

QUICK POLL

Outlook 2010: How Nonprofits Are Responding to Investment Challenges

The **Nonprofit Management Research Panel** recently conducted a Quick Poll of nonprofit executives and investment committee members responsible for overseeing endowments and foundations. The poll was conducted in December 2009 and was completed by 103 executives overseeing asset pools ranging in size from US \$25 million to more than \$1 billion. None of the participating organizations were institutional clients of SEI. The key findings are summarized in this report.

Traditionally, nonprofits have been the pioneers among institutional investors when it came to investing in alternative investments. Alternatives have been viewed as a way to diversify the portfolio's return enhancement, but have also presented risks to the overall liquidity of the portfolio. As 2009 ended, many nonprofit investment committees were addressing the challenges that resulted from the impact recent events had on the alternative markets. Furthermore, committees are currently evaluating the entire investment management process and whether or not it addresses the organization's needs.

This poll looked into the current investment management practices of nonprofits, the challenges they are facing and how these organizations are prioritizing and addressing these concerns heading into 2010.

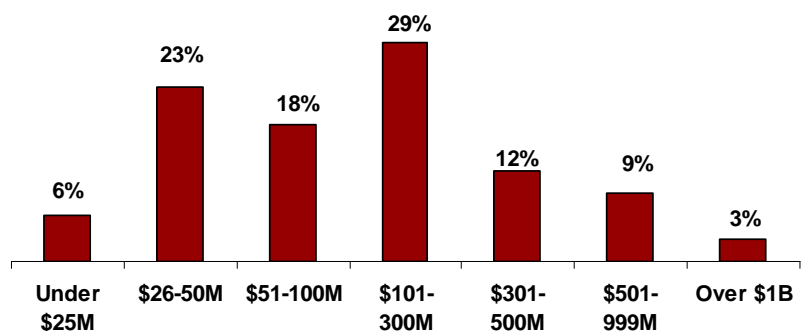
SECTION I – CURRENT STATUS

Organizations Polled

Depending on the type and size of the organization, the challenges can differ greatly. Below are breakdowns of participating organizations based on the type of organization and by size of asset pool:

- 43% educational institutions
- 16% private foundations
- 11% community foundations
- 9% social services
- 9% hospital or healthcare system
- 6% cultural or arts
- 4% faith-based organizations
- 2% health and human services

Respondents by Size of Asset Pools



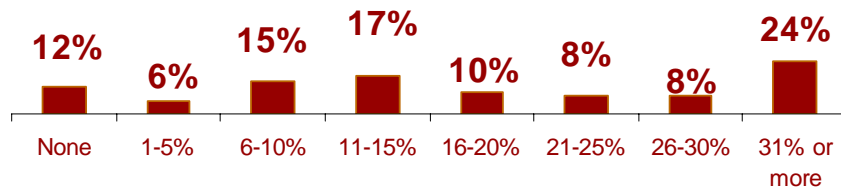
High allocations to alternatives

Nonprofits have traditionally invested significantly in alternatives and the poll results show that allocations remain high:

- Two-thirds of those polled (67 percent) have at least 11 percent of the portfolio invested in alternatives
- 40 percent of those polled said the organization has at least 20 percent of the portfolio in alternatives
- Almost one-quarter (24 percent) of those polled invest 31 percent or more of the portfolio in alternatives

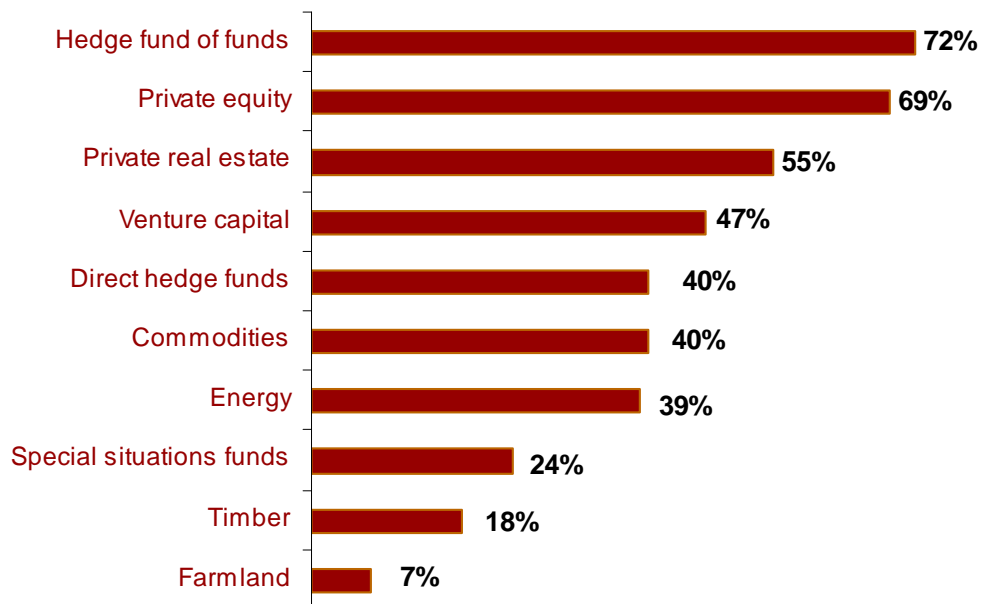
FAST FACT:
Nearly nine out of ten (88 percent) nonprofits in the poll have endowment or foundation assets invested in alternatives

What percentage of the organization's portfolio is currently invested in alternatives?



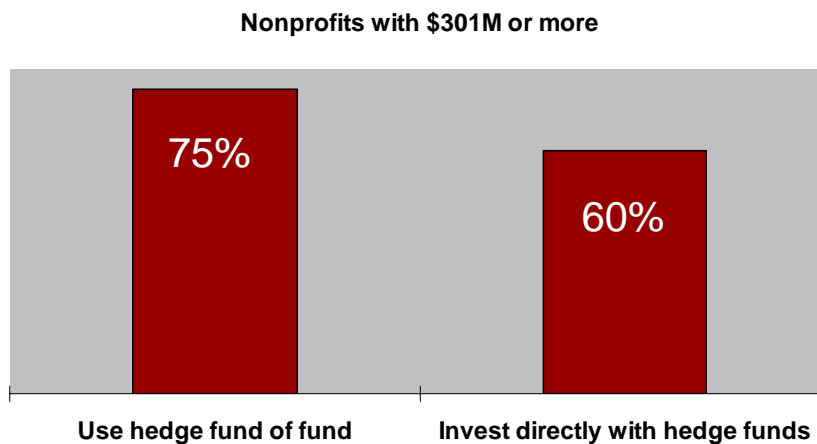
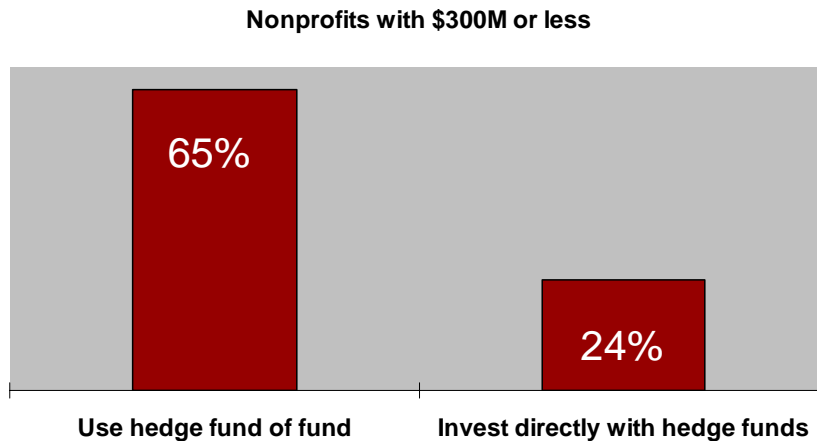
As would be expected, the smaller endowments had a lower allocation to alternatives. Nearly half (42 percent) of those polled with less than \$300 million in assets had 10 percent or less of the portfolio allocated to alternatives. By comparison, only 4 percent of those with more than \$300 million in assets had 10 percent or less invested in alternatives.

Here is a breakdown of which alternatives are currently being used by poll participants:



Hedge fund investing

Nearly three quarters of those polled (72 percent) currently invest in a hedge fund of funds while less than half (40 percent) invest directly with hedge funds. This is likely due to the fact that the size of the organization's portfolio can influence the overall hedge fund strategy due to manager minimums. The poll results below suggest that institutions with over \$300 million in assets are more likely than those with less than \$300 million to invest directly with individual hedge fund managers.



Current Approach to Investment Management

Poll participants were asked to identify the organization's current approach to the investment management of assets:

- 70 percent said the investment committee uses a consultant but has internal resources focusing on manager selection and change decisions
- 21 percent said the investment committee outsources all manager decisions to an external fiduciary partner such as a Manager of Managers
- 9 percent said the investment committee does not use any outside investment consultants or advisors and handles all investment decisions internally

FAST FACT:

More than half (53 percent) of all respondents said the organization prefers active investment management instead of passive or indexing

SECTION II – CHALLENGES AND CONCERNS FOR NONPROFITS

Nonprofits Identifying Organizational Priorities

From an investment management perspective nonprofit endowments and foundations are prioritizing their focus areas. The most common issue identified as a priority by 98 percent of the poll participants was “maintaining liquidity across the portfolio.” Similarly, 96 percent of respondents said “inflation protection” was a priority.

While inflation protection and maintaining portfolio liquidity were identified as priorities by most respondents, it is interesting to understand to what degree they define the importance of those priorities. Participants were asked to define priorities as either “marginal,” “high” or “extremely high.” Below is a chart showing the percentage for each:

	Marginal Priority	High Priority	Extremely High Priority
Inflation protection	38%	52%	6%
Maintaining liquidity across portfolio	43%	41%	14%
Defining fiduciary responsibilities for trustees and investment consultant	34%	35%	15%
Immunizing short-term cash portion of portfolio	42%	27%	7%

Investment Committees Concerned About Fiduciary Roles and Responsibilities

Investment committee roles and responsibilities are unquestionably complex and can vary from one organization to another. The investment downturn of late 2008 and early 2009 left many investment committees questioning the advice of their consultants. Further complicating matters in early 2009 were highly publicized events where nonprofits invested with fraudulent money managers, resulting in uncertainty around who is responsible for the decision to put money with these managers.

Now, there appears to be some questioning around how much fiduciary accountability the consultants own. The events of 2008 and 2009 have clearly had a lasting impact on nonprofit investment committees. As the chart above shows, “defining fiduciary responsibilities for trustees and investment consultants” had the greatest percentage of respondents to rate it as an “extremely high priority.”

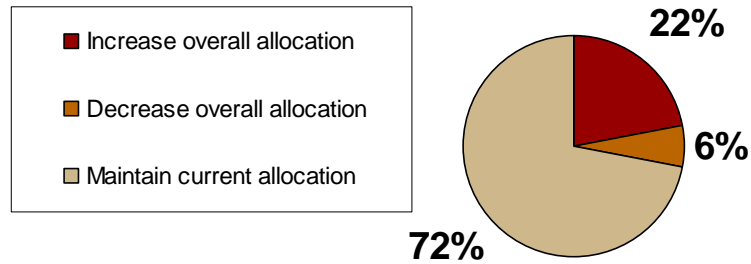
FAST FACTS:

- *24 percent of those polled said the investment committee is concerned about the resources required to perform the necessary due diligence around investment managers moving forward*
- *87 percent of those polled said the organization is no longer experiencing a significant increase in the cost of borrowing.*

SECTION III – HOW NONPROFITS ARE RESPONDING

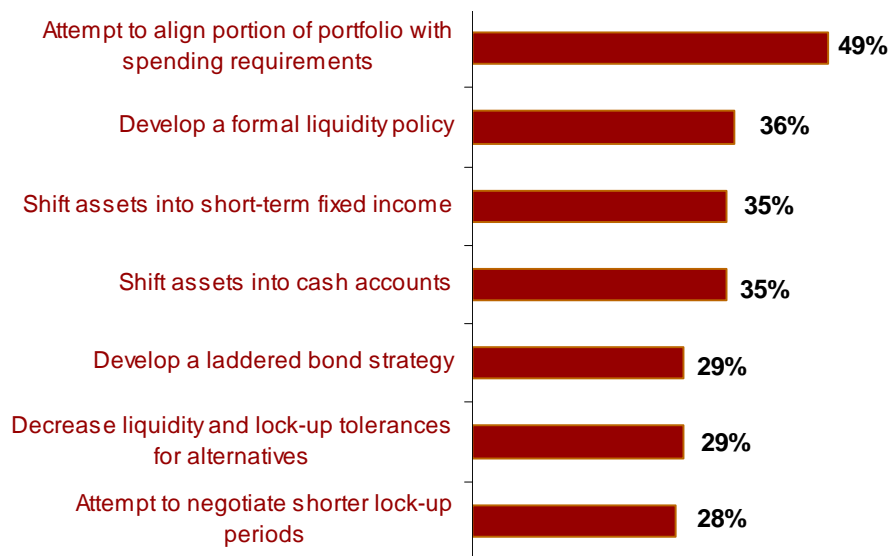
While most of the nonprofits in this poll plan to maintain the portfolio's current allocation to alternatives, nearly a quarter of the poll participants are planning to increase from their current allocation within the next six months:

When it comes to investing in alternatives, which of the following actions is your organization most likely going to take in the next six months?



Addressing Liquidity Concerns

Poll participants were asked which actions they've either already taken or are considering taking when it comes to addressing liquidity concerns:



FAST FACTS:

- 40% said the organization has increased the overall percentage of assets in cash reserves
- More than a quarter (26%) said the organization is looking to develop an asset allocation more aligned with the levels of flexibility in their spending policies

Considering Changing Traditional Consultant Approach

One-third (33 percent) of those polled said the recent market downturn has caused the organization to consider a different approach for investment management. While nearly three-quarters (70 percent) said the investment committee currently uses a consultant, 40 percent of that group said they plan on evaluating the consultant or investment advisor relationship within the next two years.

FAST FACT:
Almost two-thirds (60%) of those nonprofits using an investment consultant have not changed that consultant in more than five years

Conclusion

Despite an improvement in the performance of capital markets over the year 2009, for many nonprofits the market volatility over the past two years has resulted in an increased focus on addressing liquidity when making asset allocation decisions for alternative investments. The poll results show a continued interest in alternatives among nonprofits however the results also suggest an emphasis on addressing liquidity needs, concerns around fiduciary responsibilities and overall evaluation of the complete investment management process.

Moving forward, interest in alternative investing appears to remain high among this group. As the poll indicates, in 2010 nonprofits appear to be focused on aligning alternative investment decisions with the short-to-mid term spending needs of the organization. Additionally, organizations will be spending time evaluating their current consultant or advisor and considering the best approach moving forward for fulfilling fiduciary obligations.



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