Investment Management for Nonprofits: is the famed "endowment model" holding you back?

Nonprofit endowments have for decades trended towards the standardized approach made famous through its success with Ivy League institutions. Born out of Yale and tagged as the gold standard, the endowment model starts at the macro level and creates a "manager of managers" environment. The investment firm serving as the lead engages dozens – sometimes more than 100 – best-in-class managers across all asset classes to create a highly diversified portfolio.

The model is tempting due to its success with leading institutions and headline fame. Yet it was designed for some of the largest portfolios in the nonprofit world; for those with more modest endowments of less than $50 million, it can generate more challenges than it does positive results.

<u>Opportunity</u>: Building a customized endowment that is a better fit for the NFP's mission
<u>Challenge</u>: Identifying holdings that individually play a role in reaching the NFP's overall objectives
<u>W&F goal</u>: Creating a portfolio that enhances the likelihood of meeting the NFP's financial goals and aligns more closely with its values

The risk lies in a lack of connectivity inherent in the model. The wide range of discrete managers not only layers additional fees on the portfolio, it leads to the scattered team members seeking out investments in silos. As these managers are often looking for similar criteria in their selections, they can inadvertently create too much correlation in the portfolio across too many asset classes. When the market goes down, the holdings are exposed to heightened downside.

Nonprofits deserve a better approach that is more customized and fit for purpose. Portfolios should be constructed by a portfolio manager who is a member of a centralized team that selects individual securities, or complimentary funds whether public or private, with each holding playing a role in the balancing act of suitable investing. That provides more control over goals such as capital preservation to help meet liquidity needs, growing an income stream, and directing assets to fulfill an organization's mission.

For example, if a nonprofit is focused on scholarships for underserved students, a well-designed portfolio will consider factors such as when scholarship funds are released to students. The way that individual securities are chosen helps to support the overall plan.

A more focused approach can also support values alignment and the integration of environmental, social, and governance (ESG) factors. Nonprofits are increasingly striving to match their endowment strategy with the values that are associated with their mission; customized portfolio construction enables that goal.

At Welch & Forbes, we work with each nonprofit client to create strategies and investments that support their specific mission.

We invite you to learn more by contacting Ed Sullivan, Vice President, at 617-557-9800 or esullivan@welchforbes.com.