'Banner Year' Doesn't Mean 'Money in the Bank' for Endowments

While many university endowments saw incredible one-year returns in the 2020 to 2021 fiscal year, that does not mean they are awash in cash. Sources say careful planning for the future is called for.

By Justin Mitchell | **December 9, 2021**

Even as the world reeled from the coronavirus crisis, institutional investors, and especially university endowments, experienced some of the best returns they had ever seen between the middle of 2020 and the middle of 2021. But that doesn't mean they are awash in cash.

The key to the returns was the endowments' tendency to have high allocations to riskier asset classes like public equities, private equity and venture capital. Among the Ivy League schools, institutions like Brown University with higher levels of risk in their portfolios performed better than other schools, such as Harvard University and Columbia University, that had less.

These kinds of allocations were handsomely rewarded. Many endowments have seen the market value of their assets skyrocket. Brown's endowment was valued at $6.9 billion as of June 30, up from $4.7 billion the year before. **Duke University**'s endowment grew to $12.7 billion from $8.5 billion on a 56% return. The Massachusetts Institute of Technology had a 55.5% return and grew to $27.4

billion. Princeton University had a 46.9% return and saw its assets grow from $26.6 billion to $37.7 billion.

That looks like a lot of money on the table. Some schools have increased spending on things like financial aid, in the case of Brown.

Still, others say what appears to be a cash windfall can be deceptive.

In a recent edition of his newsletter, Charles Skorina, managing partner at search firm **Charles Skorina & Company**, brought up the idea that many of these private equity and venture capital returns were unrealized, meaning that even though holdings these endowments have in private equity and venture capital funds may be valued highly, that does not mean the investors have seen any of that cash. Indeed, they may not for years – if at all.

"The [venture capital managers] can hang onto distributions for two or three years," Skorina told FundFire. "There's nothing the limited partners can do. If they say, 'God, we have got to have some cash now,' it doesn't matter."

Data from **Pitchbook**, as of March 31, 2021 shows an increasing level of unrealized returns for both private equity and venture capital.

"This means that some of the returns we have reported are based on estimated valuations rather than locked-in results," the Pitchbook report said. "Should those estimates not be realized, these phenomenal results could be rescinded."

In particular, the last five quarters of venture capital showed a "massive amount" of unrealized returns.

"This represents value that is at risk of not coming to fruition," Pitchbook said.

Mary Cahill, chief executive officer and chief investment officer of **Acansa Investment Management Group**, and the former longtime CIO for **Emory University**, put it bluntly in an email to FundFire: "Gains on paper are not the same as money in the bank."

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The pressure from unrealized returns speaks to a general tension currently being faced by institutional investors. A recent paper from consultant Verus examined the tension between assets that provide value primarily through income and assets that provide value primarily through price appreciation.

At one time, income, especially that provided through bonds, could often get an institutional investor to their target returns, said Verus Director of Strategic Research **Thomas Garrett**. Now, in an investment

landscape marked by long-term low interest rates, investors have to make up the difference through price appreciation – which means putting more capital into risker, growth-oriented asset classes like equities, private equity and venture capital.

When the next market selloff comes, investors that have been forced to take on more risk and to “reach a little bit more for returns” will be exposed to greater potential losses.

“That’s a central theme in the market environment that many investors are facing at the moment,” Garrett told FundFire.

While the headline numbers have been “exciting,” many investors know that much of their gains are unrealized and are looking for ways to rebalance, said **Jeff Mindin**, chief investment officer at **ASU Enterprise Partners**, which invests on behalf of **Arizona State University**. Despite this “banner year,” he said now is a good time to rebalance, before the market turn comes.

“When these gains are illiquid and unrealized, it does add some complexity into that rebalancing question,” he told FundFire. “But I think this is the time to be having those rebalancing discussions.”

As always, chasing “yesterday’s returns” is not a winning strategy, Cahill said. She encouraged endowments to stick with their long-term strategy. Still, she did recommend endowments consider “targeted

opportunities" to sell some venture and private equity holdings on the secondaries market as part of a rebalancing process.

Verus is telling its clients much the same thing – to rebalance back to their target allocations, Garrett said. Market drawdowns are not actually that unusual, he warned.

"We kind of like to think about expecting the unexpected," he said.

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