Graystone Consulting
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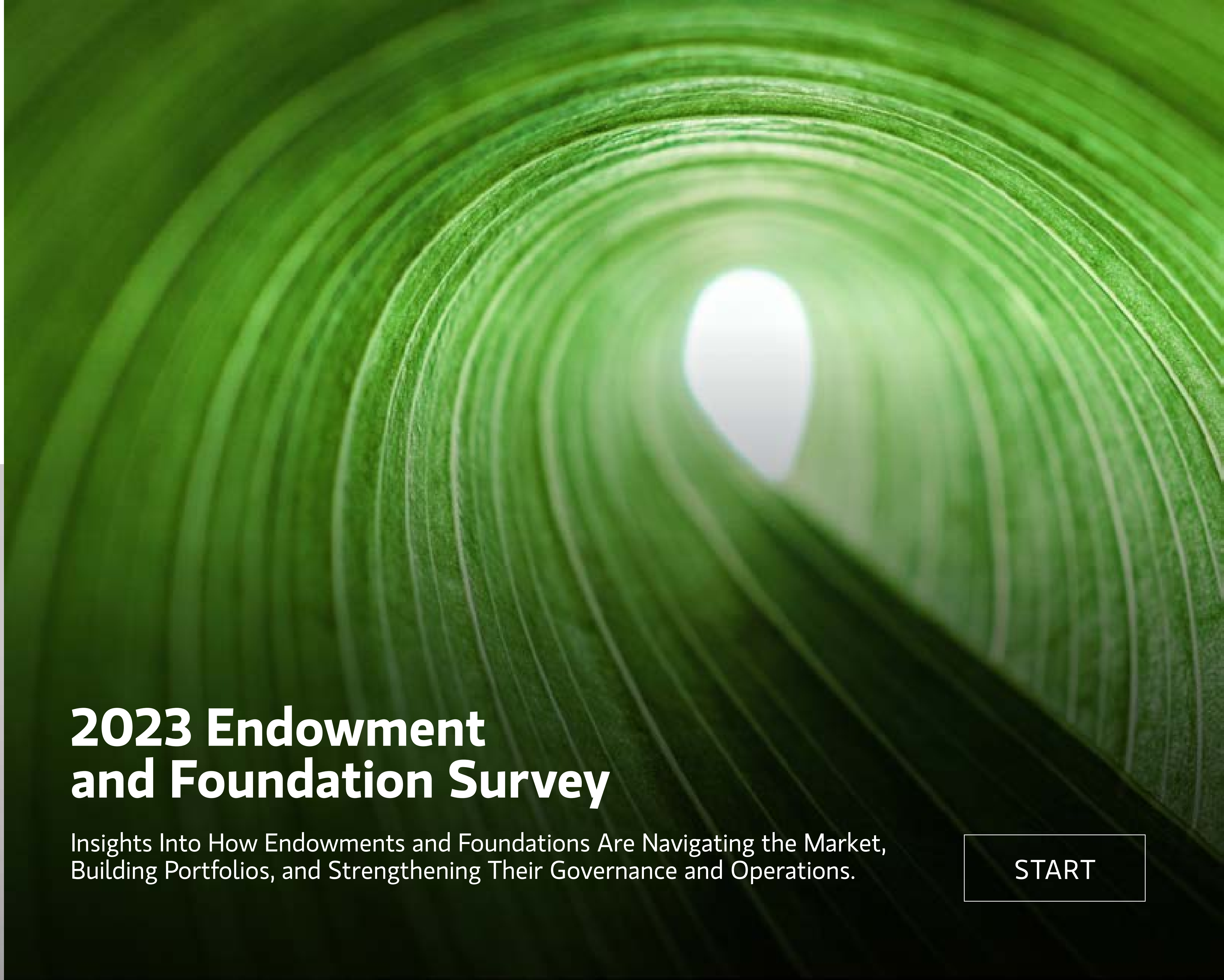


2023 Endowment and Foundation Survey

Insights Into How Endowments and Foundations Are Navigating the Market, Building Portfolios, and Strengthening Their Governance and Operations.

START

Jeremy France
Managing Director
Institutional Consulting Services

Introduction

At Graystone Consulting from Morgan Stanley, one of our core values is putting our clients first. That starts with asking questions about the needs, priorities, and concerns of not just our clients, but of the broader marketplace our clients operate in. This thinking motivated us to conduct our inaugural survey of endowments and foundations.

We serve a wide variety of institutional clients—ranging from endowments and foundations to corporations and Taft-Hartley plans. Every one of them brings their unique set of goals and objectives to the table. Even within a single client segment, we see many different approaches to investing and asset allocation. But what do these institutional investors have in common? Actually, more than you might expect.

For our inaugural survey, we focused on endowments and foundations. We wanted to learn about the worries keeping them up at night and their expectations for the market and economy. In addition to gathering information about portfolio positioning, we explored critical topics such as staffing levels, governance, and more. We plan to expand this initiative to other types of institutional investors in future years.

We're excited to share the results of this research. We welcome the opportunity to talk with you about the findings and how these insights can inform your organization's approach to managing your portfolio and fulfilling your mission.

Thank you,
Jeremy France

In This E-book, We Explore:

Market Environment

Recent market volatility has affected the confidence and dampened expectations of E&F investment teams.

Portfolio Management

Alternatives continue to play a growing role in E&F portfolios, but respondents cite challenges to fully accessing private markets and other alternatives.

Governance, Operations and Staffing

E&Fs anticipate growing their staffs and operations while recognizing the value of training for their boards and investment committees.

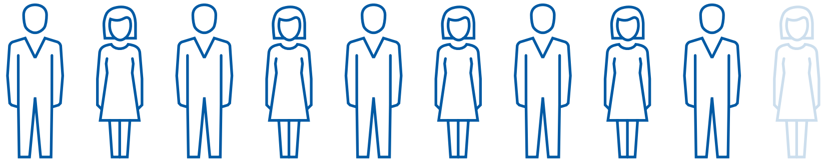
About the Survey

In May 2023, Graystone Consulting surveyed investment decision-makers at 100 endowments, foundations, and other non-profit organizations.[1]

All respondents represented organizations with at least $100 million in AUM, with 56 of them representing an organization with more than $1 billion in AUM.

Respondent Roles

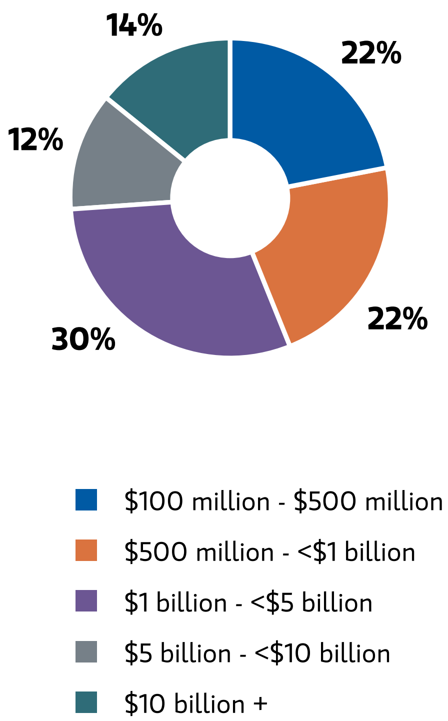
Nine of 10 (89%) respondents hold positions of CIO, Strategy Head, Senior Analyst, or Portfolio Manager



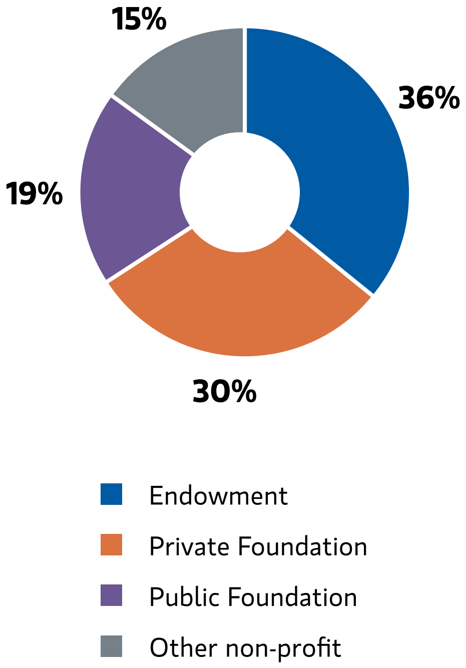
1. The survey was conducted by independent research firm 8 Acre Perspective. Graystone Consulting / Morgan Stanley was not identified as the research sponsor.
2. Base: Endowment or non-profit (n=51). Totals exceed 100% because some respondents selected multiple categories.

Respondent Characteristics

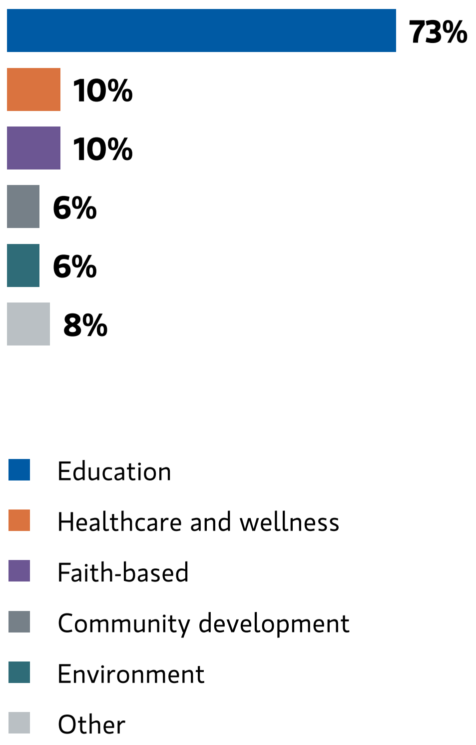
Size - Assets Managed

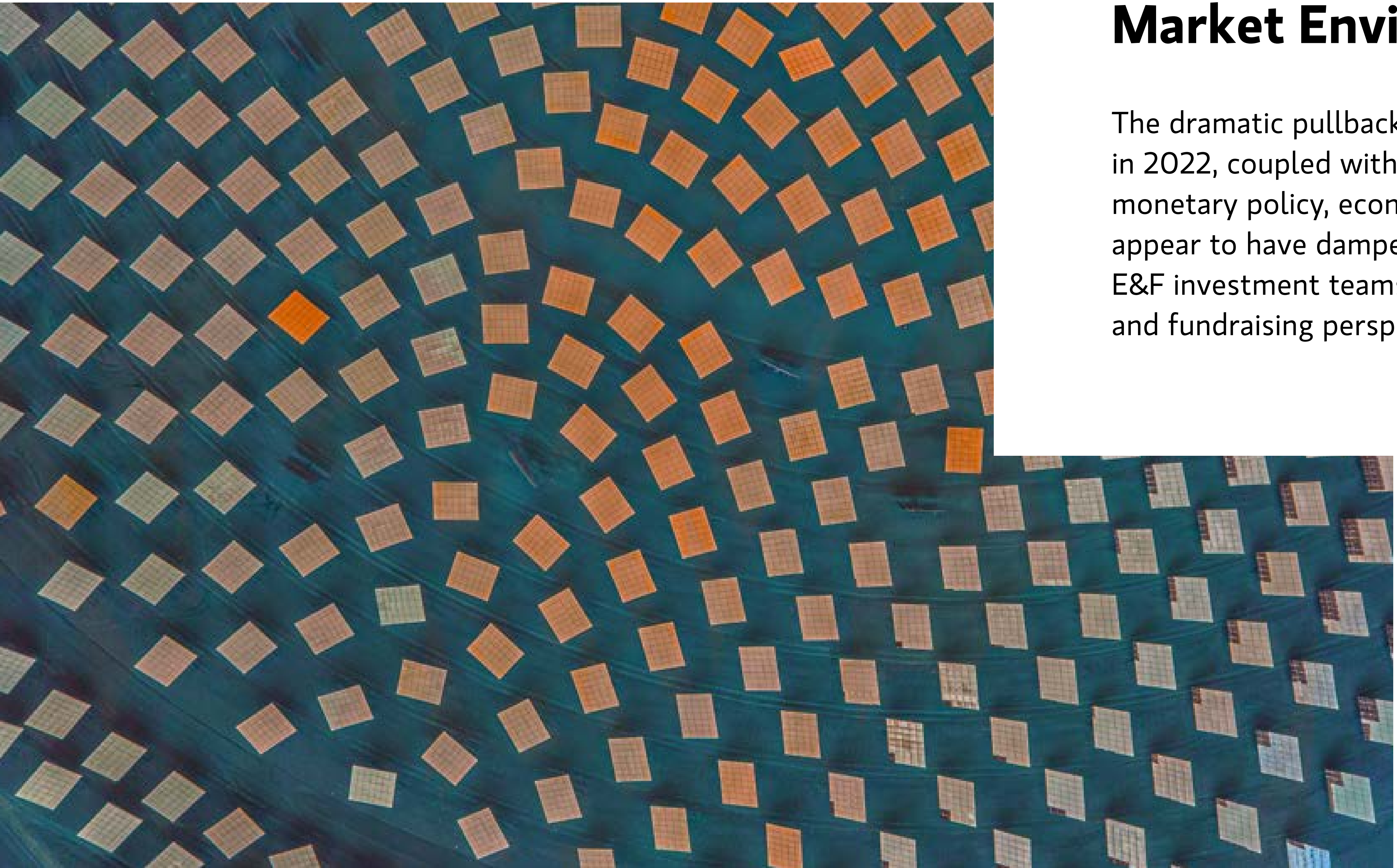


Type of Institution



Sector / Interest Area of Responding Endowments and Non-Profits[2]





Market Environment

The dramatic pullbacks in equity and bond markets in 2022, coupled with continued uncertainty about monetary policy, economic growth, and geopolitics, appear to have dampened the expectations of E&F investment teams — from both investment and fundraising perspectives.

MARKET ENVIRONMENT

Investment Expectations Are Muted

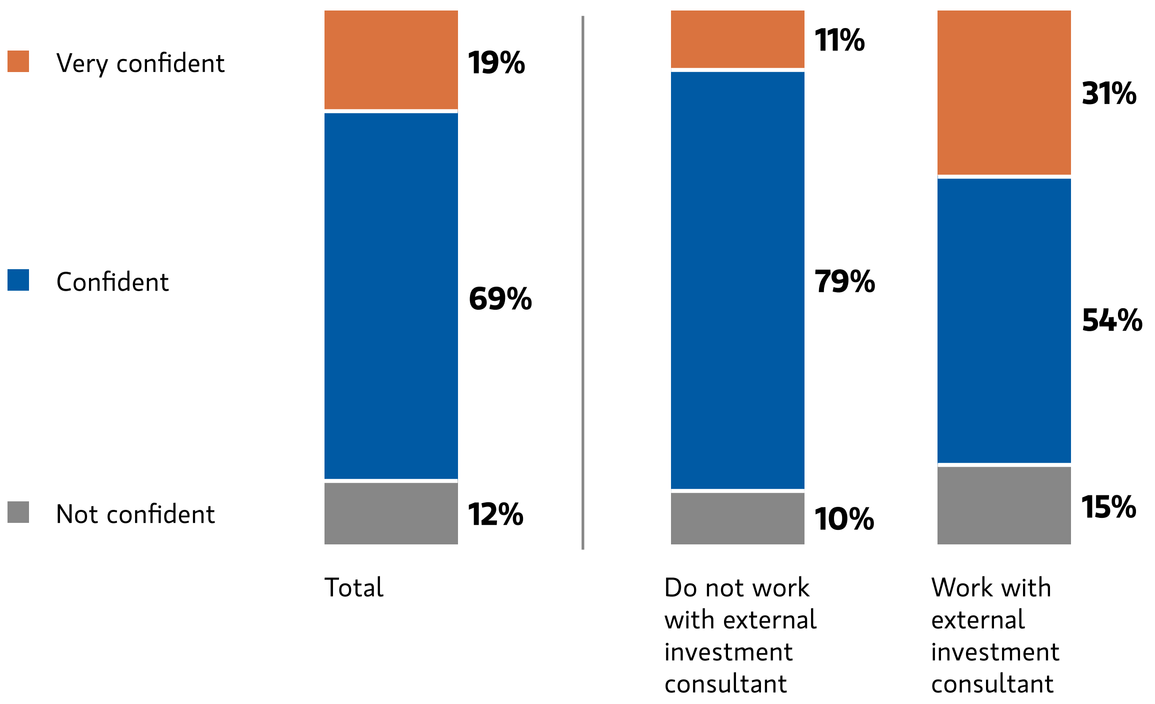
Consultant relationships appear to bolster investor confidence

Given the uncertain market environment, it's not surprising to see that E&Fs have relatively muted expectations for their portfolios. Only one of five (19%) respondents are "very confident" their organizations will achieve their 3-year targeted investment returns.

Working with an external investment consultant, however, seems to have a dramatic impact on these expectations. Nearly three times as many respondents who work with an external consultant feel very confident compared to those who do not (31% compared to 11%).

Q **How confident are you that your organization will achieve its target annualized return over the next 3 years?**

Confidence Organization Will Achieve Target Annualized Return Over Next Three Years



MARKET ENVIRONMENT

What's Keeping Investors Up at Night?

The top concerns among investment decision-makers reflect the long-term focus of endowments and foundations

Considering how much attention interest rates, geopolitical uncertainty, and inflation have garnered since 2022, one might expect those issues to dominate E&Fs' list of concerns.

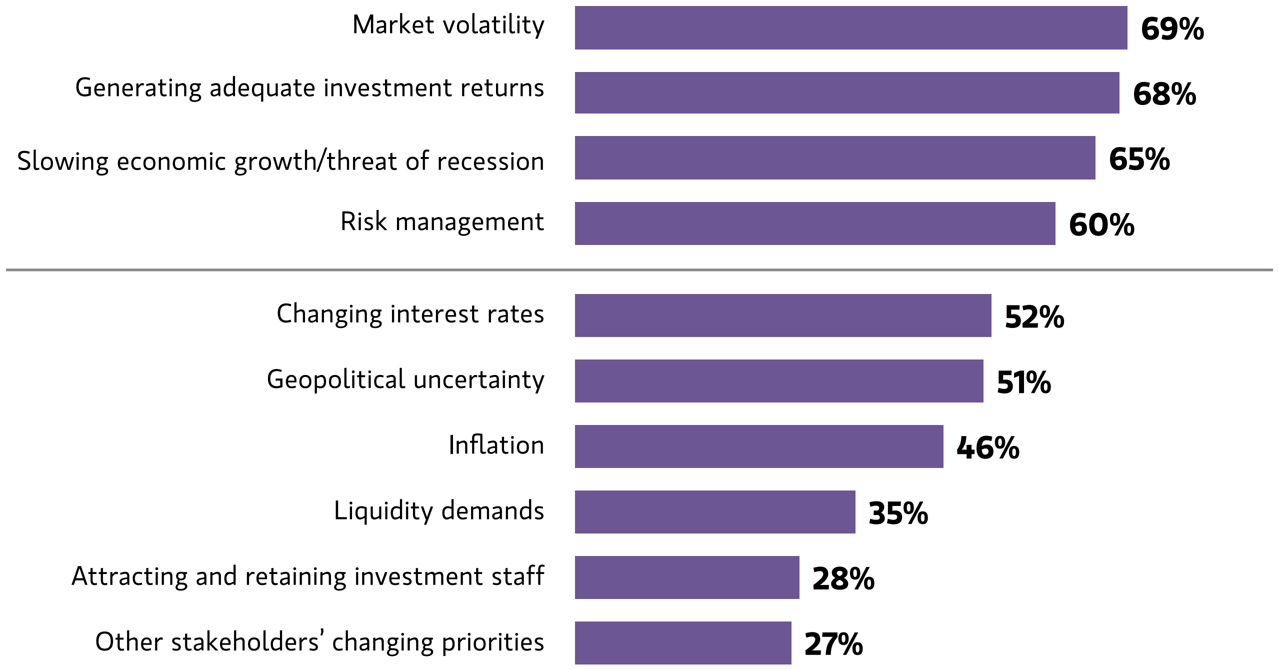
While respondents certainly acknowledge those timely issues, more fundamental challenges top the list of concerns, including those related to hitting investment targets and managing risk in an environment marked by volatility and slowing economic growth.

These results, along with the relatively low concerns about liquidity demands (35%), likely reflect the long investment horizons E&Fs use to manage their portfolios.

Q Which of the following are significant financial challenges that (figuratively) keep you up at night?

Top 10 Financial Challenges of Concern

Mean # of concerns selected: **6**



MARKET ENVIRONMENT

Gifting Expectations Are Dampened

Lack of consensus may reflect unpredictable economic situation

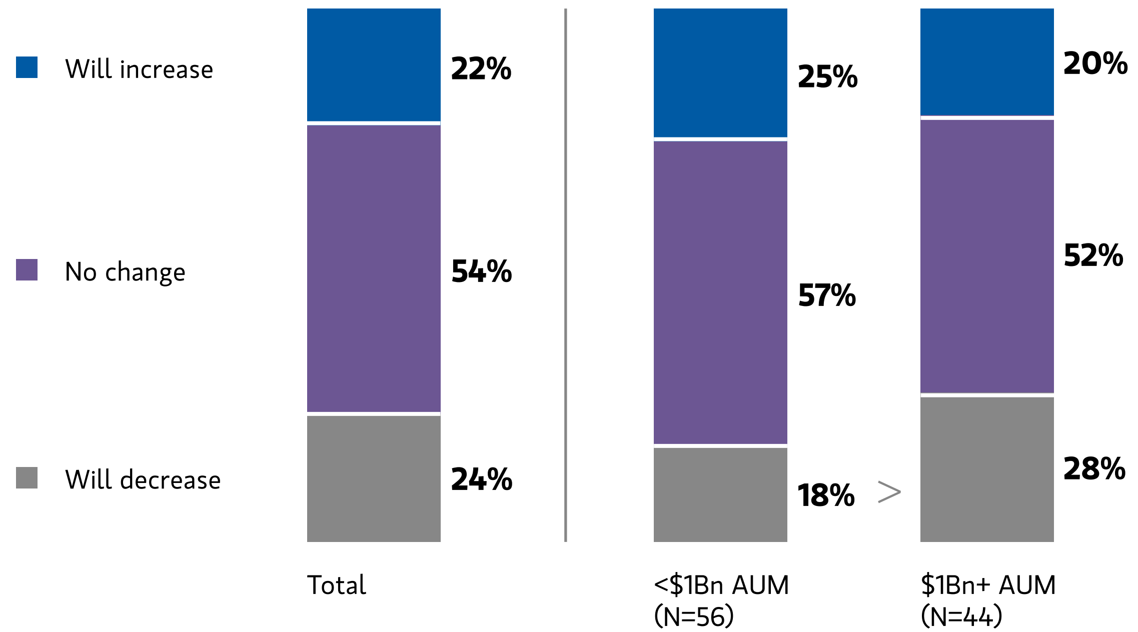
Respondents are roughly split on whether they expect donations to increase or decrease from last year.

These results may reflect the lack of clarity about the economy's direction as of mid-2023. At the time, there was much debate about whether the U.S. economy was headed for recession or could pull off a soft landing.

Respondents representing large E&Fs tend to be more pessimistic than smaller ones about giving trends. This may reflect larger E&Fs' greater resources and/or access to research, providing them with more advanced insights and expectations for an economic downturn.

Q How do you expect your organization's 2023 donations to compare to 2022?

Expected Donations in 2023 vs. 2022



Portfolio Management

Alternatives, particularly private markets, continue to play a growing role in E&F portfolios as investors seek diversified sources of return. Fully utilizing the potential benefits of non-traditional asset classes, however, presents meaningful challenges related to manager access and liquidity constraints.

PORTFOLIO MANAGEMENT

Endowments and Foundations Are Building Widely Diversified Portfolios

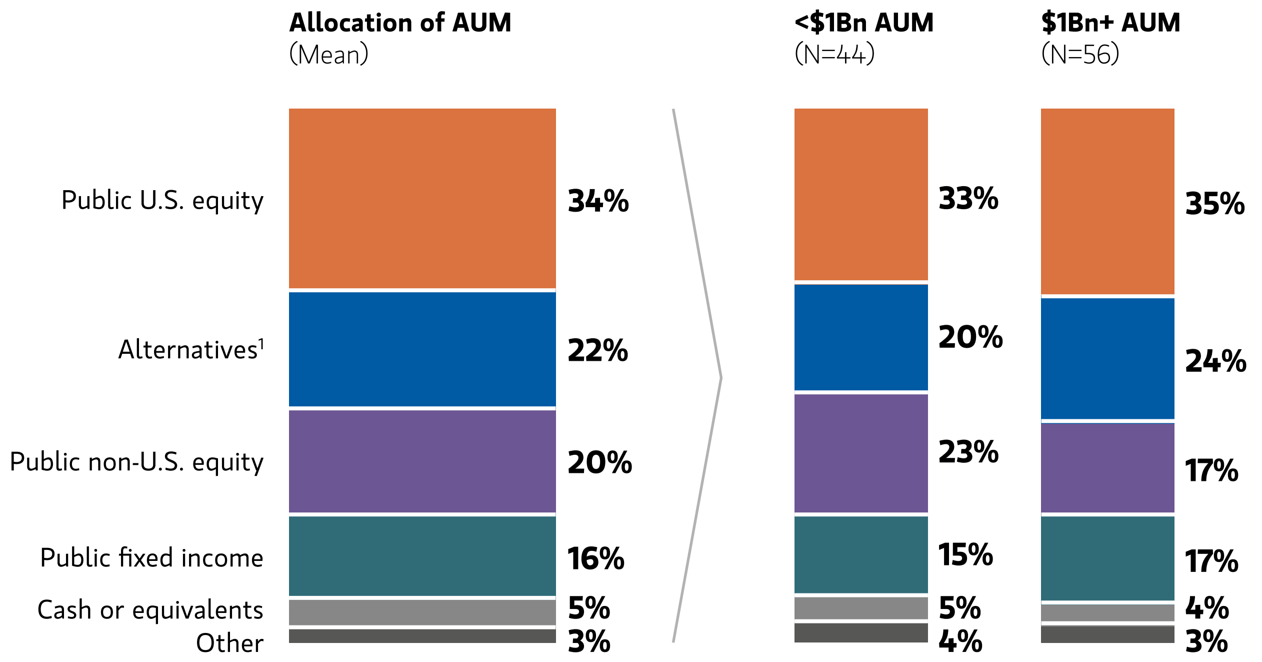
Access and expertise directly affect the ability to fully utilize the benefits of alternatives

Larger respondents report allocating more to alternatives than smaller respondents, although the difference isn't statistically significant. Much of these larger plans' alternatives exposure comes from their non-U.S. equity exposure.

Given the complex nature of alternatives and the wide dispersion of returns among managers, it is not surprising that larger plans tend to have higher alternatives allocations. Larger E&Fs tend to have bigger, more experienced staffs, greater access to top managers, and more tolerance for illiquidity. As a result, they tend to be better-positioned to manage the complexities of alternatives.

The complexities of alternatives also explain why many E&Fs rely heavily on external consultants to fully utilize the benefits of these non-traditional, often less liquid asset classes.

Asset Class Allocation as Percent of AUM



1. Alternatives include private equity, private credit, real estate, infrastructure, hedge funds/marketable alternatives, and commodities.

Q What percentage of your organization's portfolio is invested in the following asset classes?

PORTFOLIO MANAGEMENT

Alternatives Will Have an Increasing Role in Portfolios of Endowments and Foundations

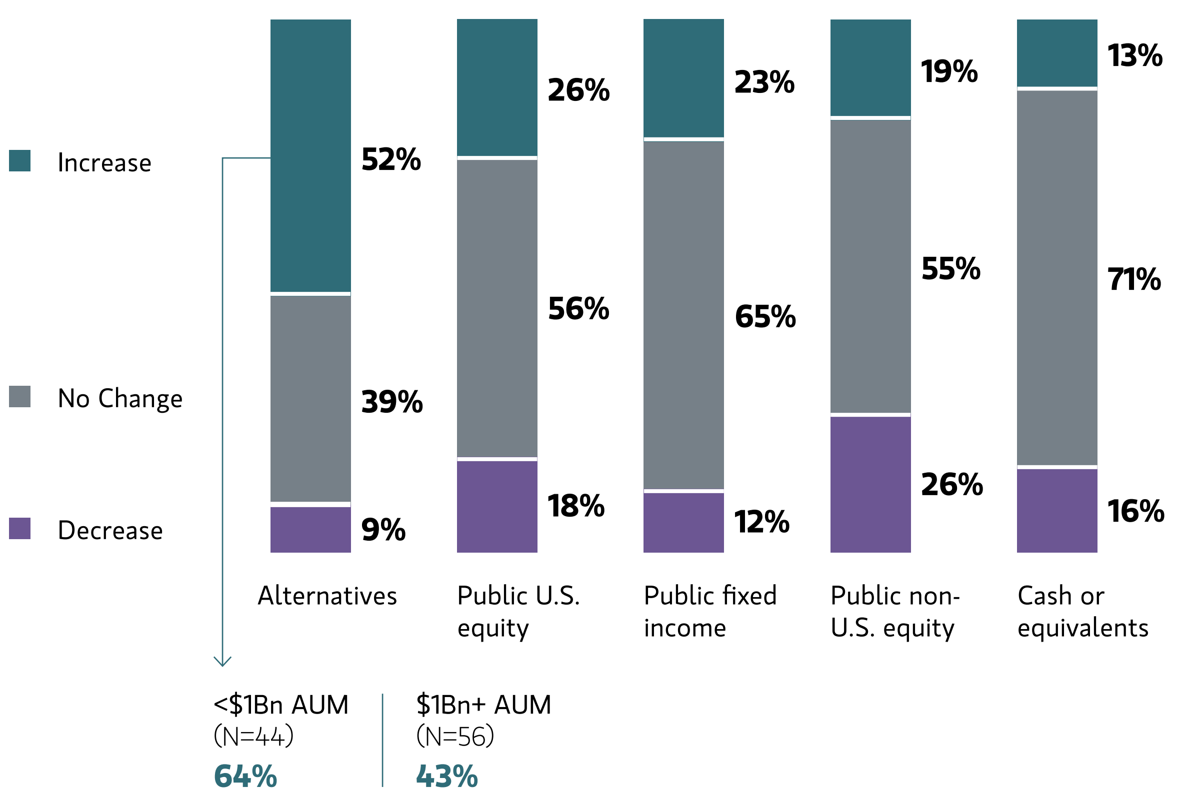
Planned increases to alternatives far exceed any other asset class

The rise of alternatives in institutional portfolios has been well-publicized. Still, it is striking to see how this momentum is poised to continue — especially relative to the intentions of endowments and foundations for other asset classes.

Despite already representing nearly a quarter of E&Fs' portfolios, most respondents intend to continue building on these positions. More than half (52%) of respondents — and nearly two-thirds (64%) of smaller E&Fs — expect to increase their allocations to alternatives in the next year.

The large tilt to alternatives raises the question of where those assets will come from. One indicator is that expected decreases among public non-U.S. equities and cash outpace expected increases. But in general, these results highlight one of the challenges investors face when they think about future allocations and the associated rebalancing.

Expected Change in Allocation Over Next 12 Months



Q Over the next 12 months, how do you expect your allocations to each of the following asset classes to change, if at all?

PORTFOLIO MANAGEMENT

Allocations to Alternatives Are Dominated by Private Markets

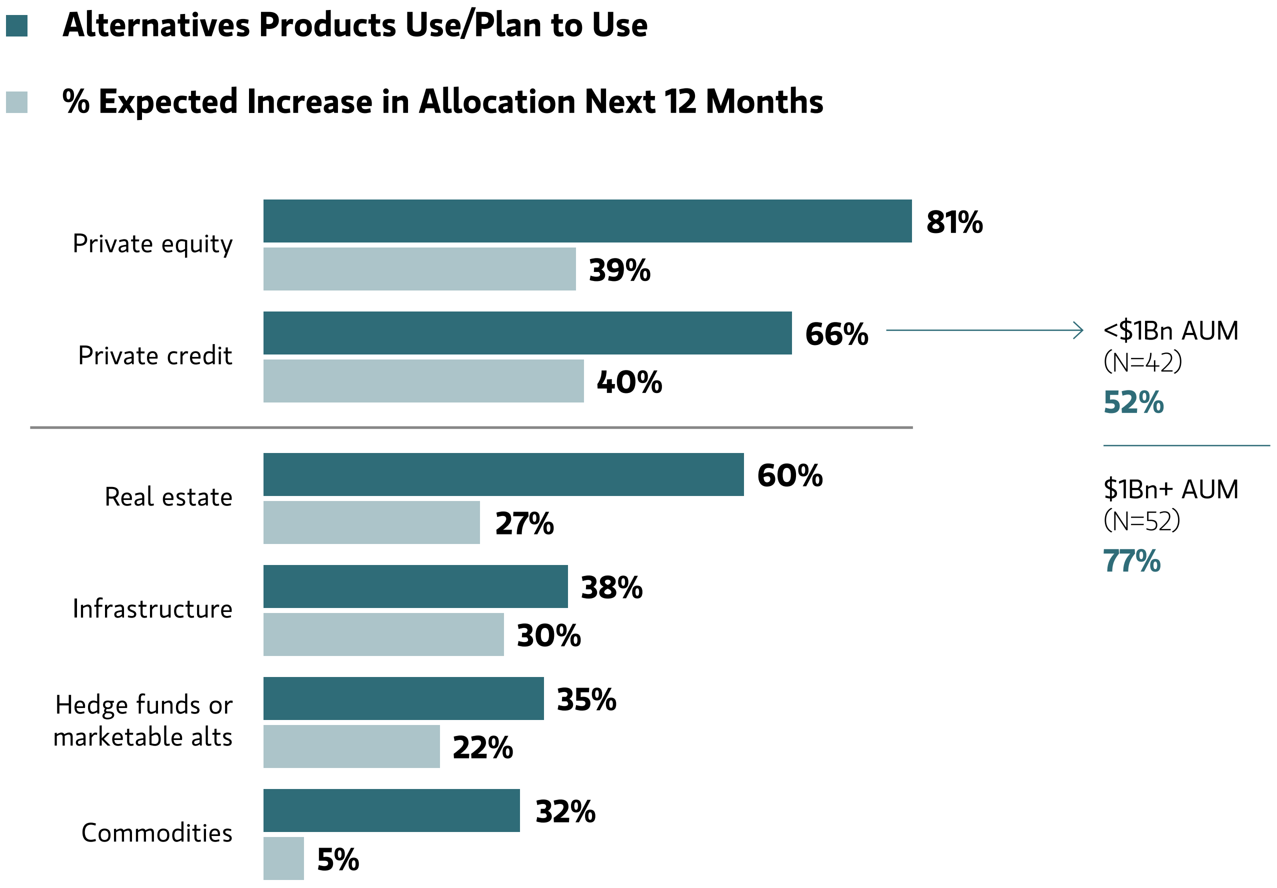
Cyclical economic concerns highlight the importance of manager selection

Within alternatives, respondents show a clear preference for private markets. Private equity continues to be the most-used alternative asset class, as more than eight of 10 E&Fs currently allocate and/or expect to allocate to private equity.

Meanwhile, two-thirds (66%) of respondents, including more than three-fourths (77%) of larger E&Fs, use or plan to use private credit. With the rising threat of an economic downturn, manager selection is paramount in all alternative asset classes, but particularly private credit, which faces higher default risk in a recession.

Q What alternatives products do you use (or plan to use if 0%)?

Q Over the next 12 months, how do you expect your allocations to each of the following asset classes to change, if at all?



PORTFOLIO MANAGEMENT

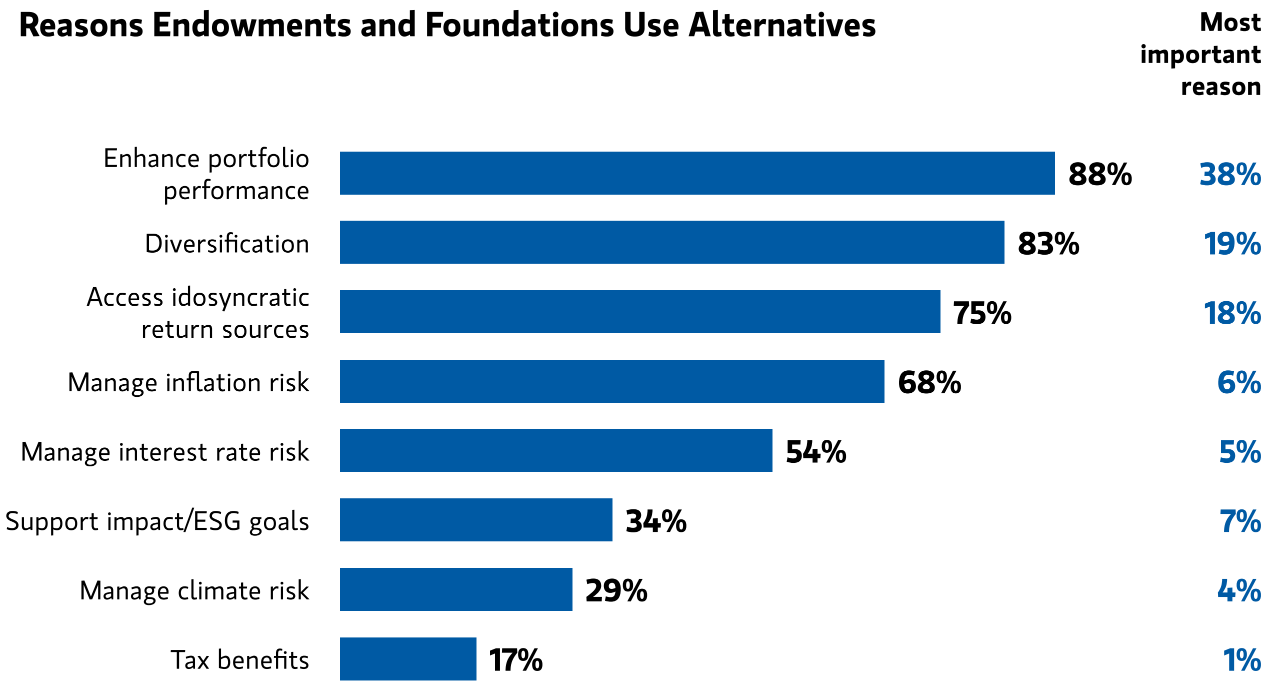
Endowments and Foundations Are Pursuing Alternatives for Many Reasons

Performance and diversification are the primary motivators

Not surprisingly, enhanced portfolio performance is the most-cited reason for using alternatives, with 38% of respondents calling it their most important reason.

The vast majority of E&Fs also rely on alternatives for diversification (83%) and access to idiosyncratic return sources (75%).

The survey results also highlight the role that alternatives can play in sustainable investing—at least for a portion of investors. Nearly one-third of respondents cite supporting impact or ESG goals (34%) and managing climate risk (29%) as reasons they invest in alternatives.



Q Which of the following are important reasons your organization uses (or plan to use if 0%) alternatives? Base: currently use alternatives or plan to (n = 94).

Q Which one of these is the most important reason your organization uses (or plan to use if 0%) alternatives? Base: currently use alternatives or plan to (n = 94). Totals for "Most important reason" may not add to 100% due to rounding.

PORTFOLIO MANAGEMENT

Endowments and Foundations Acknowledge that Alternatives Present Challenges

But there is little agreement on which challenges are most pressing

Access to top managers and strategies (62%) and expertise required to perform due diligence (56%) were two of the three most frequently cited challenges to using alternatives. These results are particularly relevant because nearly nine of 10 respondents either plan to (41%) or may (46%) conduct external manager searches in the next 12 months. Notably, 63% of these respondents plan to search for a private equity manager in the coming year, the highest of any asset class.

Respondents cited illiquidity (21%) and portfolio integration (13%) as the most significant challenges to using alternatives. These results show that building well-rounded portfolios that align with the organization's cash flow needs are top-of-mind for E&Fs as they seek to harness the benefits of alternatives.

Q

Which of the following are significant challenges to using alternative investments?

Q

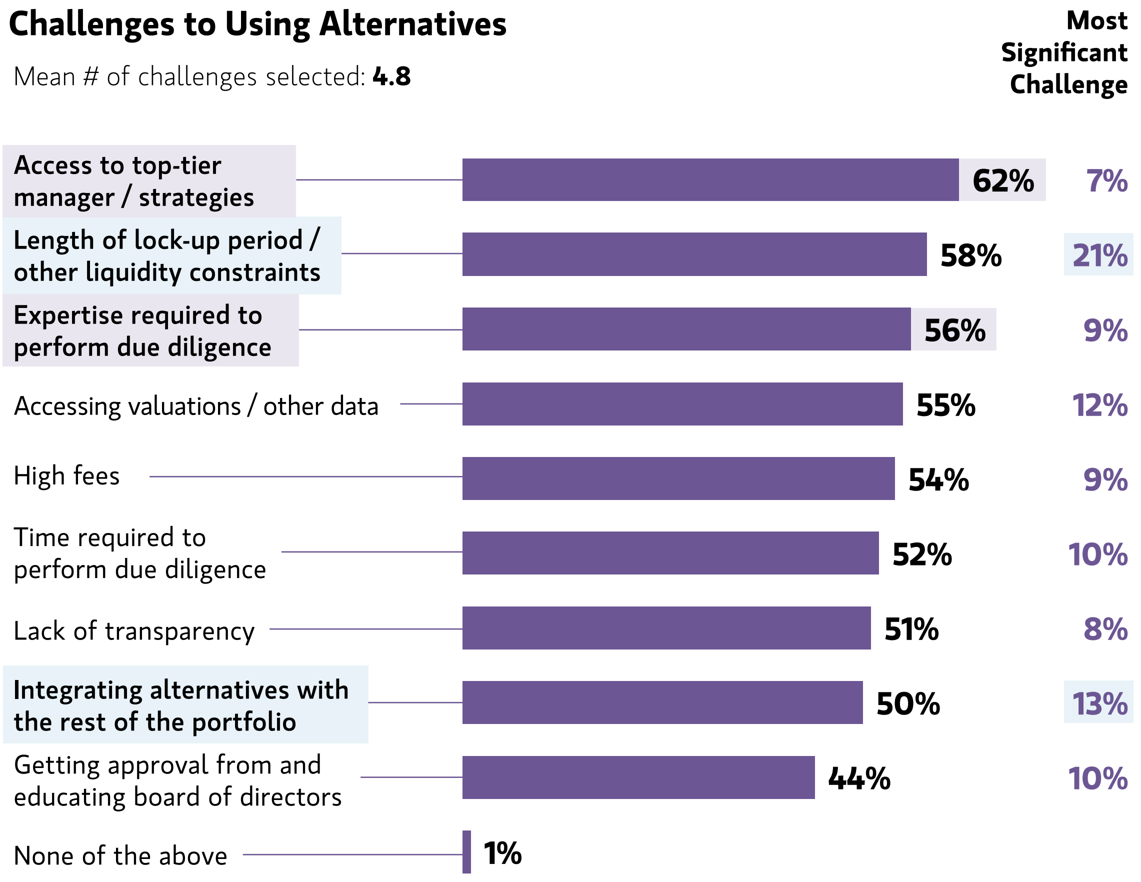
Which one of these is the most significant challenge to using alternative investments?

Q

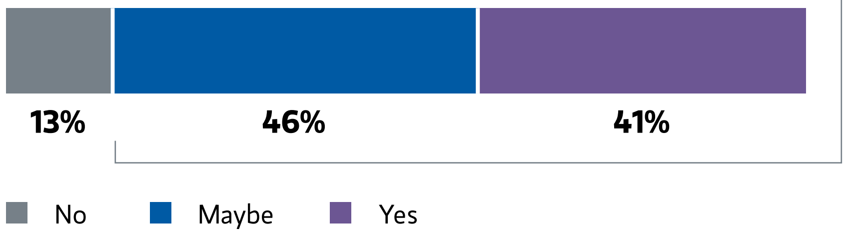
Are you currently conducting or do you plan to conduct any external manager searches over the next 12 months? If so, which asset classes?

Challenges to Using Alternatives

Mean # of challenges selected: **4.8**



Currently or Planning to Conduct External Manager Searches in Next 12 Months



63%

Among those planning or considering a search, 63% of searches will be for private equity managers

Governance, Operations and Staffing

Despite a challenging market and fundraising environment, many investment teams at E&Fs anticipate growing their staff and/or spending more on operations. Meanwhile, organizations recognize the importance of educating their boards and investment committees.

GOVERNANCE, OPERATIONS AND STAFFING

Many Endowments and Foundations Are Preparing for Growth

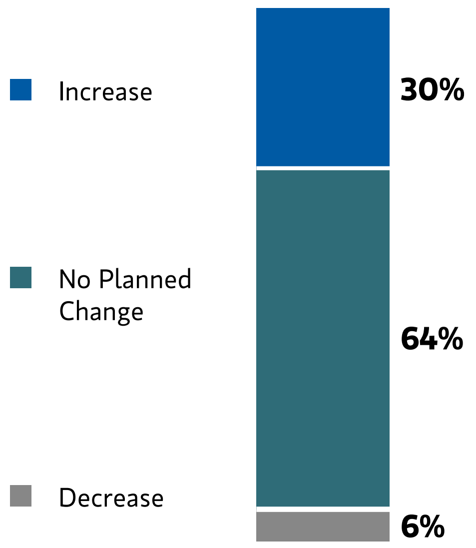
Despite headwinds, more plan to expand than retract

Despite uncertain markets and several other challenges cited, many E&Fs are planning to expand their operations.

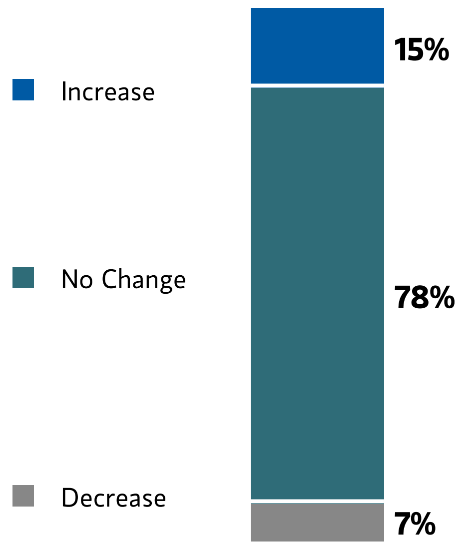
Three in 10 E&Fs plan to grow their investment teams in the next three years, while just 6% expect to reduce staff. Meanwhile, more than twice the number of respondents said they expect to increase spending at their organizations (15%) compared to decrease it (7%).

These organizations may be responding to — and preparing for — an investment landscape that has become more complex every year, especially as alternatives gain prominence and navigating ESG, impact, and mission-aligned investing requires balancing the views of numerous stakeholders.

Expectations for Staff Size Over Next Three Years



Expected Change to Organization's Spending Rate in Next Three Years



Q How do you expect the size of your investment / finance staff to change, if at all, over the next three years?

Q How do you expect your organization's spending rate to change, if at all, in the next three years?

GOVERNANCE, OPERATIONS AND STAFFING

Endowments and Foundations See the Need for Investment Training for Boards

Formal training programs can help boards provide strong oversight of portfolios

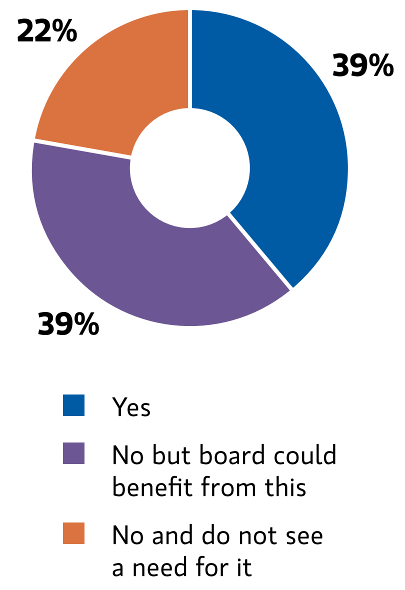
Most E&Fs (78%) either have an existing training program for their boards or recognize the benefits of having one. Among respondents that have an investment committee (IC), 64% feel the same regarding training of their ICs.

These results may reflect respondents' views that board and IC members, as fiduciaries, need to:

- Understand how investments are aligned with their organizations' missions
  Monitor and evaluate how investments are being managed as they oversee ICs and/or investment policy statements
- Stay up-to-speed on the changing investment landscape

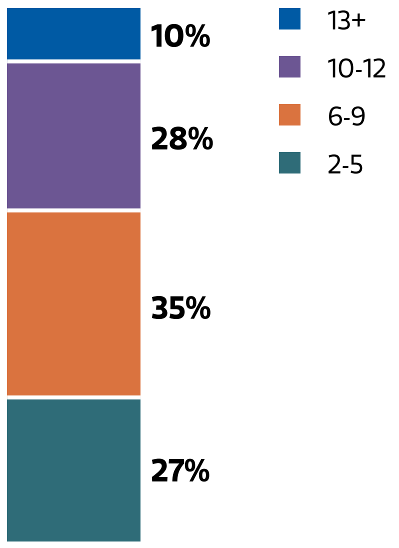
Respondents have, on average, approximately nine board members. This highlights the importance of a well-organized and coordinated training program to help E&F boards provide strong oversight of the organization's investments.

Have a Formal Investment-Focused Training Program for Board Members?



Number of People on Boards of Directors

Average: **8.6**



Q Does your organization have a formal investment-focused training program for board members?

Q How many people are on your organization's board of directors?

GOVERNANCE, OPERATIONS AND STAFFING

Results Show Common Practices of Investment Committees

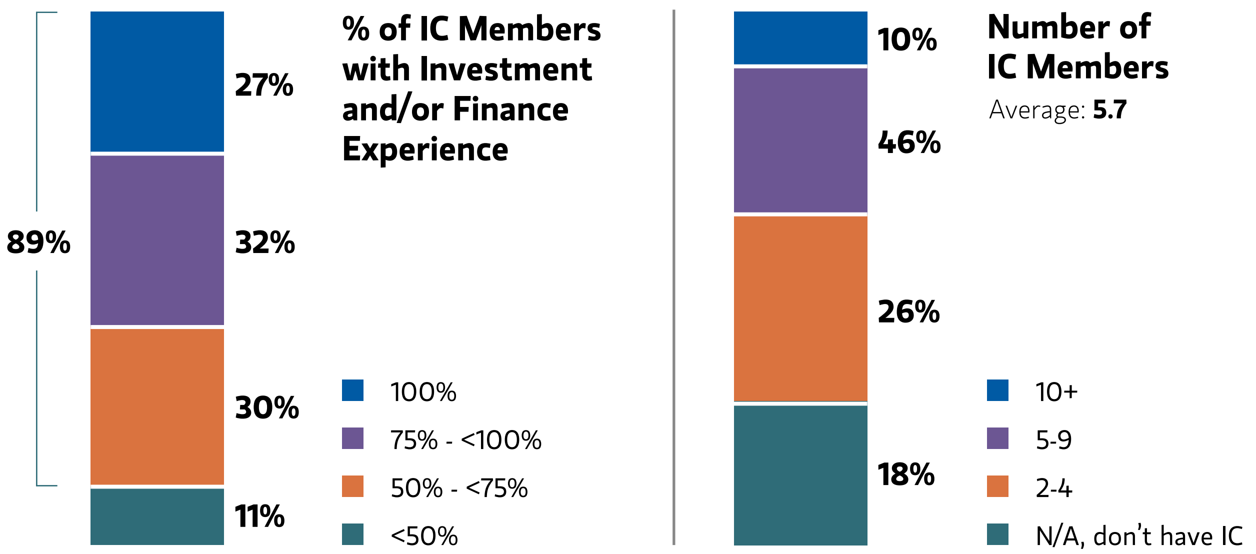
Investment experience is prized but not essential for IC members

More than eight of 10 responding organizations have a formal investment committee (IC). Amid an increasingly complex investment landscape, these committees play a vital role in overseeing the portfolio, drafting and updating the **investment policy statement (IPS)**, and keeping the board informed about major decisions.

Learn more about effective investment committees:

To dive deeper into an investment committee's responsibilities and the best practices of successful committees, download our e-book, **Non-Profit Board's Guide to Building an Effective Investment Committee**.

82% of Respondents with a Formal IC



Frequency of Meetings and Reviews

74% of ICs meet quarterly

9% meet monthly

80% review their investment policy statement at least annually

Q

How many people are on your organization's investment committee (IC)?

Q

How often does the investment committee meet?

Q

How often does your organization formally review its investment policy statement (IPS)?

Key Takeaways for Endowments and Foundations

The survey's findings about how E&Fs are currently approaching markets, portfolios, and governance can guide boards and investment committees as they strive to fulfill their organizational missions.

Recapping the Major Themes from the Survey

Understanding the drivers of these themes can help Endowments and Foundations navigate the challenges and capitalize on the opportunities of the current landscape.

Lagging Confidence

Market volatility and economic uncertainty are dampening E&F investors' confidence in meeting both performance and fundraising goals. However, working with a consultant can increase confidence in meeting performance objectives.

Fundamental Challenges

Respondents appear to be less concerned with recent, timely issues like rising interest rates or inflation; instead, they identify more fundamental challenges such as meeting investment goals and managing risk as pressing issues.

Continued Rise of Alts

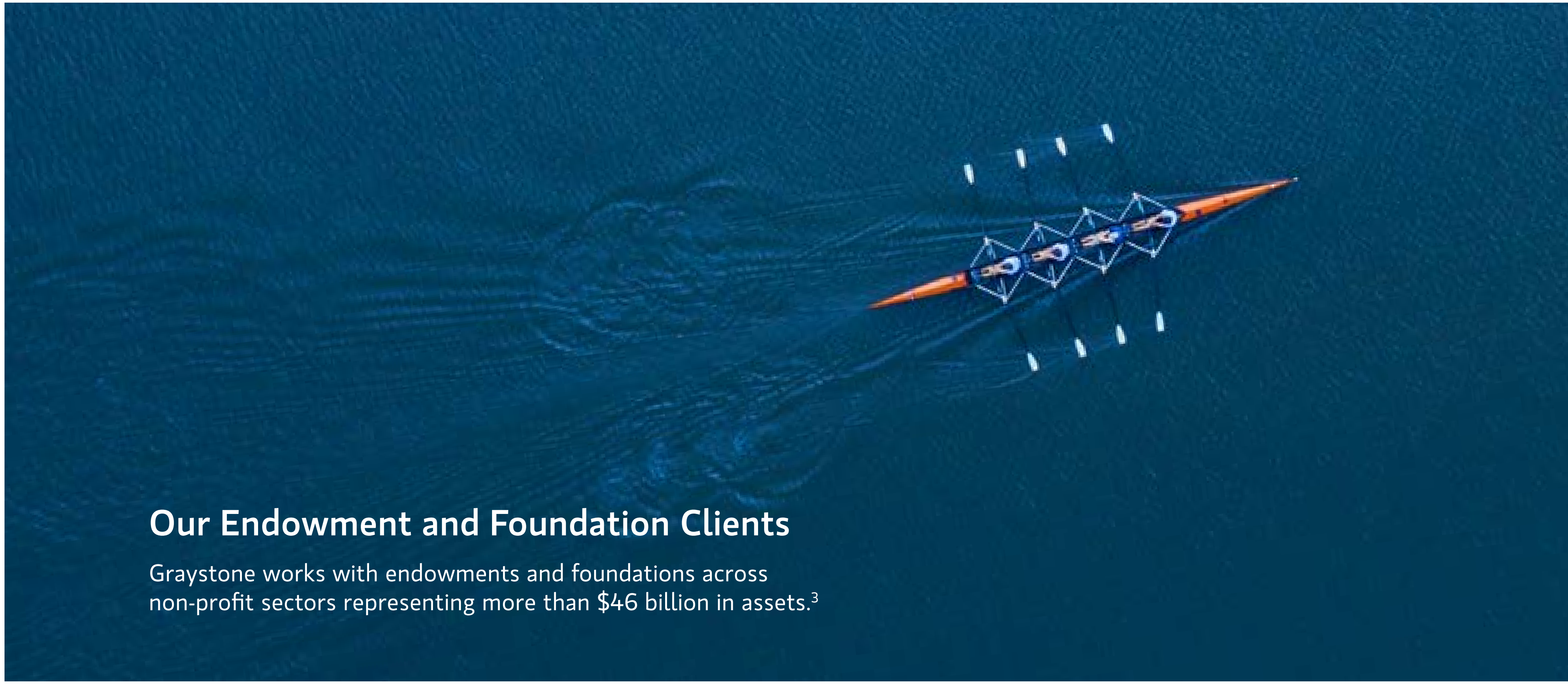
E&Fs are seeking diversified return sources for their portfolios, often looking to alternatives. While smaller organizations are generally lagging their larger peers in allocations to alternatives, smaller E&Fs are aggressively looking to increase their alternatives allocations in the next year.

Preparing for Growth

Despite a challenging market and giving environment, many organizations are staffing to support their growth and manage an increasingly complex investment landscape. Given the speed at which market conditions and investment options are evolving, E&Fs see the value in training their boards and investment committee members.

Trusted Guidance for Endowments and Foundations

Graystone Consulting is committed to providing trusted advice and customized solutions to E&Fs. We deliver the high-touch service you would expect from a boutique, and the resources and access that come from being backed by a global leader in financial services.



Education **Healthcare** **Faith-Based** **Community** **Arts and Culture**

3. Source: Morgan Stanley Wealth Management, as of September 30, 2024.

Global Resources with Local Expertise

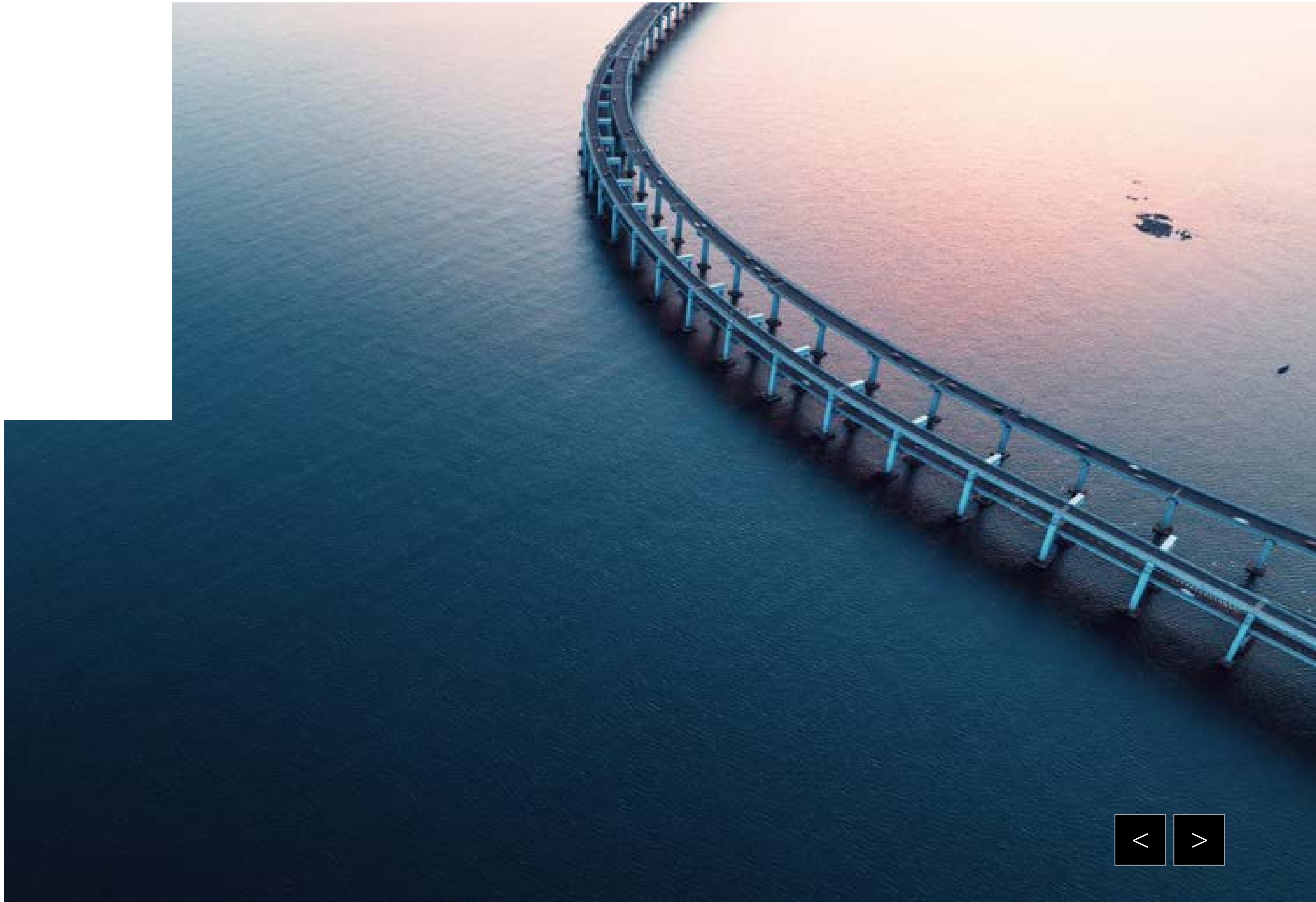
At Graystone Consulting, we combine local expertise and global resources to help your organization make informed, confident investment decisions.

$793 Billion in total institutional assets under management[4]

50+ Years of experience advising institutional clients

4,800+ Strategies monitored annually[5]

4. Source: Morgan Stanley Wealth Management, as of September 30, 2024.
5. Source: Morgan Stanley Global Investment Office, as of March 2024.



Let's Talk

We look forward to starting the conversation on how we can help.

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IMPORTANT DISCLOSURES

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[2] Base: Endowment or non-profit (n=51). Totals exceed 100% because some respondents selected multiple categories.

[3] Source: Morgan Stanley Wealth Management, as of September 30, 2024.

[4] Source: Morgan Stanley Wealth Management, as of September 30, 2024.

[5] Global Investment Manager Analysis (GIMA), March 2024 Investments and services offered through Morgan Stanley Smith Barney LLC When Morgan Stanley Smith Barney LLC, its affiliates and Morgan Stanley Financial Advisors and Private Wealth Advisors (collectively, "Morgan Stanley") provide "investment advice" regarding a retirement or welfare benefit plan account, an individual retirement account or a Coverdell education savings account ("Retirement Account"), Morgan Stanley is a "fiduciary" as those terms are defined under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), and/or the Internal Revenue Code of 1986 (the "Code"), as applicable. When Morgan Stanley provides investment education, takes orders on an unsolicited basis or otherwise does not provide "investment advice", Morgan Stanley will not be considered a "fiduciary" under ERISA and/or the Code. For more information regarding Morgan Stanley's role with respect to a Retirement Account, please visit www.morganstanley.com/disclosures/dol. Tax laws are complex and subject to change. Morgan Stanley does not provide tax or legal advice. Individuals are encouraged to consult their tax and legal advisors (a) before establishing a Retirement Account, and (b) regarding any potential tax, ERISA and related consequences of any investments or other transactions made with respect to a Retirement Account.

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The returns on a portfolio consisting primarily of Environmental, Social and Governance ("ESG") aware investments may be lower or higher than a portfolio that is more diversified or where decisions are based solely on investment considerations. Because ESG criteria exclude some investments, investors may not be able to take advantage of the same opportunities or market trends as investors that do not use such criteria. Diversification does not guarantee a profit or protect against loss in a declining financial market.

Fixed Income investing entails credit risks and interest rate risks. When interest rates rise, bond prices generally fall. Foreign investments involve greater risks than U.S. investments, including political, economic, market risks and the risk of currency fluctuations.

Private equity funds typically invest in securities, instruments, and assets that are not, and are not expected to become, publicly traded and therefore may require a substantial length of time to realize a return or fully liquidate. They typically have high management, performance and placement fees which can lower the returns achieved by investors. They are often speculative and include a high degree of risk. Investors can lose all or a substantial amount of their investment. They may be highly illiquid with significant lock-up periods and no secondary market, can engage in leverage and other speculative practices that may increase volatility and the risk of loss, and may be subject to large investment minimums.

Asset allocation and diversification do not assure a profit or protect against loss.

Alternative investment securities discussed herein are not covered by the protections provided by the Securities Investor Protection Corporation, unless such securities are registered under the Securities Act of 1933, as amended, and are held in a Morgan Stanley Wealth Management Individual Retirement Account.

Alternative investments often are speculative and include a high degree of risk. Investors could lose all or a substantial amount of their investment. Alternative investments are appropriate only for eligible, long-term investors who are willing to forgo liquidity and put capital at risk for an indefinite period of time. They may be highly illiquid and can engage in leverage and other speculative practices that may increase the volatility and risk of loss. Alternative Investments typically have higher fees than traditional investments. Investors should carefully review and consider potential risks before investing

METHODOLOGY

Phone survey among 100 endowments and foundations. Respondent qualifying criteria:

- Part of team that makes investment decisions
- Organization AUM $100 million+
- <$1Bn: N=44; $1Bn+: N=56

Data collection occurred during May 2023; Graystone Consulting / Morgan Stanley was not identified as research sponsor

Statistical testing was done at the 90% confidence level.

8 Acre Perspective, an independent research firm, conducted the research.

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