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Endowments and Foundations See Losses in Early 2022 Numbers

Following a year of record returns, a volatile market is already impacting nonprofit portfolios, but it could be months before the true level of damage is known.

By Justin Mitchell

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Foundations and endowments are already seeing losses in their portfolios amid this year's market tumult, but things could get even worse once final private markets numbers start coming out later this year.

Wilshire's Trust Universe Comparison Service on Tuesday released its numbers for the second quarter of 2022 as well as the 2022 fiscal year that ended on June 30.

Across all plan types, one-year returns were down, but foundations and endowments with assets over $500 million had the smallest drop, at -1.15%. The drop in the second quarter was larger, coming in at -5.33% for large endowments, Wilshire said.

There was a wide spread between these larger nonprofit pools and smaller ones. Foundations and endowments with less than $500 million in assets saw declines over 10% in the second quarter and over 12% over the year, the Wilshire numbers show.

Across all the corporate and public pensions as well as foundations and endowments measured by Wilshire, the median return was -9.63% for the second quarter and -10.59% for the year ending June 30.

Due to nonprofit investors' heavy allocations to private markets, which are reported on a lag of at least a quarter, the damage is likely be much worse than initially shown, said **Jim Dunn**, chief investment officer of **Verger Capital Management**, an outsourced chief investment officer, or OCIO, that works mostly with nonprofit investors. The Wilshire numbers are likely using private markets numbers for the first quarter at the latest, he said, and things have only gotten worse since then, and that will eventually be reflected in return numbers.

"For those that will include them, it'll definitely be a drag on their performance," he said. "For those that don't include them, they'll look better, but they'll take that hit in fiscal year [2023, so] that will take awhile to show up in the numbers."

Last year was an historic year of returns for foundations and endowments, with public and private equities as well as venture capital providing explosive returns, as reported. Since then, the Federal Reserve has begun aggressively raising interest rates and macroeconomic developments such as Russia's invasion of Ukraine have triggered a simultaneous drop in both public equities and fixed income, wreaking havoc for many investors.

"It's really difficult to create a portfolio that can capture the upside last year … and then avoid the downside this year," Dunn said. "A lot of portfolios aren't built that way."

While the one-year returns will be rough for endowments, it is important to focus on the long term, said **Kane Brenan**, CEO of **TIFF Investment Management**, another nonprofit-focused OCIO firm.

Fiscal 2021 was a "rubber-band year," as portfolios bounced back from the covid-ravaged first half of 2020, he said. Since many endowments had "gangbusters" returns for fiscal year 2021, a lot of that upside will still show up in longer-term returns.

"[If] you zoom out over the last two years, three years, ten years, [or] 15 years, I don't think anyone's going to look at June of 2022 and say, 'oh my gosh, we were doing everything wrong,'" he said. "Because if you look out over a slightly longer period, [you could say], 'wow, actually, we did a lot of things, right.'"

One way to possibly get an early idea of what private market drawdowns might look is the secondaries market, said **Brad Alford**, founder of OCIO search consultant **Alpha Capital Management**, where private equity investors sell off illiquid holdings.

"[Secondaries investors] really underwrite [stakes] and look at the underlying companies and really give you a third-party valuation rather than the owner of the assets valuing [the stakes]," he said.

Data from **Jefferies** shows private equity and venture capital stakes being sold at a record volume in the second half of 2021 and the first half of this year, according to the Financial Times. Stakes in buyouts, venture capital and real estate funds were selling at 86% of their face value on average, with stakes in venture capital funds selling at just 71% of their most recent valuations.

Dunn was skeptical that drawdowns of that level would be reflected in private valuations for the second quarter.

"I think people are pushing it out. They're waiting to see what happens," he said.

In conversations with endowment investors, Brenan says that while nobody is sure what final returns will look like the this fiscal year, they continue to believe in the so-called "endowment model" pioneered by former **Yale University** CIO **David Swensen**, who died last year.

In fact, investors will need to be ready to take more passive, active or liquidity risk or a combination of all three to maintain strong returns going forward as the landscape changes from the low interest rate environment that dominated over the last few years, Brenan said.

“In a world with this much macro volatility, you have to be nimble,” he said.

Michael Taffe contributed the graphics in this piece.