Profile of Katrina Butt ’13

Bucknell’s focus on the undergraduate experience allows students to gain hands-on exposure to finance and investing, even while studying miles from Wall Street. I am an economics and mathematics double major, and have augmented my core studies by participating in the experiential Student Managed Investment Fund (SMIF) course and also by working as an executive intern in the Endowment Office.

Created in 2006, Bucknell’s Undergraduate Executive Internship Program allows students to work alongside senior administrators, gaining professional experience within various areas of the University. Working in the Endowment Office for the past two years, I have contributed to various projects, including creating endowment asset manager profiles, conducting research on asset classes and investment strategies, and assisting in ongoing due diligence of existing managers. The opportunity to work beside financial professionals as an undergraduate while gaining an inside view of the University’s investments and financial position has been a unique and invaluable experience.

I am also a student analyst in SMIF, a two-semester course that provides experience in securities analysis and portfolio management by allowing students to manage approximately $1 million of Bucknell’s endowment. The students determine the asset allocation based on overall economic and market forecasts and then select individual securities based on a fundamental research process. When determining investment selections, students engage in global economic analysis, research of specific industry trends and econometric modeling, and conduct an in-depth study of management strategy and equity valuation. The course also allows students to improve negotiation, communication and leadership skills through collaboration and generation of investment decisions. The fund not only provides an avenue for real-world application of portfolio theory for students, but also adds incremental return to Bucknell’s endowment allowing students to manage approximately $1 million of Bucknell’s endowment. The students determine the asset allocation based on overall economic and market forecasts and then select individual securities based on a fundamental research process. When determining investment selections, students engage in global economic analysis, research of specific industry trends and econometric modeling, and conduct an in-depth study of management strategy and equity valuation. The course also allows students to improve negotiation, communication and leadership skills through collaboration and generation of investment decisions. The fund not only provides an avenue for real-world application of portfolio theory for students, but also adds incremental return to Bucknell’s endowment.

The broad and rigorous liberal arts education at Bucknell allows students to gain critical thinking, communication and analytical skills. These additional opportunities allow students like me to gain practical experience and apply their knowledge to add value to the University. Through internships in the Endowment Office and participation in SMIF, we can contribute to the overall success of Bucknell.

A Message from the Chief Investment Officer

Tail Risk

Following the credit crisis of 2008, the term “tail risk” took on a more prominent role in the lexicon of the investment world. In a normal environment, financial assets like stocks and bonds have an expected range of rates of return, impacted by inflation, interest rates, corporate profits and other factors. The extreme upper and lower ends of this normal range of expectations can be described as the “tails” – where returns are much better than expected, or as was the case in 2008, much worse than expected.

Following that crisis, the asset-management community quickly engineered new product offerings and investment funds, offering investors the opportunity to reduce or eliminate the “left” tail – that big negative hit to returns. For a fee, of course.

These products are essentially supposed to act like insurance policies. Similar to homeowners, auto or life insurance, they attempt to provide a return when something bad happens. Unfortunately for investors, many of these tail-risk products haven’t worked out as advertised – they have ended up costing much more than expected and in some cases failing to provide the anticipated protection from market losses.

As we approached the fall of 2012, the Investment Committee of the Board of Trustees had concerns about how a number of events might negatively impact the endowment fund, most notably the elections and political transitions in the US, Europe and Asia. Rather than using one of the expensive new products in the market, we tapped into the Committee’s expertise in the field of stock options.

Stock options are financial instruments that enable investors to gain or reduce exposure to an asset class or a specific security by using less money than it would cost to own the underlying security. Specifically for Bucknell, we were able to design an options strategy to provide downside protection for $50 million of our US equity portfolio through the end of the year. By using options, we were able to avoid disruption with our US equity managers, while still temporarily reducing exposure to the asset class. At the end of the year, the market did not react negatively to the global events, and our insurance policy only cost 0.06% to our return - significantly less than it would have cost to use an external service.

Bucknell is fortunate to have a breadth of expertise on the Investment Committee to advise the Investment Office on a broad array of asset classes. Their balance of thoughtful asset allocation, risk management and long-term thinking has enabled the endowment fund to meet its obligations to the University by making payments in excess of $30 million during 2012.

In an uncertain world of deficits, debt and underemployment, we will continue to keep risk management, including tail-risk management, as a critical component of our investment decision-making.

'Ray Bucknell!

Christopher D. Brown ’81, CFA
Chief Investment Officer
Commentary for the six months ended December 31, 2012

The fiscal year began with a number of political events on the calendar in the US and abroad, including a US presidential election, Japanese general elections and a once-in-a-decade leadership transition in China, to name a few. Despite these political uncertainties, equity markets rallied behind improving global growth and continued monetary intervention by global central banks. In the third quarter the Federal Reserve launched an open-ended, $40 billion-a-month bond-purchase program. At the same time, European equity markets rallied on European Central Bank (ECB) President Mario Draghi’s announcement of a new bond-buying program that allows the ECB to make unlimited interventions in the sovereign debt markets. Finally, in December Japanese equities rallied sharply amidst hope that political change could lead to dramatic monetary policy changes that could end the economic deflation that has plagued Japan for decades.

- For the six months ended 12/31/12, US equities as measured by the S&P500 index returned a positive 5.95 percent. Smaller-capitalization US equities slightly outperformed, with the Russell 2000 index up 7.20 percent over the same period. Master Limited Partnerships (MLPs) were up 5.14 percent, slightly underperforming the broader equity market amidst heightened uncertainty regarding the 12/31/2012 fiscal cliff and potential changes to the tax code.

- Non-US equities posted double-digit returns as the Morgan Stanley international equity index (MSCI ACWI ex US) finished up 14.09 percent and the emerging-market equity index up 13.95 percent. Emerging-market debt also netted a double-digit return, gaining 10.32 percent as measured by the JP Morgan EMBI index.

- US Treasury bond yields remain at historic lows, with yields on two-year and 10-year bonds at 0.25 percent and 1.78 percent, respectively. Six-month total returns on US investment-grade corporate and high-yield fixed-income securities were approximately 1 percent and 8 percent, respectively.

- Hedge funds as measured by the HFRI Fund of Funds index were up approximately 4 percent over the six-month period, as managers broadly underperformed the global equity rally. Pockets of strength included residential mortgage credit that benefitted from expectations of an improving US housing market.

At December 31, 2012, Bucknell’s endowment fund was valued at $625.3 million, up from $599.2 million at June 30, 2012. Over the six-month period, distributions totaling $15.9 million were transferred out of the endowment to help support current scholarships, grants, athletics and other University operations. The fund received gifts and transfers of $9.3 million and had net investment gains of approximately $33.0 million.