Special Report **April 2025**

Latest Endowment Study Shows Positive Gains in FY 2024

Strong Investment Returns and Growing Gifts Propel Endowments

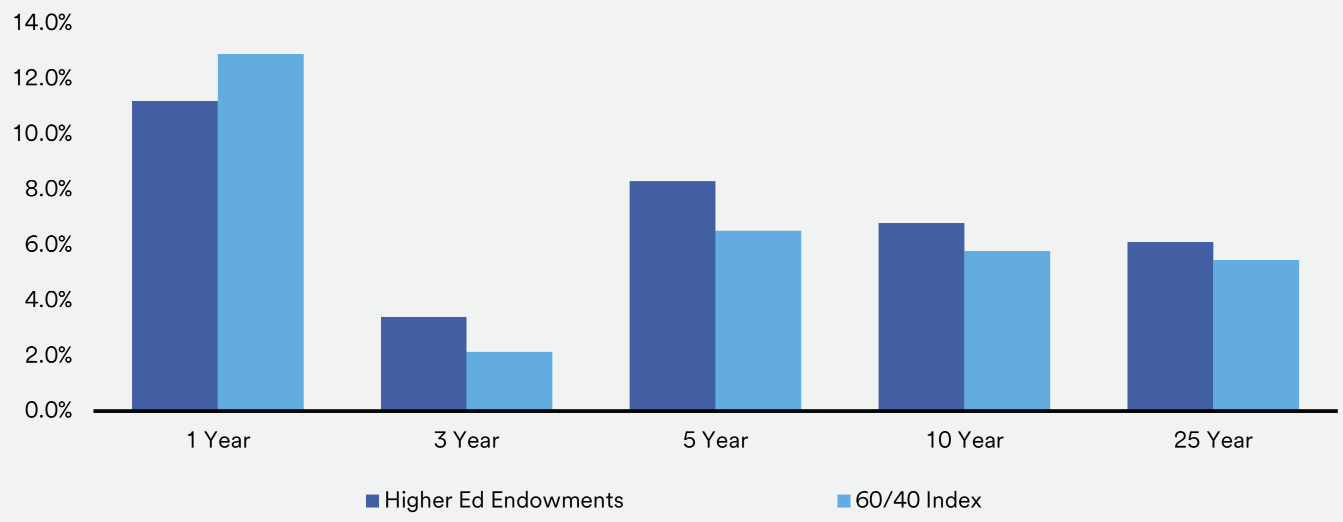
In a year marked with challenges and surprises, endowment returns continue to outperform a 60/40 index over the long term. The addition of alternative strategies, which provide diversified return streams from non-correlated assets classes, often helped dampen volatility and produce positive contributions. Endowment returns bested a 60/40 index for the trailing 3-, 5-, 10-, and 25-year returns ending June 30, 2024.

According to the 2024 NACUBO-Commonfund Study of Endowments (NCSE) published earlier this year, U.S. higher education endowments returned 11.2% on average for the fiscal year (FY) ended June 30, 2024. This is an improvement from the 7.7% return that was reported in FY 2023. Six of the seven endowment cohorts (by size) achieved double-digit returns with the largest cohort (by size) earning a 9.1% return.

The dispersion between the cohort groups was 390 basis points (bps) versus 980 bps last year. Looking at longer horizons, the 10-year annualized rate of return was 6.8% in FY 2024 while the 25-year annualized returns moved to 6.1%.

While higher education endowments experienced strong returns, we compared NCSE's annual return of 11.2% to the 12.9% annual return of a balanced 60/40 portfolio (60% MSCI ACWI (net) Index and 40% Barclays Aggregate Index). It was the only period where endowment portfolios trailed the 60/40 index. The outperformance of the 60/40 index relative to endowments can be partially attributed to a large allocation to domestic equities within the MSCI ACWI. Since domestic equities were a strong performer once again, the large allocation propelled the index's return. In addition, endowments generally maintain sizeable exposures to public and private real estate which dragged on performance. Real estate is not represented in the 60/40 index.

Average Annual Returns for U.S. Higher Education Endowments Compared to a 60/40 Index as of June 30, 2024

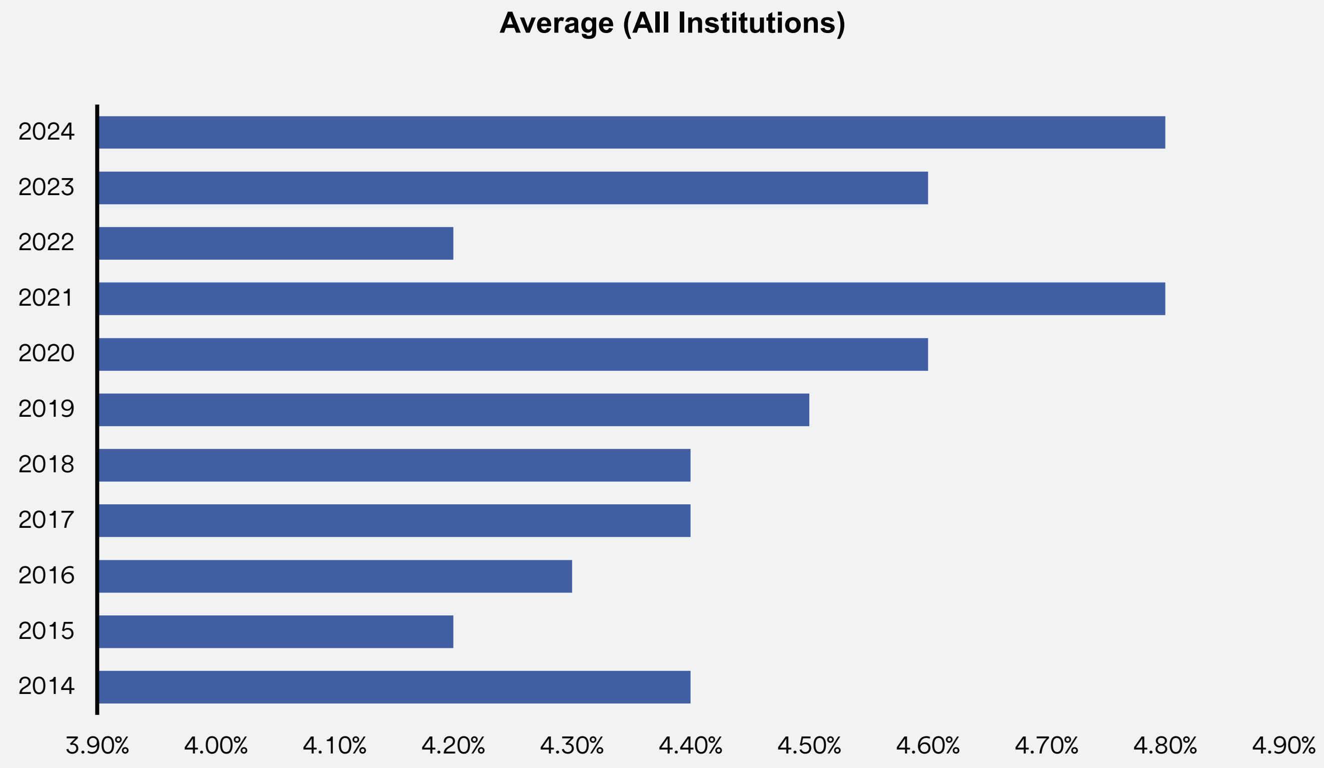


Endowments as represented by the 2024 NCSE. Returns are net of fees. 60/40 Index as represented by the 60% MSCI ACWI (net) Index and 40% Barclays Aggregate Index.

In addition, survey respondents show total new gifts increased from $12.4 billion last year to $15 billion in FY 2024, a 21% increase. The combination of rising gifts and positive returns propelled endowment assets, of those surveyed, from an aggregate of $819.0 billion last year to $873.7 billion this year.

Effective Spending Continues to Rise

The 658 surveyed institutions reported an average annual effective spending rate (by endowments) of 4.8% in FY2024. That marked an almost 5% increase from the 4.6% in FY2023. Spending has now returned to the previous high reached in 2021.

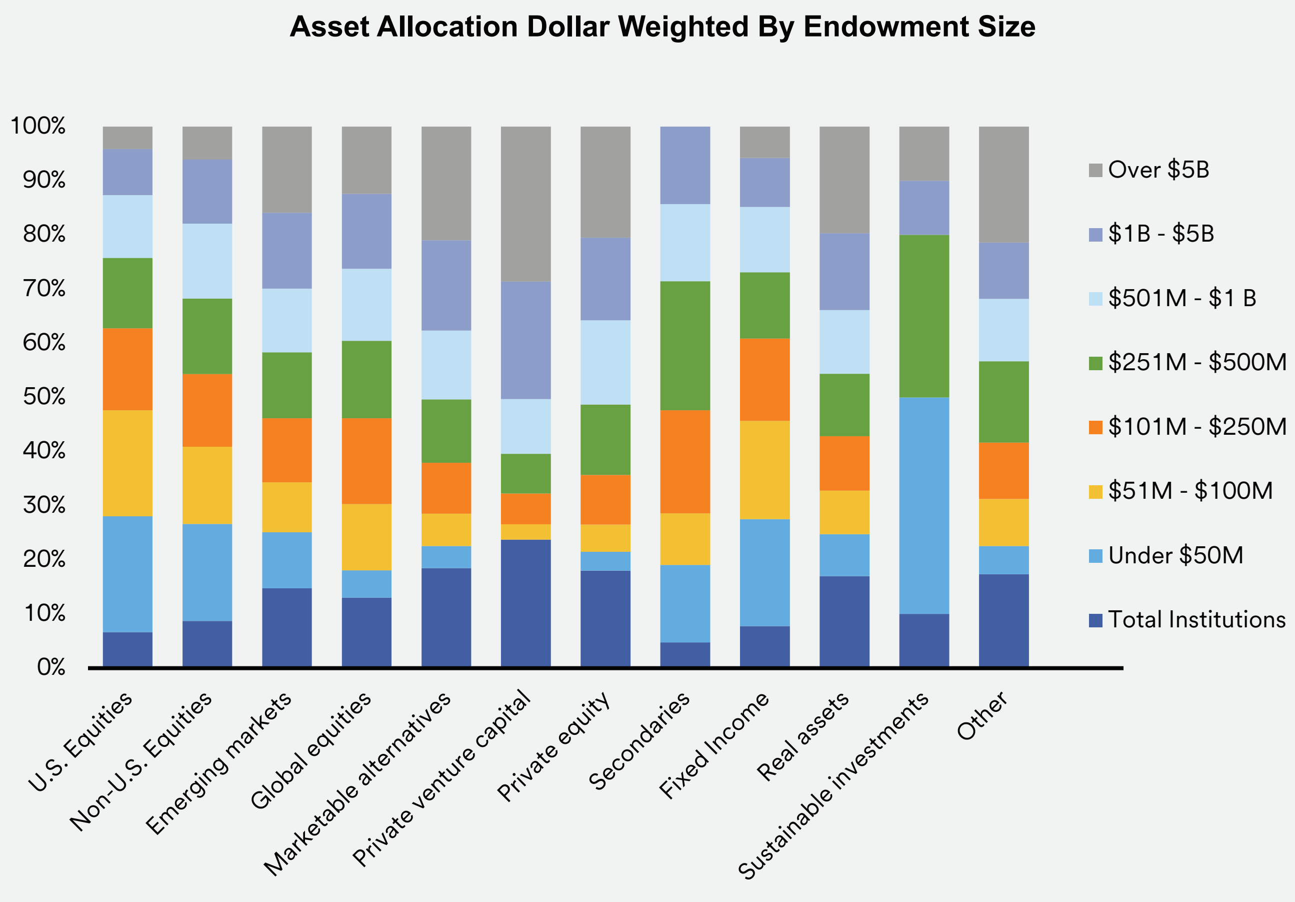


2024 NCSE. All data is reflected as of June 30 each year-end. The effective spending rate represents the distribution of spending divided by the beginning market value (endowment value on or around the beginning of the fiscal year). The distribution for spending is the dollar amount withdrawn from the endowment to support expenditures on student financial aid, faculty research, maintenance of facilities and other campus operations, as determined and defined by each institution. The rate is calculated net of any investment fees and expenses for managing the endowment.

Across all institutions, student financial aid accounted for 48.1% (highest category) of spending policy distributions in FY 2024, while campus operations and maintenance accounted for 6.7% (lowest category) of spending. In total, academic programs and research, endowed faculty positions and “other” accounted for 45.2% of spending.

Asset Allocation

FY2024 was the second year in a row where U.S. Public Equities lead asset class performance. Endowments of under $50 million in assets allocated 42.1% to U.S. Public Equities, compared to endowments over $5 billion that allocated just 8.1%. These allocations benefited the smaller institutions in FY 2024 (as they did in FY 2023), where the average yearly return for endowments with $50 million or less was 13.0%, compared to 9.1% for endowments with over $5 billion. Larger endowments tend to have their greater exposures in the alternative areas than do smaller endowments.



2024 NCSE.

Responsible Investing and DEI Initiatives

In FY 2024, 84% of institutions that responded to the study include environmental, social and governance (ESG) in their investment policy. Regardless of stakeholder group (students, alumni, employees, donors and grantmakers) all show a slow but growing interest in ESG investing. Yet 62.5% of respondents said they still did not practice responsible investing in any form.

Interestingly, 58.8% of institutions in the largest surveyed cohort considered responsible investing as a potential source of alpha, compared to only 13.5% of the smallest endowments. However, it should be noted that actual implementation of ESG/SRI/Impact Investing strategies do face some notable headwinds. The 2024 study highlights that 36.2% of respondents mentioned that their use of pooled fund structures (including private investments) makes it difficult to implement these strategies. Another 34.3% of respondents expressed concern about the "potential adverse impacts on investment performance." And another 30.6% cite potential conflicts with the board's fiduciary duty to ensure mission sustainability.

On diversity, equity and inclusion (DEI) initiatives, an overwhelming 94.7% of participants voiced that some level of gifts in FY 2024 was tagged to support DEI initiatives.

Top Concerns

This year the Study introduced a new area of inquiry by asking participating institutions to identify their top two concerns from a list of 20 choices. Respondents were asked to select their top two without ranking them.

The number one concern, cited by 23.2% of respondents, was student enrollment. It was identified at more than twice the rate of the number two concern, which was fundraising, which was selected by 12.0% of respondents. When considering the same data across the different endowment cohorts (by size), the largest endowments were more concerned about liquidity and not meeting target returns.

Our View

As we continue to face an evolving and uncertain market environment, with an expectation of challenged investment returns over the intermediate-term but improving over the long-term, we believe that it is important for institutions to remain up-to-date with their investment and spending policies while being mindful of the costs associated with their investment program. Here are a few considerations in view of the latest NCSE study:

- With demands on endowment funds increasing, institutions may consider revisiting their target asset allocation to ensure portfolios are positioned appropriately given the expectations for returns, inflation and fees associated with their endowment program.
- After two back-to-back strong years in the domestic equity market, it might be a good time to examine the mix of active and passive exposure by asset class. A quick review of the dispersion of manager returns in each asset class can give you an indication of whether it pays to be active. Low dispersion among manager returns means that alpha is hard to find. High dispersion shows alpha is available and worth using active managers to try and find it.
- With respect to fees, costs are one of the few things that can be directly controlled and should be monitored regularly. Institutions should consider reviewing all external vendor contracts related to the endowment to ensure reasonable fees are being expended to support the endowment.
- Lastly, it may be a good time to revisit your board education plan for the year. Managing expectations is a critical component of successful endowment management. After several years of compelling returns, the board might need a refresher on the cyclical nature of investment returns and the need to remain vigilant and prudent in their portfolio positioning.

Please feel free to reach out to your relationship manager if you have any questions.

Sources

https://www.nacubo.org/Research/2024/NACUBO-Commonfund-Study-of-Endowments