

Sources of Endowment Growth at Colleges and Universities

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Preface

Commonfund Institute is Commonfund's focal point for educational and professional development programs, research and publications, information sharing, and communications. These varied and ongoing efforts are all aimed at advancing investment knowledge and promoting best practices among nonprofit organizations, investment staff and trustees.

From the very founding of Commonfund in 1971, education has been a central part of our mission. Today, Commonfund Institute sponsors a number of major programs, including the Commonfund Benchmarks Study[®] of investment policies and practices in the education, foundation and healthcare communities; the Endowment Institute, an intensive, week-long seminar for trustees and senior investment officers; Trustee Roundtables, luncheon meetings held throughout the year in various regions of the country; Regional Investment Seminars, one-day meetings for investment staff and trustees; and our continuing series of investment conference calls.

In addition, Commonfund Institute sponsors the publication of books, monographs, educational brochures and white papers related to investment management for nonprofit institutions. This paper, Sources of Endowment Growth at Colleges and Universities, is one such effort in this series. Investment policy, asset allocation, spending rates and related subjects have been closely scrutinized over the years. But a great deal less attention has been given to the role of gifts and fundraising and the long-term impact they can have on educational endowments. As the product of two experienced leaders in this field, Fred Rogers and Glenn Strehle, it is a thoughtful, professional and carefully prepared work that deserves widespread readership within the educational community.

Commonfund Institute is pleased to have teamed with Messrs. Rogers and Strehle and commend them for their fine work. We believe this paper does much to renew once again Commonfund's commitment to promulgating best practices and sharing knowledge for the benefit of nonprofit institutions everywhere.

Executive Summary

College and university endowments are a topic of much discussion and comparison. While institutions and the public media compare total endowments and the most recent investment performance, less attention has been paid to the long-term changes in endowments and to the underlying strategies that lead to sustained growth. Drawing upon the results of three national studies, this paper concludes that gifts to endowment are as important as investment returns and endowment spending in determining the long-term growth and size of an institution's endowment.

While institutional policy in recent years has focused on spending rules and asset allocation, for many institutions with modest endowments an equally important focus is on fundraising and additions to endowment. Unitized endowment accounting is an easy means to assess the long-term contributions to growth from additions as compared to reinvestments. In the future, we believe more attention should be paid to such measures. Institutions should examine their policies and practices in light of their intended longer term goals for endowment growth, and hence, their ability to support the educational mission.

In recent years, public institutions have been national leaders in building endowment through gifts, as measured in terms of percentage growth from this source. Often beginning from a small base, they have aggressively pursued new sources of gifts and have made it an increasing priority to designate gifts for endowment. Private institutions with the largest endowments have generally added less as a percentage, but did add meaningfully to endowment through giving. Financial officers can assist their institutions in both understanding the importance of giving to long-term endowment growth, and in implementing management practices and assessment methodologies that will strengthen the fundraising results.

Introduction

Endowment funds are an important source of income to colleges and universities. Although often associated with large private universities, more than four hundred mostly smaller colleges and universities report annually on the size of their endowments in the Commonfund Benchmarks Study (CBS). Endowment income is important to all of these institutions and further growth is typically an important part of their long-range plans. In addition to the Commonfund Benchmarks Study, this paper is based on an analysis of data from the Voluntary Support of Education (VSE) survey on fundraising and the National Association of College and University Business Officers (NACUBO) Endowment Study report of market values and average investment returns and spending.

Although the size, performance and purposes of endowment funds are generally known, there are many other characteristics that are not well understood. Multi-year endowment growth trends result from two principal outcomes: reinvested income and net additions. In the past few years of declining values in the equity markets many endowments experienced net investment losses, and as a result, focused increased attention on the endowment spending rule. Often the result was a decline in future endowment spending, and in some cases there was also a change in the endowment spending rule. An analysis of the common characteristics of endowment funds in higher education results in a pattern of behavior that provides insights into both the management of these funds and into the strategies that are most likely to result in continued growth and success. These strategies can be useful for improving both avenues for endowment growth.

Although most often identified with private institutions, public universities have made a major effort to expand their endowments in recent years. Sixty percent of the fundraising campaigns seeking more than one billion dollars are at public universities, although such institutions hold only about 30% of endowment assets. Endowment per student at the average public university is only 15% of that at the average private university. As state assistance continues to be reduced or to increase slowly, more state institutions will most likely devote their attention to raising gifts for both current spending and future endowment.

There are frequent reports in the press on the size and management of the largest endowment funds. At June 30, 2004, there were some forty-seven institutions with endowments over one billion dollars and thirteen of these had endowments of more than four billion dollars. NACUBO reported 741 endowment funds held \$267 billion at market value. This has the potential of producing \$13 billion of endowment income at a 5% annual spending rate. More than the size of endowment, the proportion of expenses supported by endowment income reflects the importance of endowment to many institutions. We have tried to focus our research efforts on activities that can benefit institutions with smaller endowments, but who desire to increase their endowment and its ability to support the budget.

Objectives of Endowment Funds

Endowment funds were developed to provide long-term support for the institution and its programs and are invested to provide both spendable income and principal growth to allow future spending to be at least equal to inflation (HEPI). Institutions vary greatly on their dependence on endowment income. A few rely on it for 50% or more of their support, while endowment income is less than 2% of revenues for others.

Endowment funds usually include both those funds designated by donors as endowment and those institutionally-designated funds that could be expended, but that are assigned to and invested with the endowment funds, known as quasi-endowment. In higher education, over 90% of the endowment gifts recently received are restricted as to the allocation of income within the institution. Unrestricted bequests are often a source of quasi-endowment.

Until about thirty-five years ago, many endowment funds relied entirely on spendable income as defined by the cash received from interest, dividends, rents and royalties. With the Ford Foundation report, "Managing Educational Endowments" in 1969, and the gradual adoption of its recommendations, wealth as measured by endowment market value became the primary standard for determining spendable income. This income could include some capital appreciation as well as cash income. Approval was adopted in most states through the Uniform Management of Institutional Funds Act.

The resulting focus on the growth of market values caused endowment funds to change their investment policies toward an emphasis on total investment return including both capital appreciation and income. The emphasis was usually on achieving that objective with reasonable risk and to do so by diversifying into a broad allocation of assets. Endowments can grow through reinvested returns, after spending, and through new gifts and other additions. Endowments can decline, or grow more slowly, if spending is relatively high as a percentage of recent returns or recent market values, or, if returns are diminished or negative. They also can be adversely affected if additional appropriations are made for spending from unrestricted or quasi-endowment funds invested with the endowment, or if the funds are used as a source of internal

loans for campus improvements. The evidence of the past two decades indicates that most institutions are not content to allow endowment to simply grow at the rate of inflation, which is a frequently stated goal for endowment management. Those institutions that only achieved endowment growth equal to inflation, over longer time periods, were significantly behind the faster rate of growth of most of their peers.

Endowment Gifts and the Sources of Endowment

Endowment funds at most colleges and universities did not suddenly appear at their founding although many have had relatively small endowments for much of their existence. In the early years, some schools were able to accumulate surplus operating funds or to save some large current gifts or bequests from being spent immediately. These may have been added to a founding endowment or trust to benefit the college or university. As these schools matured, growing the endowment became a continuing part of their financial operations. Spending policies were adopted that focused on the need to preserve over time, rather than spend, some of the investment returns. There was a need to assure that, over the years, the market value of their endowment funds at least kept up with inflation, and thus the spendable income would maintain its relationship to the budget in real terms. In addition, fundraising for endowment became an important part of the total fundraising effort.

Most analyses of changes in endowment market values are over relatively short time periods, such as one to three years, and focus on investment results and spending levels. In such short periods, the volatility of securities markets makes it appear that the major factor in endowment growth or decline is caused by overall market changes. Over longer time periods, such as five to ten years or more, quite a different conclusion can emerge. It is the annual additions to endowment funds from gifts that are frequently a major reason for relative success in achieving long-term endowment growth.

Our recent study of the sources of endowment growth began with a request from The Boston Consortium* in 2003. We were asked to examine the sources of endowment growth for eleven of the member schools and help them understand the key factors in the growth of their endowment funds over the prior ten years (1994-2003). We observed wide variations in total growth, gift inflows and investment performance. We might have assumed that the growth of each fund over the decade was a result of retained investment returns after spending. In fact, we found that gifts to endowment were more important than retained investment returns for some schools, even if their investment performance was above average.

Although we see little written these days about the importance of gifts to endowment growth, this was not the situation in earlier years. The report “Funds for the Future” published in 1975 by the Twentieth Century Fund Task Force on University Endowment Policy devoted a chapter to “Endowment Building” through fundraising. It is particularly revealing of attitudes at that time, following the 1973-1974 market decline. The chapter on the importance of fundraising begins on page nine and before the chapters on “Endowment Management” and “Formulating Spending Policy.” In focusing on endowment building, the Task Force urged “trustees to undertake a concerted and aggressive effort to assure its development through systematic and effective fundraising.” It went on to recommend “that every board of trustees must establish a development committee.” It cited the 1974 NACUBO survey of 128 institutions that reported gift additions to endowment averaged 3.3% for the year.

* The Consortium is currently comprised of the following institutions: Babson College, Bentley College, Berklee College of Music, Boston College, Boston University, Brandeis University, Harvard University, Massachusetts Institute of Technology, Northeastern University, Olin College, Rhode Island School of Design, Tufts University, Wellesley College, and Wheaton College.

Beginning with the eleven Boston Consortium members, we sought a larger database to understand the importance of gifts to the growth of endowment funds. Fortunately the Commonfund Benchmarks Study provides information on endowment growth resulting from gifts for 645 institutions. In addition, we were able to acquire actual giving data from 250 institutions from the VSE database, and we utilized the published figures from the NACUBO Endowment Study results to obtain endowment market value changes.

Analyzing Average Returns for Endowments Over Ten Years

We took the approach developed for the eleven Boston Consortium schools and applied the same form of analysis to a much larger sample. We had available from published reports the total growth in endowment size of some 390 college and university endowment funds over the ten years from the end of fiscal 1993 to the end of fiscal 2003. These 390 were the subset of institutions who participated in both the 1993 and 2003 NACUBO endowment surveys. In the latter year, these 390 institutions held 90% of the market value of all reporting endowment funds. We then studied the published average results for investment returns and spending for all the schools as reported by NACUBO.

According to figures published by NACUBO, the average investment return over the ten years 1994-2003 was 8.7% for the entire 2003 sample. If the average spending was 5.0% of current value over the same period, then about 3.7% would have been reinvested each year, which would have compounded to 44% over the ten years. Thus, our first estimate of the increase in the average endowment pool unit value over that ten year period was a 44% growth. Yet, our study of 390 endowments over ten years showed that the median endowment grew by 119%, based on their published market values. If true, then 75% (119% - 44%) included in the 119% came from gifts and other additions and the appreciation on these new units. Since new units were purchased at varying unit value prices over the decade, the actual appreciation on new units is not known. Knowing that the ending market value results from the unit value multiplied by the number of units, we conclude that these endowments on average had added 52% more units which were worth an average 44% more per unit than at the beginning of the decade. Inflation as measured by the Higher Education Price Index over this same decade increased by 40%, so the average endowment kept pace with inflation from reinvested returns, but grew by more than this amount from gift additions.

Looking at the numbers by category of institution, it became apparent that the importance of gifts to endowment growth and the relationship to retained investment returns varied between categories of schools. During the ten year period, almost all the large public universities and many smaller private college endowments were growing their endowments, on average, much faster from gifts than from retained investment returns. By contrast, the very largest private endowment funds with particularly strong investment results in recent years were growing their endowments more rapidly from retained investment returns. Yet the majority of endowment funds were not in these two categories and gifts to endowment were, on average equally as important as retained investment returns to the growth of endowment funds.

Using the Commonfund Benchmarks Study 2005

The “Gifts” chapter in the Commonfund Benchmarks Study for 2005 provides useful information on the importance of endowment gifts in both fiscal 2003 and 2004. In the most recent year, it showed that gifts to endowment averaged 5.5% of market value for all respondents, the same as in 2003, and 4.2% for all private colleges and universities. Although not shown in the published study, those private colleges and universities with endowments over one billion dollars added an average of 2% to their endowments from gifts last year. The CBS illustrates in other exhibits that the smaller endowments are generally adding more from gifts than the larger endowments, as a percentage of their starting market value. It also shows that the public institutions added 4.5% from gifts to their university endowments, and that private foundations in support of education added an average 8.1%.

Although gifts are not the only source of additions to endowment funds, based on reported results for endowment transfers, we believe that gifts, including bequests, are almost all the net additions at most schools. Other sources such as net operating surpluses, reinvestment of investment income and transfers from expendable funds and maturing life income plans received in earlier years can also be important. Special appropriations for spending and similar external transfers can reduce endowment funds.

The Commonfund Benchmarks Study reports on (1) investment returns, (2) spending rates and (3) gift inflows and other net additions to endowment funds. An important question is whether we can evaluate the differences among institutions in those three factors in endowment growth. In periods of relatively low investment returns, our thesis is that gift inflows are just as important as investment returns in determining endowment growth. Schools would be well served by putting the same emphasis on understanding their fundraising results relative to their most successful peers as they do in evaluating their relative investment returns. Such an effort might even produce more positive results than the same effort to evaluate their investment success. There are no market risks associated with fundraising success, no efficient markets that challenge the usefulness of most knowledge, and few large fees that may reduce returns.

Spending rates, measured by the market value at the start of each year, vary less from year to year than either investment returns or gift inflows. Almost all recognize that spending consistently above 5% of market value is not appropriate and should be reduced. There are examples of institutions that have successfully brought down relatively high spending rates over the past decade to about 5%. There are, however, a small percentage of all reporting institutions that have consistently spent 7% of market values or more. The evidence we have is that such spending is so large as to make it almost impossible to achieve endowment growth near the average of their peers.

Endowment Gift Statistics

We used various sources of gift statistics to find the aggregate total of endowment gifts at colleges and universities, as well as to understand the distribution of these gifts at specific schools. In aggregate, there were \$5.3 billion of endowment gifts in fiscal 2003 on a beginning base of \$222 billion in endowment funds at colleges and universities as reported by VSE. This indicates that gifts to endowment averaged 2.4% of market values before any other transfers to endowment funds.

To understand the differences among institutions, we studied the endowment gifts records over five years for some 250 colleges and universities. We did a detailed five-year analysis of approximately one hundred of the largest private endowments (endowments of \$200 million or more in 1999). These schools together held some sixty percent of all college and university endowment assets. We also did a detailed study of fifty of the largest public endowments. All these studies revealed a large difference among schools in the amount of gifts being added to their endowment funds each year.

To avoid the problem of large fluctuations from year to year, we obtained the gifts to endowment for each year 2000-2004 and then compared the five-year total with the 1999 endowment market value for each school. Our study of the one hundred largest private endowments was particularly revealing. We found that the average endowment giving was 2.1% a year of market value, the median was 1.8%, and one-half of the schools (25th to 75th decile) averaged between 1.2% and 2.6%. The most successful fundraising schools raised the average well above the median. The schools in the top decile of ranking added an average of more than 3.7% a year while the bottom decile added less than .9%.

We then compared our gift results with the increases in endowment market value for those schools from 1999 to 2004. Over this five year period, the mean increase in market values was 19.0%, the median increase was 15.7% and the median addition from gifts (see above) was 9.1% (or an average of 1.8% a year). This implies that almost 60% of the increase in endowment funds came just from gifts. Since sixteen percent of the schools had a decline in endowment values over the five years, the aggregate statistics are not fully comparable. It does illustrate the importance of gifts to endowment, particularly during a period of low investment returns. If forecasts of low investment returns prove to be correct, then gifts will continue to be a very important portion of endowment growth in the next five years as well.

Keys to Successful Long-Term Endowment Growth

The areas reported by the Commonfund Benchmarks Study represent the three key factors in planning for the long-term growth and success of an endowment fund: investment returns, spending policy and fundraising approach. Responsibility for the endowment is usually divided among the investment committee, an executive or finance committee, and a development committee. The investment committee typically sets the overall objectives for return and risk and determines an asset allocation. A method for “rebalancing” the endowment investments ensures that, as assets change in value, the overall allocation to asset classes continues as intended. Managers are typically hired within a desired asset class and for a particular style or approach. It is assumed that the committee and the staff have adequate resources to hire and monitor their managers and to allocate assets in accordance with policy. This is an important issue, especially for smaller institutions. Those with little or no dedicated investment staff may utilize outside advisors to assist the committee in their evaluations and deliberations.

The three key factors for long-term endowment growth are listed as follows:

1. Investment Returns

- *Asset Allocation*
- *Manager Selection*

2. Spending Policy

3. Fundraising Approach

A key component of defining an institutional investment approach is the investment policy statement. This usually defines a role for the investment committee in setting or recommending the annual endowment spending and specifies the guidelines and criteria to be used by the committee in making their determinations. The investment policy statement may also specify other attributes such as appropriate benchmarks, authority for executing transactions and spending policy. Colleges are managed by people, of course, and this process will often be more collaborative among the president, staff and trustees than implied by the investment policy statement.

Investment Returns

In seeking to obtain a high total return relative to risk, we believe the first focus should be on asset allocation rather than manager selection. If not specifically defined, committees can often devote too much time to manager selection and monitoring rather than focusing on the factors that most affect performance. Those schools that use pooled funds, such as those at Commonfund, may find it easier to focus on asset allocation rather than those that must devote most of their time to hiring, reviewing and terminating managers. Once an asset allocation or “model portfolio” is determined, the committee can go about the task of identifying appropriate means of investing the endowment in the targeted asset groups and investment styles.

While committees often spend considerable time reviewing investment results and buy/sell decisions, we believe they should allocate at least an equal amount of time assessing the results of their committee decisions. How has their chosen asset allocation performed compared with alternative asset allocation models? How have the managers selected performed compared to

those considered and not selected? How have those who were terminated compared with their replacements? Is the committee able to obtain timely and relevant information and to make a decision in a reasonable time period? Investment committees need to devote time to understanding their past investment results and how they can learn from both their successes and shortfalls. Internal staff and consultants should be responsive to the needs of investment committees to fully evaluate their choices in asset allocation as well as manager selections and funding. A committee that meets frequently, has full attendance from its members, and good staff support seems more likely to apply its knowledge to meet their long-term objectives. Investment committee members selected for their business and investment knowledge and with a multi-year, but finite, commitment to serving on the committee can be particularly effective.

Spending Policy

After disappointing results in the 1970's, rising securities markets in the 1980's and 1990's resulted in growing income for spending. It also meant that endowment income would be reduced if the market value of endowment funds declined.

Spending policy is under review at many institutions because of the large fluctuations in the past five years caused by rapidly rising followed by rapidly declining markets. Although more than 80% of endowment funds had previously used past market values in a formula to determine spending, these did not provide as much stability to spendable income as some other methods. Last year 42% of endowment funds in the Benchmarks Study reported a decrease in spending dollars from the endowment as compared with 36% reporting a decrease in the prior year. Some 29% of participants reported they changed their spending policy last year, up from 20% in 2003, and 14% in both 2002 and 2001.

Those methods that place a limit on the increases or reductions in any year while still using market value guidelines would have provided more stability in the past five years. The emphasis on holding spending over time to an annual amount at or below 5% of market value is well established if intergenerational equity is to be achieved. The Benchmarks Study reports that more than one-half of endowment funds have intergenerational equity as an important factor in setting their spending policy.

Fundraising Approach

The growth of total endowment funds over time is a major factor in the financial success of an institution. The growth in endowment fund assets over time is a function of investment returns together with the cash inflows and outflows resulting from spending, and additions from fundraising and other sources.

It should be obvious that an endowment fund that is adding 4% per year to its endowment from new gifts is likely to grow faster than one that adds 2% per year or less. While one might assume such an annual shortfall might be made up by better investment returns, we know that it is difficult achieving 2% a year more than peer institutions with similar asset allocations.

Unit Value Accounting

The Commonfund Benchmarks Study reports that about 96% of all large endowment funds keep their records on a unit value basis in investment pools. As a result, gifts are added to the endowment at their current market value and a number of units are assigned based on the most recent market value per unit. A current listing of a school's endowment funds shows the past gifts to endowment at their current market value, including all the appreciation, or depreciation, attributed to them over time. It is the growth of units as a percentage of the starting units for a time period that defines the role of gifts retained for investment in the total endowment. For example, if the number of pool units has at least doubled over twenty-five years, then at least one-half of the endowment's value came from gifts and other additions made in the past twenty-five years, including their subsequent appreciation. If there were no gifts to endowment in this example, then the market value of the total endowment would only be about one-half its size. Institutions may devote considerable time to carefully allocating investment returns over time between the needs of the present and the needs of the future, but should also understand and develop their ability to build endowment through the retention of gifts and the future appreciation on them. Unit value accounting can be a very helpful tool in clearly differentiating over time between growth from reinvested income and endowment growth from new additions. We recommend that institutions report on both the total investment return and the total growth in units on an annual basis.

Those who struggle with balancing budgets may note that gifts to endowment are sometimes restricted to new or expanded programs that are not part of its core mission. In fact, it is often the need for designated endowment funds for new programs that encourages gifts to endowment. This makes it even more important that successful fundraising policies be put in place to assure that the gifts solicited included a meaningful portion to support the core mission. Such fundraising would seek gifts that can be retained for endowment and, in addition, would add large non-recurring unrestricted gifts to quasi-endowment. These gifts often come from unrestricted bequests or are designated to its core academic units and purposes.

Gifts and Other Transfers

The NACUBO Study does not report gifts and other transfers to endowment funds for individual schools, but on Tables 24 through 27, in the 2003 study, it did report transfers to and from endowment funds as an average percentage of each school's endowment. We reviewed both the results for all schools and for those with endowment funds from \$100 million to \$500 million. It appeared that gifts and other transfers averaged 2.3% of market value for all schools, after both investment returns and spending. For the \$100 million to \$500 million endowments, the average gifts and additions were 3.3% of endowment assets in fiscal 2003. While we generally assume that "other additions" to endowment funds are a net positive, this is not always the situation. In the most recent year, the Benchmarks Study found that 17% of reporting institutions had voted special appropriations for spending beyond the normal formula for setting endowment income.

Gifts Statistics in the Five Years 2000-2004

Gifts to the endowment are the primary source of endowment growth from additions. Maturing life income plans, operating surpluses and allocations from other funds may be important in particular years, but the larger endowment funds rely primarily on gifts. Gifts from individuals or their foundations are the primary source of endowment gifts. Corporations and foundations can be important donors to endowment funds for specific programs, but usually allocate their giving for current expenditure.

We found that smaller endowment funds can often grow their endowments substantially over short time periods just from gifts. The CBS shows that some 645 institutions, including some 145 private secondary schools, had gifts to endowment averaging 5.5% of their market values. This was heavily influenced by the large giving relative to size at those 315 endowments of less than \$50 million in size. Those endowment size categories from \$51 million to more than \$1 billion had gifts averaging from 4.1% of market value (\$51-100 million) to 2.4% (\$501 million to \$1 billion).

We know that gifts to endowment, even among the largest institutions, vary greatly from year to year. This is the impact of both large gifts, including those received by bequest, and of market conditions that affect the value of appreciated securities. Bequests average 25% of all individual giving to higher education, although there is considerable variation among institutions.

The Commonfund Benchmarks Study confirms the large volatility of year-to-year endowment giving. The average increase in endowment gifts in FY2004 was 96% and the average decline was 43% with smaller institutions having the largest percentage changes. Even the biggest endowment funds, however, have large changes in their annual gifts to endowment. If we look at the year-to-year variation in 2000-2004 for those private endowments of \$200 million or more in FY1999, the median difference was 123% from the highest year to the lowest in endowment giving.

We analyzed those one hundred endowments to avoid the large annual variations caused by large gifts to small endowment funds. We then totaled the endowment giving and total giving for each institution over the five years, 2000-2004. This total of gifts was compared with the size of their endowment to get the percentage that the endowment would have increased just from gifts over that five year period. The mean increase was 10.1% and the median was 9.2%. An average of one-third of total gifts was allocated to endowment (33.7% for the mean and 33.3% for the median.) Only 8% of the schools had endowment gifts of 50% or more of total giving and only 12% had endowment gifts of less than 20% of total giving. Since gifts buy into unitized pools at varying unit values, the exact effect of gifts can only be computed for each institution.

One might expect those that had a large percentage of gifts going to endowment would also be growing their endowments from gifts at a higher than average rate. In fact, there is only a weak correlation between the average allocation to endowment gifts and the percentage of endowment growth that came from gifts over the five years. The schools whose endowments are added to most rapidly from gifts are also the schools with the largest percentage of total giving for all purposes relative to the size of their endowment. Several schools with very large endowments do allocate a higher-than-average proportion of their total gifts to endowment, but both endowment gifts and total gifts are still below average as a percentage of their total endowment. For these schools, decades of successful fundraising and the favorable retention of net investment returns creates a large endowment relative to their current fundraising potential.

The list of the fastest growing endowments is largely populated by the large public universities and their foundations. By looking only at separate gift statistics for the private colleges and universities, we are able to identify the private colleges and universities that were also high achievers. We generally categorized high achievers as being in the top quartile and usually in the top decile of endowment giving relative to the size of their endowments. More broadly, we looked at those schools with the strongest giving to endowment as a percentage of the size of their endowment in their Carnegie category.

Looking at the High Achievers

Using the endowment gift and endowment growth statistics for the past five years (2000-2004):

- A private university added 38% just from gifts leading to a 51% increase in the market value of its endowment.
- A private university added 16% just from gifts leading to a 27% increase in the market value of its endowment.
- A private university added 19% just from gifts helping it to achieve a 62% increase in the market value of its endowment.

Using endowment gift statistics for the ten years (1994-2003) combined with each school's ranking in the U.S. News and World Reports Best Colleges Survey, we computed the total gifts over ten years to endowment as a percentage of their 1993 endowments at market value:

- A US News top five university added 77% from gifts.
- A US News top thirty university added over 100% from gifts.
- A US News top ten liberal arts college added 76% from gifts.
- A US News top fifty liberal arts college added over 100% from gifts.

Organizational Commitments for Increasing Endowments

To successfully build endowment from both investment returns and gifts requires a commitment from the trustees, the president and the faculty. Our study shows that many organizations have been able to grow endowment even while growing their annual fund and other current giving levels. Thus, effective endowment fundraising can take place while also successfully raising expendable gifts. In addition, we believe that consistent and robust investment results can assist in fundraising because of the donor confidence it inspires in the endowment as a desirable “investment” vehicle.

There are examples of schools that are already bringing together a team from both fundraising and investment management to do this effectively. Among the large universities, we know that at least three have developed effective ways for fundraisers and investment staff to work together in communicating with potential donors of endowment gifts.

Skilled fundraisers are usually needed to assist the president and trustees in soliciting gifts to endowment. Just as important, they need to manage the long-term relations that are often necessary to develop really large gifts. These can be summarized as follows:

- Institutional commitment to build the endowment.
- Developing an overall plan that includes:
 - ▶ Encouraging gifts for long-term investment.
 - ▶ Encouraging cooperation among investment, development and financial staffs.
 - ▶ Communicating the importance of endowment in publications and meetings with alumni and friends.

When we read of single large gifts to endowment funds, we know that the donors of such support are often associated with the institution in some long-term relationship. In our experience, presidents and deans who work closely with their professional fundraisers and key trustees are the most effective teams to achieve fundraising success. The development of large gifts sometimes occur over many years and even over many decades. As a result, these important efforts may not readily respond to financial incentives that relate to gifts received rather than relationships developed or maintained.

In addition to the trustees, president, and faculty, chief financial officers needs to play a role in this process. Their role should include:

- Building staff capacity in all the functions necessary to bring in gifts to endowment.
- Building confidence in endowment management and stewardship.
- Helping fundraisers understand the endowment and endowment policies.
- Encouraging unrestricted bequests be added to endowment.
- Encouraging creative giving.
- Being a friend to the major gifts staff.

Importance of Bequests and Life Income Plans

We know from annual surveys of fundraising results that over one-fourth of individual giving comes in the form of bequests and the present value of deferred gifts. While bequests can be directed to any purpose, we believe that one measure of success is the relationship between average annual bequests and the total endowment fund. A good measure from our study of the one hundred largest private endowments over the past five years is that bequests of 1% a year, as a percentage of endowment market value, is about the mean. There is a large difference among institutions with the top decile adding 2% a year or more while the bottom decile did 0.4% or less a year.

We also know that many schools try to allocate most of their large unrestricted bequests to quasi-endowment funds. As a result, bequests are an important part of almost all efforts to expand gifts to endowment. When we look at the high achievers, they all have strong bequest and deferred giving programs. Overall gift statistics show that the present value of life income plans, at the time of the gift, is only about 20% of the value of bequests within any period. Those managing planned giving programs should be knowledgeable in all forms of giving. They do need to devote time to the stewardship of potential estate donors even though it is often difficult to understand the value of these efforts except over long time periods.

It is particularly important that the president and key trustees understand that the potential donors of large bequests include some alumni and friends who may not be among your largest donors during their lifetimes. Many of these potential donors are elderly and may not be able or interested in meeting with anyone except long-time friends from your school. Many have no direct family heirs. One measure of success is the ability to become the principal or primary beneficiary of their estates. Such bequests frequently come from those who lived modestly and never achieved leadership in their profession. They did know how to build or preserve financial wealth and also how it can be effectively used by future generations.

Summary

Most colleges and universities have long-term plans to increase their sources of revenue, including through endowment growth. The large investment returns over the last two decades of the twentieth century caused a strong emphasis on investment returns and moderate spending policies. While these factors are important, we find that gifts have been and continue to be just as important to the growth of endowment funds.

We recommend that college and university trustees together with their president, deans and vice presidents, review and renew their efforts to build endowment funds from all sources. We believe that a careful analysis of past investment results and future expectations can help achieve strong investment results. This should include a careful understanding of the investment policies and asset allocation strategies and their reasons for success or disappointment. Efforts to grow endowment must also focus on endowment giving. If successful, they can make a very meaningful change in the resources available to both the current and future generations. Fortunately there are many examples of high achievers in these efforts today and we encourage the success of those who make this increased effort.

Biographies

Glenn Strehle is a Principal and Founder of Campus Business Advisors, LLC. This consulting firm assists in endowment and debt management and in developing effective administrative and financial practices in higher education. He retired from MIT in 1998 as Treasurer Emeritus.

Fred Rogers is currently the Vice President and Treasurer of Carleton College. He is a Principal and Founder of Campus Business Advisors, LLC. He is the Senior Vice President Emeritus of Cornell University and also served as the Chief Financial Officer of Carnegie Mellon University.

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