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Endowment and Foundation Update

Key 2023 trends for the endowment, foundation, and nonprofit marketplace

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SEPTEMBER 2023

The following article summarizes key trends we're observing from the many nonprofits we work with in the endowment and foundation marketplace. The Wilmington Trust Endowments and Foundations team categorized them into investment and fundraising trends, since these are the two key ways to grow endowment funds. With the pandemic essentially behind us, many nonprofits are now assessing their endowment strategies, fundraising goals, and strategic plans in light of a slowing economy and stubborn inflation.

INVESTMENT-RELATED TRENDS

Higher interest rates, stubborn inflation, a slowing economy, and the Russia-Ukraine conflict are leading many nonprofits to assess their endowment strategies

Lingering inflation, rising interest rates, and the Russia-Ukraine conflict are leading to greater uncertainty on the U.S. economy and capital markets. With the S&P 500 index* finishing down almost 18% in 2022, nonprofit boards are reviewing their endowment strategies and strategic plans. Many boards are reassessing their asset allocations and liquidity positions, while numerous nonprofits are dealing with a new world without the CARES Act funds and other government funds that supported their operations. Investment committees are also speaking regularly with their investment advisors about their risk levels and applying stress testing to their portfolios.

Boards also continue to monitor and refine their investment policy statements, which include strategic and tactical asset allocation targets and endowment spending rates, as market returns are expected to be lower over the next decade. Some nonprofits have assessed their spending levels. In these current times, endowments and foundations are also asking about the overall value-add services, such as fundraising insights and peer review comparisons, as they seek to grow their endowments in other ways, such as through fundraising.

* The S&P 500 index measures the stock performance of 500 large companies listed on stock exchanges in the U.S. and is one of the most commonly followed equity indices.

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At a glance:

- **Lingering inflation and geopolitical tensions continue to add uncertainty on the U.S. economy and capital markets**
- **The stock market has rebounded through mid 2023 but nonprofit boards are still reviewing their endowment strategies and strategic plans after a difficult 2022**
- **Many nonprofits are seeking ways to grow their endowment funds through a holistic approach that includes fundraising**
- **Fiduciary responsibility remains an important topic, especially during these unusual times**

Observations

While the stock market has rebounded through mid-2023, there continue to be a number of risks we are following such as inflation trends, interest rates, a slowing economy, and the geopolitical environment. Our Investment Committee is in constant discussion as we continue to evaluate the economic ramifications of the Russia–Ukraine war.

Many nonprofit investment committees have had to quickly review and respond to the new world of market volatility related to higher interest rates and geopolitical concerns. Some investment committees have reviewed their asset allocations more closely, and most of our endowment and foundation clients have maintained their target allocations and focus on being diversified. Some investment committees have moved to rebalance back to their targets, while some more conservative committees have remained underweight to their equity targets. Portfolio stress testing has become an important part of our client dialogue.

A number of clients have taken a closer look at their spending policies and have reviewed the study recently posted by the National Association of College and University Business Officers (NACUBO), which provides useful benchmarks for asset allocation, spending, and returns for colleges and universities (www.nacubo.org). A main focus is also having enough liquidity in the portfolio for day-to-day operations. *Pensions & Investments* magazine noted that higher allocations to private equity have benefited some larger nonprofits' portfolios.

Many nonprofits continue to review their overall fee structures, including their direct advisory fees and the imbedded manager/mutual fund/ETF costs. Some nonprofits have commented on their desire in having a higher level of valued-added services to help them reach their overall missions.

The Federal Reserve (Fed) continued to raise short-term interest rates in July to fight inflation, which has impacted fixed income returns

In March 2022, the Fed started to raise short-term interest rates as a result of higher inflation and a return to normalcy. The number of increases has been data dependent. This has improved the returns on short-term fixed income portfolios, and at mid year we continued to have an inverted yield curve. Longer-term rates have also risen, which has hurt longer-term fixed income values. However, investing in fixed income potentially offers a better return for investors going forward.

Observations

The higher short-term interest rates in the market are beneficial to nonprofits as they are now seeing higher yields on their operating funds. It may also allow them to earn more competitive returns without having to take on greater risks. We have a number of clients that are assessing the different options available in the money market and bank deposit arena. For longer-term portfolios, many nonprofits allocated more to core and intermediate fixed income to take advantage of the higher rates. Some are watching their credit exposures through their corporate bond holdings. Some clients had been considering the addition of new strategies such as high yield and hedge funds. Nonprofits have also had to review their borrowing costs in a world with higher rates.

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With geopolitical turmoil and potential interest rate hikes, nonprofits seek to be even more diversified with their fundraising plans, especially nonprofits that are focused on special events (e.g., galas, golf), direct mail, and significant government funding (e.g., health care, social services, and public colleges), which is prone to government cutbacks.

Continued interest in Socially Responsible investing

There continues to be interest in SRI (socially responsible investing) and ESG (environmental, social, and governance) investing. SRI refers to situations where we screen portfolios to avoid certain types of stocks (e.g., fire arms, tobacco, alcohol, etc.). On the other hand, ESG investing is when our managers actively try to identify companies with three attributes (environmental, social, and governance) in their businesses and potential for strong long-term investment returns.

Observations

We have worked with a number of nonprofits over the years that have followed specific SRI criteria. For example, Catholic organizations follow the U.S. Conference of Catholic Bishops (USCCB), which releases guidelines, and health care organizations often have their own restrictions. The USCCB in November 2020 released updated investment guidelines that refine their earlier restrictions. Other religious groups have their own specialized screens; for example, one church was focused on excluding weapons, while another church was reviewing fossil fuel stocks. We have seen interest from some clients as they explore ways to add ESG strategies. One private school was following its own ESG criteria, while another church was planning to implement some impact investing criteria. A number of investment managers have been incorporating a sustainable investing overlay into all of their strategies. We also started to help our clients with requests related to custom indexing that allows for SRI at a passive level.

Wilmington Trust's Head of Sustainable Investing and Senior Equity Portfolio Manager Steve Norcini authored a thought leadership piece on this topic, *Sustainable Investing: Redefining Investing for the Long Term.*

Governance: Fiduciary responsibility remains an important topic, especially post COVID

Each nonprofit sector was impacted differently by the pandemic, requiring an assessment of strategic plans, endowment levels, and fundraising strategies. Now with geopolitical concerns on the table, boards are reviewing their sustainability and looking at different scenarios for the future.

Observations

Some nonprofits have moved to update their investment policies and some have added underwater endowment language to their investment policy statements. We have had a number of emerging nonprofits that have received significant unrestricted donations ask about starting or growing their endowment funds; we have developed an educational module called "How to Start an Endowment" in response. We continue to offer client education sessions that seek to help our nonprofits understand their fiduciary responsibilities, especially for newly established endowment programs. On April 25, 2023 we held session #102: *Private Foundation Panel: Current Developments on Accounting, Compliance & Investing* to help our private foundation clients understand the current trends.

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Planned giving continues to be a very important fundraising channel for many nonprofits.

FUNDRAISING-RELATED TRENDS

Nonprofits continue to diversify their fundraising strategies and revenue sources in a post-COVID world

Nonprofits now find themselves in a post-COVID world, with a slowing economy and greater uncertainty. Many nonprofits are dealing with a new world without the CARES Act funds and other government funds that supported their operating budgets. They are also having to deal with much higher inflation (8% in 2022), higher interest rates, a difficult hiring environment, and a slowing economy (read what our Wilmington Trust investment team is thinking in our July/August edition of *Capital Perspectives)*.

The regional bank crisis has also impacted some nonprofits through their local financial and philanthropic relationships. These challenges are reminding nonprofits of the importance of having diversified revenue sources. Fundraising plans are also becoming more diverse, especially for nonprofits that are focused on special events (e.g., galas, golf), direct mail, and significant government funding (e.g., health care, social services, and public colleges), which is prone to government cutbacks. Many nonprofits see the importance of having diversified fundraising plans that include planned giving options and enhanced technology plans. They also see the importance of starting and growing their endowments/quasi endowments, which are a very important resource during times of stress.

Fundraising for 2022 was much weaker than expected, as *Giving USA* reported a 3.4% decline (10.5% decline, inflation adjusted) in charitable giving from 2021.* After inflation, this is only the fourth time that giving has dropped since the report started in 1956. Giving also fell in 2008/2009, a result of the Great Recession, as well as in 1987, after the significant stock market drop. The *Chronicle of Philanthropy* commented that economic factors may have influenced giving, such as the stock market decline and much higher inflation, which impacts a family's financial capacity. At the same time, total giving was almost $500 billion in 2022, which shows how philanthropic Americans are even in these uncertain times. Over the past few years, these totals have been positively impacted by the estimated $14 billion in unrestricted, one-time gifts (more than 1,600 nonprofits) made by American novelist and philanthropist, Mackenzie Scott, to a variety of charities.

The Chronicle also goes on to mention that as a result of some of their preliminary research, they are seeing sluggish giving trends through mid-2023, which is leading to a continued challenging environment. Their research shows that there have been fewer $1 million gifts through the first five months of the year compared to 2022. Candid also has reviewed their foundation data which suggest that foundations may have lower giving levels in 2023 due to the volatile stock market (www.candid.org).

Observations

According to the 2022 *Giving USA Report*, we saw the sources of giving as: individuals 64%; foundations 21%; bequests 9%; and corporate contributions at 6%. As a comparison, 1982 showed: individuals 81%; foundations 5%; bequests 9%, and corporations at 5%. If you include bequests and half of the foundation giving, individual giving is approximately 83% of all giving, a key component. They also reported that giving by individuals grew by an annualized 4.9% over the last

* Source: www.givingusa.org

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Additional observations

Blackbaud Institute Charitable Giving Report for 2021:

- Online giving grew 9% versus 6.8% in the prior year
- Over the 36-month period since 2018, online giving has grown 42%
- Approximately 12% of overall fundraising revenue, excluding grants, was raised online
- Average gift is at $204, about 15.3% higher
- Reports that 28% of online donations were made on mobile devices

Source: https://institute.blackbaud.com/charitable-giving-report/

Please note: Blackbaud has not published a new report for 2022.

40 years, while foundation giving grew by 9.2%, a more important channel in recent years.

It was also reported that individual giving as a percentage of disposable personal income was 1.7% in 2022. In prior years, it was closer to 2.0%. Corporate giving as a percentage of corporate pre-tax profits has also trended down to 0.9%.

Giving USA also reported that giving to international affairs and foundations were the only two areas that grew faster than inflation. The giving level for international affairs is impacted by international crises, such as the current Russian invasion of Ukraine.

The Chronicle commented that donor advised funds (DAFs) continue to grow in importance as a funding source for nonprofits. At the same time, new donor advised funds to Fidelity Charitable were flat in 2022 and lower at Vanguard Charitable. Donor advised funds were one of the fastest-growing areas in 2020 and 2021 and remain a key fundraising trend. We have had a number of clients ask about how to benefit from DAFs as a fundraising and planned gift strategy. We will be covering DAFs in our session #104, *DAFS for 2023 and Beyond* on September 21, 2023.

Planned giving continues to be a very important fundraising channel for many of our nonprofit clients. Bequests continue to be an important part of planned giving programs.

We had our Philanthropic Speaker Series session #101 on Bequests on March 2, 2023 with expert Lori Kranczer, *Bequests Revisited: Expanding Bequest Programs in Current Times*, where Lori discussed how to start and build a successful bequest program.

Planned giving remains a key focus area

Planned giving continues to be a very important fundraising channel for many nonprofits especially in this new world. The *Giving USA* annual report (www.givingusa.gov) showed that 9% of all giving in 2022 ($45 billion) was related to bequests, a key planned giving option. One important planned giving strategy for nonprofits has been the use of legacy societies, which help to cultivate planned giving donors.

Ellen Dudas, MNA, CAP®, president of Planned Giving Advancement, spoke at Wilmington Trust Philanthropic Speaker Series session #103 on the *Planned Giving Strategies for 2023 and Beyond: Back to the Basics.* During the session, Ellen commented on the importance of building and enhancing your planned giving programs in these changing times.

> *"I have the privilege of collaborating with numerous nonprofits as they embark on establishing or expanding their planned giving programs. Planned gifts often represent donors' largest and most impactful contributions, providing a valuable means tor nonprofits to diversify their revenue streams. Given the ongoing transfer of wealth in the U.S., it is crucial for nonprofits to adapt their planned giving options to the evolving market landscape. Moreover, I have observed that planned giving can serve as a catalyst for building an endowment or quasi endowment, necessitating a well-defined strategic endowment plan. Some nonprofits have even introduced legacy challenge programs to inspire legacy giving. Additionally, it is worth noting that the SECURE ACT 2.0 has introduced additional planned giving benefits for donors."*

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Virtual sessions have enabled some nonprofits to expand their geographical reach and donor base.

Observations

We continue to meet with many nonprofit organizations that are focused on starting or building out their planned giving programs. Bequests, which typically represent 80% of all planned gifts during the year, are a key area for planned giving expansion (https://www.networkforgood.com/resource/4-simple-steps-to-build-a-bequest). Other focus strategies have been appreciated securities, the Individual Retirement Account (IRA) rollover, retirement plan designations, and donor advised funds. Some nonprofits observed a greater interest in planned giving during COVID-19 as donors reassessed their estate plans.

Many nonprofits have also viewed planned giving as a way to grow their endowment funds and quasi endowments; unrestricted planned gifts are an important way to add to these investment funds. We have observed a number of smaller nonprofits starting quasi endowments as a result of a large unrestricted gift from donor Mackenzie Scott. We have seen interest in developing a strategic endowment plan, which is a way for a nonprofit to memorialize its endowment growth plans. We wrote about the strategic endowment plan in our latest research report: *Independent Schools Revisited*.

Some clients have taken advantage of our custom peer reviews to enhance their planned giving websites. Several have added language related to the recent SECURE ACT 2.0 options around IRAs and Qualified Charitable Distributions (QCDs) to their websites. One included an article, *Create a Charitable Gift Annuity: If you are 70 1/2 or older, you can now use your IRA to create a gift that pays you. Get fixed, reliable income for life by making a one-time election for a qualified charitable distribution up to $50,000 to fund a CGA*.

We have also seen some clients enhance their fundraising planned giving pages by adding the IRA rollover, designations, and donor advised funds, which can be viewed as a planned gift. Some nonprofits need to refine the benefits of being a member of their legacy programs.

Technology strategies may remain crucial as we move into the post-COVID period

Nonprofits continued to enhance their technology plans over the past decade and have incorporated these ideas into their overall fundraising strategy. This includes donor databases, automatic gift processing, online giving, recurring giving, surveys, analytics, donor emails, website development, virtual events, social media, and peer-to-peer fundraising options, just to name a few. COVID highlighted the importance of having these capabilities and having a comprehensive technology plan. As part of their plan, a number of nonprofits are taking advantage of the Guidestar Transparency Seals.

During COVID, many nonprofits changed their major gifts approach to virtual discussions, which allowed them to still meet key donors "face to face." These virtual sessions have enabled some nonprofits to expand their geographical reach and donor base. Fundraisers have pivoted back to a combination of face-to-face

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and virtual meetings in our new world. Nonprofits are also focused on their online recurring giving programs as a way to retain new donors that came on board during COVID. Some recurring giving pages have become more flexible by offering multiple donation options.

Observations

Peter Hoskow, senior partner at CCS Fundraising, shares his observations on the importance of technology:

> *"The pandemic and the following months expedited organizations' need to adopt new technologies to engage with their constituencies in a virtual world. As we near the mid-point of 2023, we are seeing many nonprofits adopting these platforms and novel approaches as part of their standard repertoire for engagement. In a recent CCS survey of nearly 1,200 nonprofit organizations, respondents cited that they continue to employ pandemic-era operational adjustments such as digital giving, enhanced personalized communications, and increased social media presence.*
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> *As we consider the future of technology and philanthropy, we know that organizations are acutely aware that online and mobile giving is a critical component of their fundraising strategy. There are also opportunities for leaders to use technology, specifically Artificial Intelligence—machine learning and Generative AI both. Machine learning helps with predicting the giving likelihood and segmentation of donor databases, and Generative AI helps generate letters, emails, social media posts, graphics, and beyond. With additional automation, these tools can optimize and maximize sometimes scarce resources across an organization and allow staff to focus on meaningful work, like engaging with donors. For example, organizations can use predictive modeling and Generative AI to create personalized communication by which every donor feels seen.*
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> *With that said, while technology has opened new avenues for engagement, evergreen fundraising best practices do still apply: meet your donors where they are, and make it easy for them to give."*

According to software provider Blackbaud, for 2021, online giving grew by nearly 9% in 2020 after a review of 4,964 organizations. While online fundraising is growing quickly, Blackbaud estimates that it comprises only 12% of the total fundraising in the U.S. and was at 13% for 2020. Approximately 40% of online giving happened in the last three months of 2021 (Source: https://institute.blackbaud.com/charitable-giving-report/).

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Our Wilmington Trust, N.A., New York-based Endowments and Foundations Team assists nonprofit organizations throughout the Northeast region and nationally in meeting their investment and philanthropic objectives.

Please do not hesitate to contact Walter for more information.

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Endowments & Foundations Best Practices Check List:

Top Ten

1. Do you have adequate liquidity? Is your line of credit competitive?
2. Have you completed a portfolio annual stress test?
3. Are you getting competitive returns for your short-term funds?
4. Is there a windfall policy for unrestricted planned giving donations to build a quasi endowment?
5. Have you conducted a peer review to compare your planned giving site? Are bequests spelled out clearly?
6. Does your Legacy Society offer some key benefits to members? Do you list your members?
7. Are you set up for donor advised fund donations?
8. Do you offer flexible recurring giving options?
9. Have you earned a Guidestar Transparency Seal and is it posted on your site?
10. Have you built a strategic endowment plan for future growth?

A final word

We continue to observe that the most successful nonprofits take a holistic approach to their growth strategies, in that the focus is on both fundraising and investment performance to grow their endowments. We call this a strategic endowment plan (SEP). These strategies can help a foundation expand for the long term, despite how the world evolves.

