and take profits from areas where we have seen strong gains. As an example, we recently took profits from a long-duration treasury manager which experienced strong gains as U.S. Treasury yields saw deep moves downward (Source: Bloomberg).

[1] There can be no assurance that risk management techniques or hedging strategies will be successful in reducing risk and they may involve significant expense. The success of any hedging strategy will depend in part on the investment manager (or the manager of an underlying fund or a sub-adviser) to correctly asses the degree of correlation between the performances of the instruments used in the hedging strategy and the performance of the investments being hedged.

3. **What changes has Verger made to positioning and to allocation?**

    Verger has not made any major re-allocations or re-balancing shifts at this time, but we are carefully watching how things evolve and have made some changes at the margin. These changes include the monetization of some of our portfolio hedge positions and paring back some positions that fared particularly well during the sell-off and have limited potential for additional upside (managed futures, long-duration U.S. Treasuries). We are opportunistically funding new strategies and allocating additional capital to existing strategies that look attractive due to recent price dislocations. As we would expect in this environment, certain strategies and portions of the portfolio are participating in the market drawdown, however we continue to have conviction in our underlying managers and our overall strategy.

4. **What changes are your managers making? Are underlying managers adding risk or de-risking? What opportunities are managers seeing as result of the sell-off and the widening of spreads?**

    While no one could anticipate a global pandemic, Verger's investment philosophy is founded on a portfolio designed to perform across all market scenarios. This includes allocating capital to managers across a broad spectrum of investable strategies. We value the opinion of our managers and have been working with many of them to take advantage of the opportunities presented by this crisis.

    Our credit managers are shifting from less-liquid structured transactions to more liquid, high-quality bonds and loans that have re-priced. They are seeing better prospective returns in more liquid securities as compared to before the recent volatility. Over the past decade, many credit managers had migrated to direct primary transactions with corporates due to the unattractive yields available in more broadly syndicated bonds and loans. One large distressed debt manager recently told us they will only look to invest in secondary debt given the current market environment. Managers are focusing on securities backed by companies that they believe are high-quality and will survive the economic turmoil. Managers across the board are increasing their exposure to more liquid securities, as that is where they are seeing the greatest opportunity for the best risk-adjusted return.

    Verger's equity managers, specifically our long/short hedged managers, have historically maintained lower net exposures to the overall markets as they believed valuations were stretched. As the markets have re-rated, some of these managers are now increasing their net exposure given that valuations have come down and prospective equity returns have increased in their models. We agree that prospective long-term equity returns moving forward are likely to be greater than they were a month ago, when the S&P 500 was at an all-time high (source: Bloomberg).

    In energy markets, we have managers with dry powder who are evaluating opportunities in both public and private markets in order to take advantage of the significant distress facing the industry. Oil has fallen below $25/barrel and the debt of many energy companies is under significant pressure (source: Bloomberg). There will likely be many over-levered companies that do not make it through this market turbulence. Oil has been shocked on both the supply and demand side. The world economy has largely shut down, and at the same time OPEC has begun a price war. Our managers are focused on backing the survivors in this carnage. Some banks are unwilling to lend to these companies and thus, capital providers can drive attractive terms at the top of the capital structure. While the near-term environment is sure to be challenging, we believe that as the supply-side corrects and demand comes back, the survivors will enjoy a less competitive market environment.

We remain in close contact with many of our private markets managers as they work with their portfolio companies to minimize the impacts of this crisis. Private equity firms are likely to come under pressure as portfolio companies' revenue and access to debt will be impacted by the current economic downturn. We have generally focused on partnering with firms that are not heavy users of leverage and expect our managers to be able to weather this downturn.

5. **What is Verger hearing from other Endowments, Foundations, and Non-Profits? How are they faring through this turmoil?**

   While most of what we are hearing is anecdotal at this point, it is clear that the implications of COVID-19 are frightening for the entire non-profit community. Institutions with a bias to equity strategies and a higher beta to the overall markets have been the most impacted. We are hearing that some portfolios are down as much as 15% to 20% for the calendar year. Drawdowns of that magnitude are particularly dire for institutions that depend upon their portfolios for a high percentage of their operating capital. The potential for significantly lower distributions from the portfolio paired with the additional loss of income resulting from the suspension of normal day to day activities may prove catastrophic for some institutions. Verger remains committed to protecting our clients' assets and providing for the long term, and the current environment is a reminder of why we built an all-weather, antifragile portfolio.

6. **Are hedge programs working? Going forward are there new hedges/insurance available at reasonable prices?**

   Verger created our hedging strategy to enable investor portfolios to perform in all market environments, including the one we are living through today. The strategy has worked during the sell-off, allowing us to monetize many of the hedge positions at maximum payout levels while providing cash for liquidity and to reallocate. Historically, we have been able to build out the hedge strategy at very low cost, but with the recent spike in volatility it has been more difficult to build additional downside protection at reasonable prices. Although we haven't been able to fully replace our previous positions due to cost, we have started to build our protection level back up. Additionally, we are working to identify other indirect hedges that could be more cost effective. We continue to watch the markets closely and if we see a sustained rally or decrease in volatility, we anticipate reloading more of these hedges.

7. **Does the current market environment impact your long-term view or risk profile? Does it change how you think about liquidity?**

   Our long-term views and approach have not changed. We are not making changes to our risk or liquidity profile. As markets have significantly re-rated across the board, we are now seeing opportunities where we believe we can generate equity-like returns with credit-like risk. This is an area of interest that we will continue to spend time on. We are actively talking to our network of managers in the distressed debt space, where we are hearing there is now $1.5 trillion of debt trading at distressed prices. Our managers believe this will be a sustainable long-term opportunity. There is stress across the board in credit as investment grade bonds, securitized products, mortgage-backed securities and others are seeing significant pressure from forced selling. Our approach will remain consistent. We seek to take advantage of this distress by being a liquidity provider to forced sellers. We believe we have a strong existing manager roster that is actively taking advantage of the current opportunity set and we are staying in close contact with these partners. We may also add additional specialists in areas that we believe can provide strong risk-adjusted returns going forward.

8. **Is it your view that this is a terrible shock which will be followed by a V shaped recovery – or will it be more L or U shaped?**

   While we are always hesitant to prognosticate on the direction of markets, we do not believe this is a scenario that will be resolved overnight. It is our view that more economic pain will be felt in the coming months as companies report their earnings and job losses get tallied. The disruption caused by COVID-19 will likely have long-term implications, but in the short-term, it creates the opportunity to buy assets at much lower multiples than prior to the sell-off. A positive byproduct of this re-pricing is increased return expectations in those assets going forward. That said, uncertainty with regard to the timing of the recovery means that it is important to be an investor at this point, with a longer time horizon, rather than a speculator with expectations of short-term price recovery. Regardless of the timing or shape of the recovery, we believe Verger and our clients are well positioned to weather the current storm and benefit from the ultimate recovery.

9. **What is Verger most focused on near-term? What has changed, if anything, with regard to your long-term views?**

   In the short-term we are focused on tactically taking advantage of opportunities as we see them. Our strong liquidity position and monetization of portfolio hedges have provided us dry powder to prudently deploy capital. We remain committed to maintaining strong lines of communication with our current managers and partners as we look to them to help us evaluate the opportunity going forward. Perhaps most importantly, we remain committed to supporting our clients and keeping them informed as we navigate the volatility created by this global pandemic. Although our view on short-term market remains fluid, our longer-term view is to adhere to our mantra of Protect, Perform, Provide, while providing our clients with an all-weather portfolio designed to endure through all markets.

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Verger's investment philosophy, Protect, Perform, Provide, not only considers return objectives, but also focuses on the reduction of downside risk and portfolio volatility in order to support the long-term needs of an institution that is designed to provide for its constituents in perpetuity. We believe this approach may deliver an investment portfolio that offers high risk-adjusted returns, low volatility, significant downside protection, and the comfort of more predictable and repeatable distributions to fund operations. Our focus in this current environment is on Protect, and our whole team is working to ensure that our clients get through this difficult time well-positioned to continue to support their respective missions in perpetuity.

Verger remains available for ongoing support as questions and needs arise. For more information, please contact:

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