A Message from the Director of Investments

John F. Kennedy once said, “Change is the law of life, and those who look only to the past or present are certain to miss the future.” Though at times uncomfortable and unnerving, change is one of the few constants that we have in life, and there was no shortage of it in the financial markets during the first half of our 2015-2016 fiscal year.

The most notable of these changes was the Federal Reserve’s transition away from its accommodative interest rate policy in December, marked by the first increase in the level of borrowing rates in nearly a decade. Though the statistical sample of US interest rate hiking cycles is actually small, these cycles have historically been associated with an improving economy coupled with increasing inflationary pressures. This time the change in policy has come amid an uncertain fundamental economic backdrop, and has stoked increased trepidation among investors and increased volatility in global financial markets.

Oil prices accelerated their downward trajectory, with West Texas Intermediate ending calendar year 2015 below $40 per barrel (and precipitously declining to less than $30 shortly thereafter). This is a far cry from the $100-per-barrel prices witnessed just 18 months ago, which preceded OPEC’s now-infamous November 2014 decision to maintain current production levels in the face of declining market share usurped by a burgeoning US shale oil industry. The transition toward low energy prices has stressed all market participants, from small upstream oil and gas drillers to nations whose balance sheets and social welfare programs depend on exporting high-priced oil. These stresses have also spilled over to the creditors who lent so generously to the energy sector over the past few years. While indiscriminate repricing of most energy assets may present opportunities, we are mindful that many higher-cost energy assets may be permanently impaired in a lower energy price paradigm.

The current economic expansion is now one of the longest in US history. Financial media contributors often point to this fact with the implied question, “When will the party come to an end?” Fortunately, bull markets do not die of old age, and we continue to focus on disciplined long-term investing. The discipline element of our process requires that we focus on high-quality investments that can be purchased at attractive prices. While it has been challenging to identify assets trading at attractive prices recently, one of the advantages of falling prices is more-attractive valuations. We have significant dry powder in the form of cash in the portfolio to take advantage of these opportunities as we identify them moving forward.

Alongside the changes in the capital markets, we also welcomed some changes in the Investment Office during the first half of fiscal year 2016, including a new colleague, Angela Motto, who joined the University in August as our new Investment Operations Analyst. Change often brings opportunity, and with the guidance and expertise of the Investment Committee of the Board of Trustees, we will continue to focus on capitalizing from change to protect and enhance the endowment fund for the benefit of all generations of Bucknellians.

'Ray Bucknell!

John Luthi ’04
Director of Investments
Bucknell’s Student Managed Investment Fund (SMIF) is a unique yearlong course offered within the School of Management. This course gives approximately 20 curious and motivated seniors the opportunity to learn firsthand what it is like to work on an investment management team and co-manage a portfolio. Led by Professor Robert Needham and Professor David Jensen, SMIF gives students the opportunity to actively invest about $1,500,000 of Bucknell’s endowment.

In the fall of 2000, Lee Idleman ’54 provided the initial capital to seed this exceptional learning opportunity for Bucknell students. An endeavor of this kind at the undergraduate level is atypical at universities and was revolutionary in the early 2000s. After that initial donation, a variety of alumni recognized the real impact that this opportunity made on the students and continued to contribute to provide ongoing support and expansion of resources.

To begin each year, students create a market forecast to inform how the portfolio is allocated among equities, fixed income and alternative investments (equities typically comprised the majority of the portfolio, given the perpetual nature of Bucknell’s endowment). Throughout the year, each student is responsible for monitoring specific portfolio holdings as well as pitching a new stock idea that they believe should be added to the portfolio. “This is the first kind of project I’ve ever done that really incorporates almost everything I’ve learned over the years at Bucknell,” says Emily Dafilou ’16. In fact, it is precisely the comprehensive and targeted prerequisite course load that allows the SMIF program to be student managed, according to Professor Needham.

The stock pitch represents the culmination of a student’s SMIF experience and requires several days of research and preparation using University and alumni-supplied research tools (e.g., Bloomberg terminals) in order to bring a comprehensive recommendation to a classroom of peers. Classmates are similarly prepared to offer their perspective and devil’s advocate-style questions in order to ensure that this potential new investment is truly in the best interest of the portfolio from a risk and return perspective. Max McKelvy ’16, a member of SMIF, notes, “Disagreement is a good thing for the class; it sparks discussion and offers needed perspectives.” These conversations tend to engage the entire class, as all portfolio changes use a democratic process and require a two-thirds majority student vote.

In addition to the intense and thorough investment management experience gained through participation in the SMIF course, students also have the opportunity to hear from and network with Bucknell alumni who have made careers in the investment industry. This added benefit of the SMIF experience is particularly important given that the majority of SMIF students have gone on to careers in investment and finance, and the interaction with alumni helps to narrow down their career aspirations to specific fields within this sector.

Bucknell’s Student Managed Investment Fund has grown and evolved considerably over the last 16 years as a result of its professors’ dedication and vision, its students’ ambition, and its donors’ generosity of time and financial support. Like many other programs on campus, the SMIF course embodies the unique and rewarding challenge that is a Bucknell education.

Helen Weston ’16, economics and political science, is the Undergraduate Executive Intern for the Bucknell Investment Office.
Commentary for the Six Months Ended Dec. 31, 2015

Our Endowment is comprised of four broad asset groups (Growth, Hybrid, Real Assets, and Low Volatility) which contain several sub-asset classes.

Growth Assets
Large cap US stocks led the Growth Asset category as the S&P 500 posted a return of 0.2% during the six-month period. Small cap US equities, foreign developed market equities and emerging market equities all experienced varying degrees of negative performance as a confluence of concerns such as Federal Reserve interest rate increases, plunging oil prices, and potential slowdown in Chinese economic growth weighed on investor sentiment.

Hybrid Assets
True to their role in the portfolio, Hybrid Assets provided some ballast during the first six months of the fiscal year. Bucknell’s Hybrid portfolio is comprised mostly of a collection of hedge funds constructed to offer attractive risk-adjusted returns with limited correlation to traditional stock and bond markets. Bucknell’s hedge fund portfolio protected Endowment value as many equity investments fell significantly. The remaining portion of the Hybrid Portfolio is represented by credit investments, which faced headwinds during the period as expectations for higher borrowing rates from the Federal Reserve and higher default rates among stressed energy producers unnerved high yield, bank loan, and emerging market debt investors.

Real Assets
Real Assets are meant to provide diversification, current income, and a hedge against inflation. During the first half of the fiscal year, we witnessed a significant deflationary environment within commodities (e.g., oil) that negatively impacted Bucknell’s Real Asset portfolio. Broad commodities declined 32.7% during the period, which continues to stress the balance sheets and equity values of many energy and materials companies. Real estate was one of few Real Assets that posted positive returns over the period.

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Representative Index</th>
<th>Fiscal Year-to-Date Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate</td>
<td>FTSE NAREIT All Equity REITs</td>
<td>8.7%</td>
</tr>
<tr>
<td>US Bonds</td>
<td>Barclays Aggregate Bond</td>
<td>0.7%</td>
</tr>
<tr>
<td>US Large Cap Stocks</td>
<td>S&amp;P 500</td>
<td>0.2%</td>
</tr>
<tr>
<td>Cash</td>
<td>Barclays 1-3 Month Treasury Bills</td>
<td>0.0%</td>
</tr>
<tr>
<td>Hedge Funds</td>
<td>HFRI Fund of Funds Composite</td>
<td>-2.8%</td>
</tr>
<tr>
<td>Foreign Developed Market Stocks</td>
<td>MSCI EAFE</td>
<td>-6.0%</td>
</tr>
<tr>
<td>US High Yield Bonds</td>
<td>Barclays High Yield</td>
<td>-6.8%</td>
</tr>
<tr>
<td>US Small Cap Stocks</td>
<td>Russell 2000</td>
<td>-8.8%</td>
</tr>
<tr>
<td>Emerging Market Stocks</td>
<td>MSCI Emerging Markets</td>
<td>-17.4%</td>
</tr>
<tr>
<td>Energy Infrastructure</td>
<td>Alerian MLP</td>
<td>-24.3%</td>
</tr>
<tr>
<td>Commodities</td>
<td>S&amp;P GS Commodity</td>
<td>-32.7%</td>
</tr>
</tbody>
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Note: the returns shown represent various segments of the financial markets and are not representative of actual Endowment performance.
**Total Endowment Activity**

*Six Months Ended Dec. 31, 2015 (in millions)*

- **$789.4**
  - Market Value
  - June 30, 2015

- **$727.8**
  - Market Value
  - Dec. 31, 2015

- **$5.3**
  - Gifts & Transfers

- **($46.2)**
  - Net Investment Return

- **($20.7)**
  - Spending Withdrawal

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**Low Volatility**

Cash and high quality fixed income investments comprise the Low Volatility portfolio, which is meant to provide the Endowment with stability, current income, and liquidity in order to fund ongoing support to the University. Cash and investment-grade bonds were modestly positive as interest rates on 10 Year Treasury Bonds were little changed from June 30th to December 31st. Though this portfolio is not expected to exhibit near the volatility of other areas of the Endowment, it is not without challenges and risk given that cash instruments yield near zero, traditional bonds offer low coupons and come with significant interest rate risk, and expectations for future inflation remain volatile.