2023 Endowment and Foundation Survey

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
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 Characteristics

Size - Assets Managed

- 14% $100 million - $500 million
- 22% $500 million - <$1 billion
- 22% $1 billion - <$5 billion
- 30% $5 billion - <$10 billion
- 14% $10 billion +

Type of Institution

- 15% Endowment
- 19% Private Foundation
- 30% Public Foundation
- 36% Other non-profit

Sector / Interest Area of Responding Endowments and Non-Profits²

- 73% Education
- 10% Healthcare and wellness
- 10% Faith-based
- 6% Community development
- 6% Environment
- 8% Other

Respondent Roles

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

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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.
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.
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?
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.

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

- Market volatility
- Generating adequate investment returns
- Slowing economic growth/threat of recession
- Risk management
- Changing interest rates
- Geopolitical uncertainty
- Inflation
- Liquidity demands
- Attracting and retaining investment staff
- Other stakeholders’ changing priorities

Mean # of concerns selected: 6
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.

How do you expect your organization’s 2023 donations to compare to 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.
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.

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

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

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).

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.
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.

Challenges to Using Alternatives

Mean # of challenges selected: 4.8

<table>
<thead>
<tr>
<th>Challenge</th>
<th>Mean %</th>
<th>Most Significant Challenge</th>
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<tbody>
<tr>
<td>Access to top-tier manager / strategies</td>
<td>62%</td>
<td>7%</td>
</tr>
<tr>
<td>Length of lock-up period / other liquidity constraints</td>
<td>58%</td>
<td>21%</td>
</tr>
<tr>
<td>Expertise required to perform due diligence</td>
<td>56%</td>
<td>9%</td>
</tr>
<tr>
<td>Accessing valuations / other data</td>
<td>55%</td>
<td>12%</td>
</tr>
<tr>
<td>High fees</td>
<td>54%</td>
<td>9%</td>
</tr>
<tr>
<td>Time required to perform due diligence</td>
<td>52%</td>
<td>10%</td>
</tr>
<tr>
<td>Lack of transparency</td>
<td>51%</td>
<td>8%</td>
</tr>
<tr>
<td>Integrating alternatives with the rest of the portfolio</td>
<td>50%</td>
<td>13%</td>
</tr>
<tr>
<td>Getting approval from and educating board of directors</td>
<td>44%</td>
<td>10%</td>
</tr>
<tr>
<td>None of the above</td>
<td>1%</td>
<td>1%</td>
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Currently or Planning to Conduct External Manager Searches in Next 12 Months

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

<table>
<thead>
<tr>
<th>Search Type</th>
<th>No</th>
<th>Maybe</th>
<th>Yes</th>
</tr>
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<tbody>
<tr>
<td>Planning</td>
<td>13%</td>
<td>46%</td>
<td>41%</td>
</tr>
<tr>
<td>May</td>
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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.
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.

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?
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.

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?
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.

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)?

82% of Respondents with a Formal IC

<table>
<thead>
<tr>
<th>% of IC Members with Investment and/or Finance Experience</th>
<th>Number of IC Members</th>
</tr>
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<tbody>
<tr>
<td>100%</td>
<td>10%</td>
</tr>
<tr>
<td>75% - &lt;100%</td>
<td>46%</td>
</tr>
<tr>
<td>50% - &lt;75%</td>
<td>26%</td>
</tr>
<tr>
<td>&lt;50%</td>
<td>18%</td>
</tr>
</tbody>
</table>

Average: 5.7

Frequency of Meetings and Reviews

- 74% of ICs meet quarterly
- 9% meet monthly
- 80% review their investment policy statement at least annually
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.

Our Endowment and Foundation Clients

Graystone works with more than 450 endowments and foundations across non-profit sectors representing more than $23 billion in assets.3

Global Resources with Local Expertise

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

$515.7 Billion in total institutional assets under management

50 Years of experience advising institutional clients

4,400+ Strategies monitored annually

IMPORTANT DISCLOSURES

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.
3 Source: Morgan Stanley Wealth Management, as of September 30, 2022.
4 Source: Morgan Stanley Wealth Management, as of December 31, 2022.
5 Global Investment Manager Analysis (GIMA), June 2023

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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 95% confidence level.

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