# Missing the Target

## Nonprofits Cope With Mediocre Endowment Returns

By HEATHER JOSLYN and PETER OLSEN-PHILLIPS

The assets held in endowments by foundations and charities grew by only small percentages in 2016 — if at all, according to *The Chronicle*'s survey of 137 organizations. Over time, slow growth could spell trouble for grant makers in particular; they are required by law to give away at least 5 percent of their assets every year. That may mean less money for nonprofits, which are trying to keep up with inflation while also coping with their own sluggish returns.

### MEDIAN RETURN ON INVESTMENT

**-2%**

for groups whose fiscal years end in JUNE

**7% to 9%**

**Return needed** by most nonprofits to keep their operations running smoothly

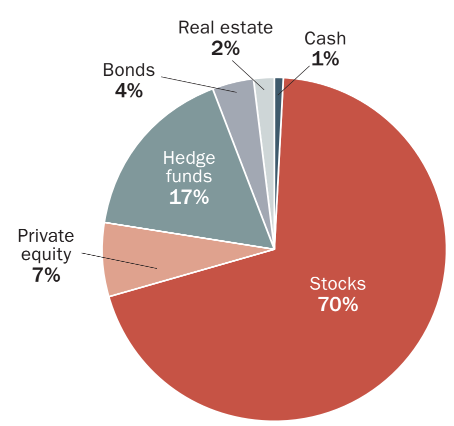
**6%**

for organizations whose fiscal years end in DECEMBER

### STOCKS: FUELING GROWTH

Organizations that have their endowments heavily invested in stocks outperformed those with more diverse portfolios.

**The W.K. Kellogg Foundation,** with a fiscal year ending in August, earned the biggest return on investment among all nonprofits that provided data to *The Chronicle* — nearly 18 percent. Half of its $9.2 billion endowment is invested in Kellogg company stock, with another 20 percent in other public equities.



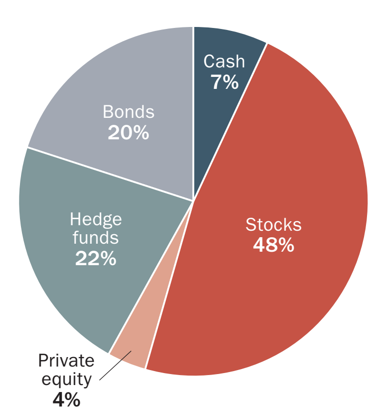

**W.K. KELLOGG FOUNDATION**

**18%**

return on investments

**The American Technion Society** earned a nearly 9 percent return last year, largely because it held 48 percent of its assets in stocks.

The allocation is a big turnaround since 2009, when the group — after losing $72 million to Bernard Madoff's investment fraud — opted for a more conservative mix, with only 30 percent of assets in stocks. Sitting on the sidelines during the long bull market, says Michael Waxman-Lenz, the society's chief financial officer, "hurt us more than Madoff."




**AMERICAN TECHNION SOCIETY**

**9%**

return on investments

### LIVING WITH LOW RETURNS

Taking the risks necessary to get higher returns can also leave an organization vulnerable to big losses during market downturns. "There's only so far you can stretch," says David Villa, board treasurer of the Marguerite Casey Foundation, whose endowment grew nearly 8 percent last year. Instead, endowment experts suggest the following:

**MARGUERITE CASEY FOUNDATION**

**8%**

return on investments

**Reduce management fees.** The Casey foundation brought its endowment-management operations in-house years ago and favors funds that require little day-to-day oversight, like index funds. It pays 40 basis points of its endowment in expenses per year, compared with the average of roughly 90 basis points paid by other nonprofits. (A basis point is equal to 0.01 percent of the endowment.)

**Consider cutting payouts during lean years.** The five-year-old Marion and Henry Bloch Family Foundation, which saw a nearly 8 percent return on its $254.7 million endowment last year, is cautious about overcommitting itself in its grant making in case it faces a down market, says David Miles, the foundation's president.

**BLOCH FAMILY FOUNDATION**

**8%**

return on investments

**Raise more donations.** More than 40 colleges are running capital campaigns with goals of $1 billion or more, according to the Council for Advancement and Support of Education. A large chunk of that money will cushion endowments.

### CHALLENGES IN 2017

**Expensive U.S. stocks:** Many investment experts believe stocks are valued so high, there will inevitably be a fall in the bull market — but nobody knows when. "You don't want to change abruptly," says Joe Curtin, head of global portfolio solutions and institutional investments at U.S. Trust and Bank of America Merrill Lynch. "You don't want to try to time markets."

**Hedge funds in turmoil:** More hedge funds closed than launched in 2016, and several high-profile ones have either shuttered or stumbled in 2017's first quarter. Stanley Ra, investment director at Seattle Children's Healthcare System, where returns grew 9.4 percent with a portfolio allocated 29 percent to hedge funds, says the funds are getting a lot of scrutiny from his peers. "Everybody's asking, Am I getting good value for the fees that I'm paying?"

**SEATTLE CHILDREN'S HEALTHCARE SYSTEM**

**9%**

return on investments

**President Trump's plans:** The new president's efforts to fulfill his campaign promises on taxes, trade, regulation, and more are sowing both anticipation and uncertainty among institutional investors. North Korea and other hot spots could amp up geopolitical risk during the next few years, many investment experts say, and roil world markets.

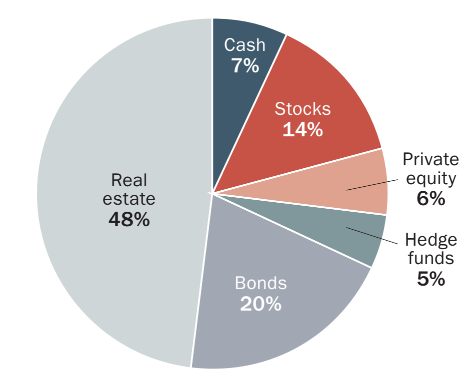
If lower taxes and looser regulation come to pass, expect more capital spending by companies, says Brian Cobb, vice president of the Charles F. Kettering Foundation, whose investments gained nearly 9 percent when its fiscal year ended in December. "There's a lot of pent-up demand," he says, and that spending and improved productivity could drive up returns.

**Slow U.S. growth.** The American economy grew at a rate of only 1.6 percent in 2016 and only 0.7 percent in 2017's first quarter, the weakest quarterly performance in three years.

### OPPORTUNITIES AHEAD

**Real estate.** Loma Linda University earned a 3.6 percent return on investment — the highest among all groups with June fiscal-year ends that provided data to *The Chronicle* — thanks largely to a 48 percent allocation to real estate and mortgage loans. Six years ago, the university began investing in apartment houses and complexes and now owns more than 10,000 units in 10 states.

**International stocks.** Many experts say international and emerging-market equities in Europe, Asia, and Africa are positioned for strong growth and are often inexpensive. Mr. Curtin says nonprofit investors may be too heavily weighted toward stock in highly capitalized American companies because these have performed so well recently.




**LOMA LINDA UNIVERSITY**

**4%**

return on investments

**Impact investing.** Of the 137 organizations in *The Chronicle*'s survey that provided data on their investment strategies, 32 reported that they were tying investments to their missions. That's a proportion roughly akin to the survey's findings in previous years, indicating that the trend has staying power.

**Private equity.** Organizations that can afford to tie up assets for several years are flocking to private-equity funds. High-quality opportunities can be hard to find, however: Christopher Philips, head of Vanguard's Institutional Advisory Services, says that according to some estimates there's more than a $1 trillion in "dry powder" — money earmarked for investment that's not being put to work — clogging the private-equity market.

**NOTE:** Chart percentages may not add up to 100, due to rounding. **SOURCE:** Chronicle reporting